

POLITICAL ECONOMY OF THIRD WORLD BILATERALISM:
THE SAUDI ARABIAN - KOREAN
CONNECTION 1973-1983

by
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ABSTRACT

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The 1970s have witnessed a rapid change in the international economic system. One of the salient aspects of this change has been the rise of OPEC members and the Newly Industrializing Countries as significant actors on the international economic scene. Aware of the importance of these new actors, a growing number of scholars in the field have paid their scholarly attention to this new phenomenon. Nevertheless, little effort has been applied to the systematic understanding of significant economic interactions among these new actors.

This study represents an effort to understand this new phenomenon within the overall framework of international political economy. In carrying out this research task, the study constructs a pre-theoretical model of intra-South bilateral economic relations, and applies it to the bilateral ties between Saudi Arabia and Korea from 1973 to 1983.

The findings of this study offer a number of counter-intuitive examples to the conventional wisdoms of international political economy. First, the study shows that developing countries are inclined to seek bilateral ties, rather than relying on collective multilateral schemes, in coping with sensitivities and vulnerabilities resulting from their integration in the international division of labor. A second finding is that the rise of Third World bilateralism is a function of a conscious and calculated state strategy to diversify external dependence and to reduce systemic vulnerabilities rather than the outcome either of spontaneous market forces or of developing countries' structural positions in the international economic system. This finding suggests that the state, even in 'dependent' developing countries, must be restored as the primary unit of analysis in understanding political economic behavior of Third World countries. Third, this study identifies the role of private entrepreneurs in the Third World as an important unit in tracing process-level dynamics of intra-South bilateralism. Finally, the findings in this research suggest that development strategy can be a useful starting point in analyzing political economic behavior of developing countries in general and the formation of Third World bilateralism in particular.

DEDICATION

TO MY PARENTS, YEO JUN KIM AND TAE SENG MOON
WHOSE DREAM HAS BEEN TO HAVE A GOOD SCHOLAR
AMONG THEIR FIVE SONS.

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CHAPTER ONE

INTRODUCTION: GLOBAL INTERDEPENDENCE AND THIRD WORLD BILATERALISM

Introduction

Bilateral economic relations among developing countries are not a new phenomenon. Although relatively minor compared to relations between the North and South as a whole, they remain a persistent pattern of economic transactions affecting developing countries. Recently, these inter-South economic linkages have revealed a dynamic dimension with the rise of new significant actors from the Southern rim in the international economic system: OPEC and the Newly Industrializing Countries (NICs).

The capital-surplus OPEC members and the NICs have shown remarkable upward mobility in the system with their increased economic capability in terms of diversified industrial structures, growing purchasing power, and entrepreneurial dynamism. The entry of these countries into the international system dramatically reactivated bilateral economic linkages among developing countries by providing new markets, increasing industrial complementarities, and by creating new incentives for mutual cooperation in the mid-1970s and after. It is difficult to predict whether or not this phenomenon will

become a solid and stable modus operandi commonly pursued by developing countries. Over the last ten years, however, inter-South bilateral economic transactions have become significant in both relative and absolute terms. As shall be discussed in chapter one, the magnitude of inter-South dyadic transactions measured by amount, volume and pervasiveness constitute an important dimension of the international political economy.

Earlier theories advanced under the rubric of interdependence and dependency -the mainstream of the international political economy- have, however, distorted' this dimension by omitting it from their analytical and empirical universe. This may be partially due to their intentional neglect of the phenomenon based on theorists' shared perception of empirical insignificance , or their theoretical inability to capture it properly. Or it may have something to do with normative positions: interdependence theorists may fear entropic fragmentation of the world by uncoordinated bilateral search for economic gain, while dependencia theorists may deny the possibility of economic gain by unilateral or bilateral actions due to systemic weakness, domestic fragility, and the economic backwardness of developing countries. Whatever the reasons, the fact is that these dyadic inter-South transactions are growing.

This study is an attempt to explore this 'ignored' or 'distorted' dimension of the international economy. The

study is guided by the three major theoretical and practical assertions. First, it asserts that collective-multilateral approaches are not the 'only' solution to the current North-South economic stalemate. Disappointed with empty rhetoric, stagnant negotiations, and the uncertain outcome of collective-multilateral approaches, developing countries tend to opt for bilateral ties or diversification in terms of explicit and/or implicit cooperative arrangements.

Second, the study argues that the rise and permanence of Third World bilateralism is a function of a 'conscious' and 'calculated' state strategy to diversify external dependence and to reduce systemic vulnerabilities, both of which are the unavoidable by-products of integration into the international economic system. This position therefore rejects the conventional understanding that the volume and direction of economic transactions between any dyadic pair is "totally" determined either by changing patterns of comparative advantage in the international economy or by systemic constraints and opportunities stemming from structural positions in the international division of labor.

It does not, however, imply an entire negation of the changing pattern of comparative advantage and systemic constraints and opportunities as factors affecting the direction and volume of bilateral ties. These are certainly responsible for the rise of bilateralism, but not in a deterministic manner. In my opinion, they are

conditioning factors to be perceived, filtered, and translated into the decision-making context of the state authorities in such a way to yield specific forms of bilateralism in terms of partner and commodity diversification.

Third, as a corollary of the second assertion, the study makes foreign economic policy-making in particular and the role of the state in general the primary unit of analysis. In other words, state behavior in terms of foreign economic policy-making is conceived as the crucial variable explaining the rise and growth of Third World bilateralism. It is deduced from this line of reasoning that "the state" in developing countries is neither obsolete conceding its power to market forces, nor helplessly trapped in a dependent relationship with the capitalist system. The assertion of an "autonomous" state as the primary agent shaping the volume and direction of Third World bilateralism in turn necessitates an examination of the nature of "the state", domestic political structures, dynamic interplay of "state and business", and of the structure and process of foreign economic policy making in those countries involved in dyadic transactions.

With these issues in mind, this study seeks to address the following set of questions;

- 1) How extensive have bilateral economic ties between developing countries been for the last two decades? What factors are responsible for the rise and expansion of these bilateral ties? What has been the nature of gain from this

bilateralism? And how does this bilateral phenomenon fit into a larger framework of the international political economy?

2) What factors inhibit or enhance bilateral ties between developing countries? What is the nature of dynamic patterns of interactions involving these bilateral ties? What are the salient forms of cooperation and conflict revolving around the inter-South economic linkages? What are the patterns of diplomacy, bargaining, issue-linkages, market penetration and receptivity, and the decision structures of this form of economic relations?

3) What practical policy implications can be deduced from such a study? What effects does this form of economic relations have on the order and stability of the international economic system? What about their permanence and pervasiveness? What sorts of theoretical lessons can be learned from this study?

In addressing these sets of questions, the study employs two strategies: one is the construction of a framework of analysis that can explain Third World bilateralism, and the other is a case study. As discussed in Chapter Two, the construction of a framework of analysis is motivated largely by the inadequacy or low theoretical utility of existing theories or approaches in explaining inter-South dyadic relations. The case study has been chosen not only because of the concentration of the phenomenon in quite a limited number of developing countries such as OPEC and

NICs, but also because of the researcher's preference to examine the issue on a basic level. The case in question concerns bilateral economic relations between Saudi Arabia and South Korea over the last decade. The Saudi-Korean case has been chosen with an expectation that it may provide us with a strong counter-example to the existing theoretical trend in the field of international political economy. Thus, the study does not attempt to generalize a theory of bilateralism from this particular case. The research simply aims at delineating a solid empirical case which has been neglected in the mainstream analysis, offering 'a' proof for the framework of analysis posited, and opening a new horizon of research area for Third World students of the international political economy.

Global Interdependence and The Third World

Over the last quarter of a century, the degree of interconnectedness among countries in the world has drastically increased. Through cob-web like networks of global communication, international trade, and human interactions, global interdependence has increased not only in terms of quantity (i.e., volume of transactions) but also in terms of quality (i.e., expansion of intricate policy networks). For example, international trade has expanded more rapidly than national economies have grown. Along with the expansion of the commodities market, international financial and labor markets have made

quantum leaps.¹ The expansion of the industrial world and the diffusion of the international market economy have integrated all parts of the globe into one increasingly interdependent whole, about which Gilpin has written: "National economies have become enmeshed in a web of economic interdependence from which they cannot easily escape." (1975:41)

The image of a global system, in which a profusion of transnational relations takes place, has been beneign and is seen as a positive sum game carefully nurtured by the market concept. As Koehane and Nye have noted: "rhetorical uses of 'interdependence' frequently carry highly positive and egalitarian overtones." (1975:367) Indeed interdependence has been adopted as a semantic symbol alleged to be composed of symmetry, equality, peace, integration, and modernization.² Thus, the higher the level of global interdependence, the higher the level of homogeneity and integration among different component parts of the global system.

This proposition has been buttressed by liberal ideology believed to be responsible for the economic order that emerged as the dominant logic of the global system after the World War II. After the economic chaos of the inter-War period and the devastation of much of the industrial world during the World War II, only the US was in a position to set the basic rules of the post-war game. The US choice was to structure such rules around on the liberal

economic order. The idea behind this liberal program was clear: toleration and/or institutional guarantees of free trade and the free movement of the factors of production would enhance global efficiency and welfare through increased consumption and expanded markets (Gilpin 1977 ; Kindlberger 1976 ; Hirsch and Doyle 1978; Caldwell 1976; Hudson 1979).

Following this logic, GATT (The General Agreement on Trades and Tariffs) was created to facilitate the lowering of national trade barriers, the IMF to set up an international monetary regime built on fixed and freely convertible rates among national currencies, and the World Bank established to provide for the international flow of capital to meet economic recovery and development needs that private investors were unable to support (Knorr 1977:1-2). Expanding international trade and investment in such a liberal institutional setting and the US hegemonic stability was seen as the most powerful engine for transforming backward and disrupted economies into national systems capable of self-sustained growth. Although this transformation was not pervasive, it greatly contributed to the post-war rise of West Germany and Japan.

This diffusion of global interdependence was not limited to the advanced industrial countries. Third World developing countries, numbering more than 130 today, have been integrated into the global economy either by choice or by historical necessity.³ The end of colonialism and the emergence of new, independent states brought new problems

to the fore. In their efforts to foster economic growth, the developing countries were faced with fundamental constraints: single crop economic structures, the lack of human and technological infrastructure, and persistent capital shortages. All of them were colonial legacies which impeded self-sustaining economic development. Under these circumstances, the costs of closing their economies were perceived to be prohibitively high. Thus, they opened up their economies in one way or another to further integrate into the international economic system going through a variety of development strategies from import-substituting industrialization, regional economic integration, and export promotion strategy.⁴ Perhaps, as in the words of Wolfgang F. Stolper, small developing countries "never really had a choice between open or closed economies, but only a choice of how open to be." (1966:59)

At this stage, the message from the developed world was clear: the more integrated you are into the system, the higher the level of your benefits. Early integrationists and modernization theorists all strongly advocated the opening up of societies and economies assuming an eventual⁵ conversion between the developed and developing world. More specifically, students of modernization theory conceived the modernization process as a grand, universally achievable, evolutionary and pervasive phenomenon applicable to all developing-traditional societies. Despite transitional disruptions and dysfunctionalities,

they believed that the modernization process would bring about prosperity and stability. To a number of liberal economists, increased market exchanges with developed economies would guarantee almost automatic and spontaneous transfer of benefits under the rubric of comparative advantage. They all argued that open economies contribute to the economic growth and welfare of developing countries.⁶

The degree of integration into the global economic system varies from one country to next, depending on the types of development strategy pursued. Countries with an outward-looking orientation integrate more deeply than those operating under inward-looking strategies. This integration process has brought new benefits and opportunities to developing countries in varying degrees. Through the global network of market mechanism, scarce goods, services, and capital flowed in, while external markets for primary commodities and manufactured goods originating from developing countries expanded. New technologies were introduced, contributing to the industrialization process in some developing countries. Indeed in the absolute sense, economic performances in many developing countries, measured by growth rates and industrial productivity, substantially improved as a result⁷ of positive integration into the international economy.

Notwithstanding these actual and perceived benefits and opportunities, however, a growing number of observers began⁸ to pay attention to the other side of coin, arguing that

the optimistic visions of the modernists, transactionists, integrationists, and liberal economists have not dovetailed with reality. On balance, it is argued, costs and constraints have been far greater than benefits and opportunities. These negative aspects are in turn attributed to a pattern of unequal exchange under an asymmetric structure of global interdependence. Rosenau, for example, perceives that the world evolving out of increased interdependence is not necessarily that of "tidy symmetry", but of "ungainly asymmetry"(1980:53). Contrary to the market analogy adduced by the liberal theorists, the structure and process of the interdependent world were not symmetric, neutral, and optimal. It involves "varying degrees of interdependence for some and of dependence for others."(Waltz 1979:143) Certainly increased interdependence has led to more collaboration, mutual knowledge, and benefits for some. But it has also led to dependency, vulnerability, exploitation, and conflict for others(Holsti 1980: 31).

Interdependence is then a Janus-like attribute of the contemporary international system. It offers to developing countries both costs-constraints and benefits-opportunities. But the crux of the issue seems to lie in the impression that the former outweighs the latter. The level of costs and constraints are not uniformly generalizable for all the developing countries. Depending upon each actor's power capability, issue-area, patterns of

development strategy, and structural position in the international system, the level of costs and risks varies from one country to another(Koehane and Nye 1977 ; Burns and Baumgartner 1977;Christensen 1977;Baldwin 1979, 1980; Haggard 1983). The growing stratification and heterogeneity of most developing countries further prevents us from coming up with common denominators for costs and risks originating from the pattern of integration into the global system. Nevertheless, it seems possible to delineate such costs and risks in terms of three major factors: systemic vulnerability, dyadic sensitivity, and structural dysfunctionality.¹⁰

One of the most obvious costs and constraints faced by developing countries is systemic vulnerability. The concept refers to the pattern of costs or constraints imposed by the transmission of external shocks and turbulence originating in the international system. Vulnerability of this sort is related to the external economic environment as a whole, rather than to specific actions of specific actors. Wide swings in world market conditions, boom and bust cycles, international financial uncertainties, protracted global recessions, roller-coaster pricing patterns of primary commodities and the like are good examples of the sources of this kind of vulnerability, all of which are the cumulative result of the movements of systemic factors. As Koehane and Nye point out, the extent of this vulnerability is usually contingent upon "the relative availability and costliness of the

alternatives that various actors face." (1977:13) Due to their highly unpredictable and undifferentiated nature, however, the costs incurred are very high even after the policies are altered.¹¹ In many cases they are not easily captured within the existing or altered policy framework, often leading to incapacitation of the state to make policy. The recent polemics over "conditionalities" imposed by international lending institutions for structural adjustment and stabilization demonstrate this point.¹²

The degree and extent of systemic vulnerability is largely a function of the pattern of integration into the world capitalist system. The more integrated into the system, the higher the level of vulnerability. For example, a country pursuing an export promotion strategy with external financing is more likely to subject to this kind of vulnerability.¹³ However, countries adopting an inward-looking strategy are not immune from this kind of vulnerability either. High import costs of capital and intermediate goods, global financial insecurities, and instability of export earnings, all of whose origin is systemic, impose a varying degree of costs and constraints on these countries. Usually the 'backwash effects' accompanying this sort of vulnerability are quite devastating to developing countries (Heilleiner 1976). Income and economic stability are negatively affected. Growth slows down. Inflation combined with unemployment

seriously affects people's welfare. Moreover it threatens economic sovereignty by limiting or constraining a country's "power to control a full range of policy instruments" (Holsen and Waelboeck 1976: 11).

While systemic vulnerability is caused by the synergistic effect of the attributes of the system over which the individual component parts have little influence, dyadic sensitivity primarily refers to the costs and constraints imposed by a pattern of external reliance in terms of specific actors and issue areas.¹⁴ A pattern of external reliance in the context of interdependence can be meaningfully understood at the dyadic level because it involves mutual dependence by choice (Caporaso 1978:2). Since the level of liability to costly effects imposed by this type of external reliance can be reduced or changed after the alteration of policies (or withdrawal of mutual dependence), the costs or constraints therefrom are 'sensitive' in the sense that they can be by and large captured or coped with by the deployment of a set of deliberate policies (Keohane and Nye 1977:13). This dyadic sensitivity is a common attribute of any exchange relationship. But the problem germane to developing countries arises from the fact that their dyadic dependence on developed countries is characterized by unequal power¹⁵ relations and disadvantageous outcomes therefrom.

In this regard, Hirschman (1978, 1980), questioning the thesis of 'mutually beneficial trade', traces a set of costs involved in this trade relationship. According to

him, exchanges between small and large states are accompanied by problems of influence, dependence, and domination. Any small country's gain from trade with a large country entails its dependence on the country bestowing it. This dependent relationship enhances the large country's leverage to control and manipulate the small countries' external economic behavior as can be seen in the case of the relationship between Nazi Germany and its neighboring countries in the 1930s. Taking advantage of a small country's dependence, a large country may deploy various means to maximize its economic and/or political interests such as the sudden interruption of commercial or financial relations and the imposition of discriminatory policies. Expanding Hirschman's insight, there could be many other costs that emanate from this dyadic sensitivity: bilateral protectionism, positive and negative economic sanctions, denial of supply, markets, capital, aid, technology, etc..

While Hirschman looks at the costs of mutual dependence through the prism of unequal power relations, another group of scholars has examined the problem of dyadic sensitivity in terms of the structure of unequal exchange shaped by the historical pattern of bilateral transactions (Burns and Baumgartner 1977 ; Singer 1964 ; Prebisch 1979 ; Emmanuel 1971). Hans Singer, for example, argues that the loss of spread or linkage effects of specialization leads to unequal exchange patterns between a dyadic pair of

developed and developing countries, which limits scope for technological progress or for economies of scale. The major reason behind this unequal exchange is a high rate of profit repatriation from developing countries' private sector by foreign investors(1964:165). In other words, the type of foreign investment and historical pattern of technological progress often drive developing countries to put all their emphasis on a single sector, usually a primary commodity sector, resulting in a high level of dyadic dependence and sensitivity. In a similar vein, Prebisch(1956, 1970) asserts that deteriorating terms of trade are a primary cause for unequal exchange leading to dyadic sensitivity. On the other hand, Emmanuel(1971) calculates the costs of unequal exchange in terms of wage differentials between developing and developed countries. According to him, the price of capital is relatively constant between countries because of its high mobility and similar rate of profit return. In most cases, however, the mobility of labor is restricted by geographic jurisdiction. Differences in the price of goods are thus determined by wage differentials in such a manner that developed countries produce higher priced goods, while developing countries produce lower priced goods. The immediate result of this unequal exchange is diminished income and decreased welfare for workers in developing countries.

The common thrust of these arguments is that the gains from external economic relations are relationally or

structurally biased in such a way that they are nullified or traded-off by the accompanying dyadic sensitivity . This posed persistent problems for most developing countries for decades particularly because of the higher level of partner and commodity concentration. In 1977, for example, almost 50% of the developing countries relied on one or two primary commodities in their total exports while their trade partners were limited to a small number of developed countries (Pirages 1978: 232-5). Even in the case of the NICs where economic structure is relatively well diversified, partner and item concentration rate is quite high.¹⁶ But dyadic sensitivity is not limited to trade. It is applicable to a wide range of external economic transactions covering capital, technology, aid, and raw materials. In contrast to systemic vulnerability which involves a high level of undifferentiated and deterministic costs, dyadic sensitivity does not determine the fate of autonomy or freedom in policy choices. A deliberate policy choice with regards to effective bargaining and diversification in commodities and partners may improve the developing countries' position in dealing with this problem.

A third major cost of increased interdependence for developing countries is structural dysfunctionality. This refers to distortion or retardation of a country's political and economic structure.¹⁷ While the first two constraints may affect both developed and developing

countries, structural dysfunctionality is a constraint unique to dependent peripheral countries. It usually accompanies a "functional derrangement" or a "functional incompleteness" of developing economies by depriving their ontogenetic momentum of a 'big spurt' (Caporaso 1978: 23; Cardoso 1979:163). It is manifested in many different forms: 1) paralysing and distorting the domestic economic structure through uneven development across sectors of the economy, resulting in an enclave economy, 2) undermining self-sustaining or self-enforcing developmental possibilities by blocking a partial or total autonomy of developmental choices, 3) accelerating socio-economic inequality across sectors of the economy, and 4) other externalities such as deteriorating quality of life, pollution, and political repression (Amin 1974; Baran 1957; Baran and Sweezy 1966; Dos Santos 1970; Frank 1967, 1972, 1981; Magdoff 1969; Caporaso 1978; Palmer 1977).

While dyadic sensitivity is a constraint on the external behavior of developing countries largely generated by process-level dynamics between a dyadic pair, structural dysfunctionality is an internal outcome as well as a cause of asymmetric incorporation into the world capitalist system. The latter is shaped largely by the dynamic interplay of domestic social forces and the logic of world capitalist development. While the former creates immediate, visible, and negotiable constraints on the external behavior of developing countries, the latter poses subtle, enduring, and structural costs and constraints on the

internal and external capabilities of developing countries. This structural dysfunctionality is cultivated and nurtured¹⁸ in the context of dependency. That is, the historical and cumulative pattern of integration into the world capitalist system characterized by structural inequality in the distribution of opportunities or constraints conditions a peculiar form of domestic social relations and productive structure. The type of development strategy in this dependency context is largely determined and controlled by the nature of the alliance between domestic class structure and international capital. The most cited direct cause of structural dysfunctionality is foreign control of the means of production in terms of direct investment or indirect capital movement. In particular the expansion and penetration of multinational corporations into developing countries has been attributed to the deepening of structural dysfunctionality in terms of the vertical integration of their trade patterns, the creation of an enclave economy, external dependency-bound production patterns, the monopoly of technology, and other socio-political impacts (Bierstekar 1978; Modelski 1978; Hymer 1972; Barnett 1974; Senghaas 1975; Sunkel 1974).

Recently a revisionist argument has been put forth by a number of scholars who assert that increased interdependence does not necessarily bring about the deepening of structural dysfunctionality. Warren(1973; 1980), Cardoso and Faletto(1979) and Petras(1982) argue

that while the conventional pattern of integration into the international economic system entails such dysfunctionalities, growth and industrialization in the dependent context is still possible and have been achieved by a number of developing countries such as the NICs. Viewed from this perspective, early dependencia theories that understood the 'development of underdevelopment' through a mechanistic and deterministic angle need to be modified. A possibility of dependent development in peripheral countries does not, however, totally eliminate¹⁹ the existing subtle costs of interdependence. To quote a well cited phrase from Cardoso:

Lacking 'autonomous technology'-as vulgar parlance has it- and compelled therefore to utilize imported technology, dependent capitalism is crippled... It is crippled because it lacks a fully developed capital goods sector. The accumulation, expansion, and self-realization of local capital requires and depends on a dynamic complement outside itself: it must insert itself into the circuit of international capitalism(1973:163).

By way of summarizing the nature of the costs and constraints, Table 1-1 offers a synoptic comparison of the three major constraints resulting from an increased global interdependence. Systemic vulnerability can be conceived as being an externally imposed cost or constraint of which duration is short or medium, yet produces intensive sector-specific impacts on national economies of developing countries. On the other hand, dyadic sensitivity is an external cost and constraint which can be meaningfully understood on a state actor or sector level. It accompanies immediate, differentiated impacts within a

short-medium term of which intensity is relatively moderate. The most crucial constraint is structural dysfunctionality which brings highly protracted and pervasive negative effects to politics and economies of developing countries and of which root causes are difficult to detect and to cure because of its subtlety.

Table 1-1: Costs of Interdependence:
Synoptic Comparison

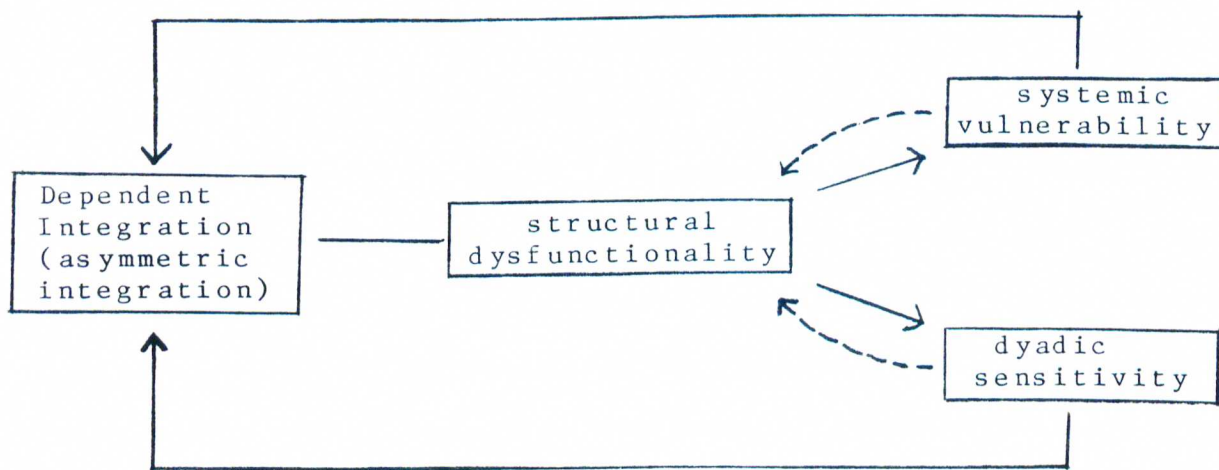
Type	Level	Determinant/ constraint	Nature/ duration	Intensity/ range(damage)
S.V	system/ sector	structural external	immediate undifferentiated short-medium	high/sector specific
D.S	state/ sector	relational external	immediate differentiated short-medium	low-medium sector-specific
S.D	system/ sector	structural internal	subtle differentiated long	high/ pervasive

S.V: systemic vulnerability, D.S: dyadic sensitivity,
S.D: structural dysfunctionality.

Of course, these three types of costs and constraints are neither mutually exclusive nor discrete. Rather they are causally interrelated, creating an interdependent whole of internal and external weaknesses. Diagram 1-1 indicates that structural dysfunctionality is the root cause as well

as the consequence of systemic vulnerability and dyadic sensitivity. It is the cause in the sense that a deformed productive structure and consequently limited developmental potential deepen systemic vulnerability by depriving the country of a defensive shield and endogenous resilience against external shocks. Furthermore it is responsible for dyadic sensitivity not only by weakening bargaining positions but also by reducing partner and item diversification capability in the bilateral context. At the same time, structural dysfunctionality is the end result of the first two constraints, given that their protracted prolongation(e.g., deteriorating terms of trade) and sporadic trauma of high magnitude(e.g., high interest rates and debt crisis or oil crisis) inhibit self-enforcing and self-sustaining

Diagram 1-1: Causal Sequencing of Dependent Integration



* Arrow indicates a positive causal relationship.

developmental possibilities by subjugating national economies to external forces. The causal sequence of these three constraints varies from one context to the next, depending on the historical experiences of the developing countries.

Facing this set of the costs and constraints, developing countries as a whole have pursued a wide range of strategies to curb such negative aspects of interdependence. A growing number of scholars have also shifted their attention from an analysis or diagnosis of these negative by-products to a search for a set of workable solutions. The following surveys a broad spectrum of strategies suggested or implemented by both policy-makers and scholars.

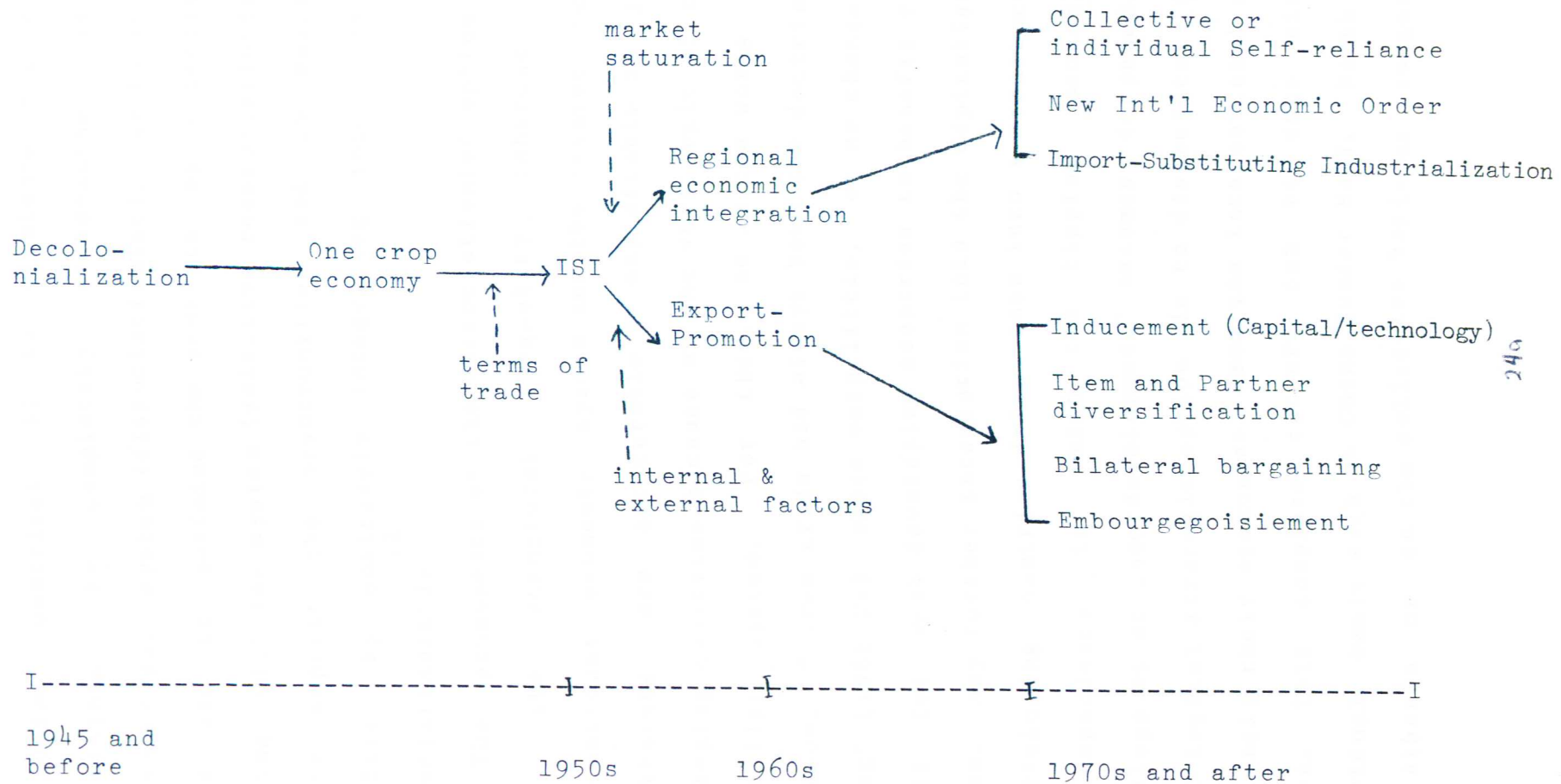
Third World's Countervailing Strategies

In contrast to the liberal view of the benign nature of increased global interdependence, others perceive outcomes as largely 'antinomical' in the sense that global interdependence has accompanied both benefits-²⁰ opportunities and costs-constraints simultaneously. This mixed blessing of global interdependence has stirred up a wide range of scholarly as well as policy debates on ways and means of maximizing benefit-opportunity and of minimizing cost-constraint. In particular various efforts have been made over the last three decades to come up with

countervailing strategies to reduce, eliminate, or avoid above mentioned systemic vulnerability, dyadic sensitivity and structural dysfunctionality. The list of suggested or implemented strategies for developing countries covers a broad range of policy options. As Diagram 1- 2 illustrates, scholars and policy-makers have come up with a number of strategy to overcome one crop economic structure and negative consequences of integration into the international economic system. Starting with import-substituting industrialization in the 1950s inspired by the Listian economic nationalism, developing countries have attempted to implement in chronological order such scholarly prescriptions as regional economic integration, collective bargaining through the proposal of the New International Economic Order, collective or individual self-reliance, and finally export promotion strategy.

Certainly the historical evolution of countervailing strategies can be regarded as being largely a function of trial and error. However, there has been a dominantly common theme in this evolutionary process. That is the heavy emphasis on systemic factors to which economic malaise is attributed and for which solutions are sought. Recent works by Diaz-Alejandro(1978), Wriggins(1978), Hansen(1979), Krasner(1981), and Inoguchi(1981), which discuss the Third World strategies from a general and comparative perspective, well epitomize this common theme. By focusing on the form and degree of integration into the international economic system, they identify three

Diagram 1-2: Evolution of Development Strategy



dominant patterns of strategic choice available to developing countries: 1) to eliminate the costs and constraints by completely withdrawing from the international system (dissociationist), 2) to reduce the costs and to maximize the benefits by selectively re-linking with the system (selective reassociationist), and 3) to exploit the opportunities and to maximize the benefits by positively integrating into the system (associationist).

The proponents of the dissociationist option believe that the structural inequality inherent in the international economic system and the related costs and constraints are not curable or exploitable in favor of developing countries because of the very logic of the world capitalist system. For them, as in the words of Joan Robinson, "free trade had always been the doctrine of the strong" (1966:24) where very little, or no chance at all exists for weak developing countries to benefit from the system. Any further integration into the capitalist system by developing countries drives them into a structural trap of dependency in which the tipping mechanism of 'development of underdevelopment' becomes deepened. Thus, their logical strategic option is to dissociate (de-link) completely their economies from the international economic system. This complete cut-off can be done either on individual basis such as China (under Mao), North Korea, and Albania or on the collective basis as suggested by

As illustrated in table 1-2, the dissociationist strategy comprises a wide range of tactical policy choices. To eliminate structural dysfunctionalities deriving from integration into the system, it emphasizes a self-reliant or autocentric development orientation where the priority is placed on balanced and equitable growth with the satisfaction of the basic needs of the majority of the population.²⁴ This policy orientation involves nationalization of foreign direct investments, elimination of the domestic comprador class, and other necessary measures to ensure the complete insulation of the national economy from the international economic system. The self-reliant autocentric development may be pursued unilaterally or collectively among developing countries within a certain region or among all the developing countries.

Table 1-2: Strategies under 'Dissociation'

	unilateral	bilateral	multilateral
* S.D	autocentric / basic needs / nationalization		collective self-reliance
D.S	closed economic regime	inter-South economic arrangement /barter	intra-South sectorial cooperation
S.V.	default / market- withdrawal	inter-South coordination	regime-negation /collective coordination

*S.D.: Structural dysfunctionality, D.S.: Dyadic sensitivity,
S.V.: Systemic vulnerability

To cope with dyadic sensitivity, this strategy calls for closed trade regime and proposes to promote bilateral trade, financial and technological ties with other developing countries in terms of barter arrangements or sectorial based collective cooperation among them, depending upon the type of developmental strategy(individual or collective) in use. Under such conditions (of dissociation), systemic vulnerability can not take place. However, in the initial stage of dissociation, countries pursuing this option may default on any outstanding external financial obligation, withdraw from external market transactions unilaterally or choose bilateral or collective coordination and bargaining options with other developing countries to minimize the opportunity costs of de-linking on the systemic level (Frank 1981,1968, 1972; Senghaas 1981; Galtung 1978; Hveem 1978; Haq 1977; Chichilinsky 1979; Wallerstein 1979; Amin 1974; Arrighi 1974).

While the dissociationists emphasize the zero-sum nature of the present international economic system and propose a complete cut-off from such a highly unfair game, selective reassociationists conceive of the costs and benefits of integration into international markets from a slightly different perspective. They see the virtues and opportunities emanating from the market as a means of exchange for developing countries if certain preconditions are met. That is, if developing countries can avoid or overcome negative side-effects by partially managing

market forces or by limiting undesirable spill-over effects of the international links on the domestic economy and polity, integration into the world market may be turned into a positive sum game. Diaz-Alejandro, an advocate of this approach, explains the utility of selective reassociationism in the following way:

International link may be useful to help the country achieve some developmental targets under some conditions and specific historical circumstances, but it is fatal to regard openness as a good thing per se and to let external links and foreign demand determine the direction and the pace of the country's economic growth (1978:110).

Implicit in reassociationist strategy is the realization that it is too costly for small and economically backward countries to close off their economies from the international economic system. Yet it is also equally devastating to open their economies completely to international market forces whose exchange structure is biased against the weak and fragile developing countries. The choice lies somewhere in the middle. Domestic re-adjustment and effective alteration of linking or de-linking policies, depending on the changing nature of the country's historical circumstance and the international market, must proceed in such a manner that the costs of re-linking are substantially minimized and that re-arranged link to the international system enhances self-sustaining economic development.

Table 1-3: Strategies under 'Selective Reassociation'

	unilateral	bilateral	multilateral
S.D.	inward-looking /balanced/ basic need		
D.S.	industrial diversification/	partner-diversi- fication/inter- bargaining	regional- integration cartel
S.V.	stabilization/ default/partial withdrawal	bargaining / selective choice/ diversification	collective regime change (NIEO)

Table 1-3 illustrates some of the tactics to be used by developing countries in the reassociationist model. To reduce any domestic economic and political distortion caused by structural dysfunctionality, the reassociationists choose an inward-looking policy option. The inward-oriented development strategy is in principle designed to locate the engine of growth in the national economy, not subject to external forces. As a result, it aims at promoting balanced growth across all the sectors of the economy and enhancing the satisfaction of basic needs of people.²⁶ This inward-looking policy orientation comprises a number of strategies to curb dyadic sensitivity and systemic vulnerability.

To reduce external dependence, the reassociationists encourage a diversification of export commodities through industrial restructuring and infant industry protection and

attempt to ensure domestic market expansion through a provision of various protectionist measures.²⁷ On the bilateral basis, they try to diversify their trade, financial and technological partners so as to minimize dyadic dependence. In addition, they seek a number of policy options to enhance their bargaining position over their dominant economic partners in various issue areas. Bilateral diversification under the reassociationist strategy is usually directed toward the small non-hegemonic capitalist trading countries or toward other developing countries. But since most developing countries are weak in terms of international power relations and domestic economic structure, the capability to diversify their partners and commodities and to increase their bargaining power as a means of reducing dyadic sensitivity is limited (Krasner 1981; Diaz-Alejandro 1978; Hansen 1979; Singer 1979).

In face of this weakness, most reassociationists opt for regional economic integration and/or collective action such as producer cartel schemes. Regional integration schemes have been conceived as being a viable option since the pursuit of an inward-looking development strategy(i.e., import substituting industrialization) often results in domestic market saturation. The expansion of the market in terms of regional economic integration among nearby developing countries might solve such a problem without necessarily deepening dyadic dependence on the

advanced industrial countries (Axeline 1978; Mytelka 1973, 1979; Balassa and Stoutjesdijk 1975; Nugent 1982). Producer cartels have also been suggested as a workable option based on the success of OPEC. Existing commodity markets are biased against sellers not only in terms of the deteriorating terms of trade but also because of unstable export income. The only effective way to correct this problem and to reduce dependence is to set up intra-South producer cartels in selected commodity areas and by discarding consumer-producer agreements (Hveem 1978; Mikdashi 1974, 1977; McNicol 1978; Pindyck 1976, 1979).

The reassociationist strategy does not eliminate systemic vulnerabilities, although it minimizes them by selective realignment of external links. Developing countries under this strategic plan must import raw materials, capital and intermediate goods to sustain import substituting industrialization. At the same time, they need to finance their development projects by external borrowings. In many cases, export earnings from primary commodities become another important source of financing industrialization. These prerequisites for selective reassociationist strategies eventually push them into the varying degrees of systemic vulnerability.

A classic unilateral response to this problem is rapid domestic readjustment in issue areas. For example, world-wide inflation and financial instability force developing countries to choose austere stabilization measures on a voluntary basis or to have them externally

imposed. If a stabilization option is perceived to be too costly in terms of domestic political and social calculations of interest, other options such as unilateral default or tentative moratorium may be considered.²⁸ To minimize vulnerabilities resulting from boom and bust business cycles, commodity diversification and other related domestic policy measures are introduced. On the bilateral level, intensive bargaining with international organizations or transnational actors may be chosen as an option to reduce such vulnerability. Simultaneously inter-South diversification as a way of altering partners and markets is usually sought. Another favored option by the proponents of reassociationism might be collective action to change the structure of the existing regime of each issue area on a multilateral basis. Since systemic vulnerability is conceived to have something to do with the structure of the system, this collective approach would attempt to correct the existing rules, norms, procedures, and decision-making context governing certain issue areas.²⁹ The collective regime change scheme is best represented by recent efforts to institutionalize the New International Economic Order (Krasner 1981; Gosovic and Ruggie 1976; Christensen 1977; Galtung 1981; Jacobson 1983; Cox 1979; Sauvart and Hapsenpflug 1979).

While the first two strategies advocate a total cut-off from or a partial realignment with the international economic system, the associationist strategy emphasizes

positive integration into the international markets as a solution to economic backwardness and functional derangement of the national economy. Its proponents assert that there is nothing wrong with the current international economic system. Given small market size and scarcity in the factors of production endemic to developing countries, any attempt to withdraw from the international market means a substantial reduction of welfare for them. Artificial efforts to manage or coordinate markets either in terms of unilateral state interventions or of collective actions such as in NIEO create distortions and thereby curtail efficiency and welfare. Naturally, its proponents do not deny the existence of costs and constraints implicit in the associationist strategy. It is assumed, however, that the benefits and opportunities outweigh the costs and constraints or that those costs and constraints are transitional in the sense that the fuller exploitation of the opportunities offered by the opening of national economies will eventually eliminate them (Balassa 1981; Krueger 1982; Bhagwati 1977; Westphal 1979; Chenery 1981; Fishlow 1978).

Compared to the first two approaches, the associationist strategy by definition entails a much higher level of costs and constraints (Keohane and Nye 1977; Katzenstein 1977; Ruggie 1983; Haggard 1983). Within the given rules of the game defined by the international market mechanism, however, countries following this option attempt to deploy a variety of countervailing strategies to hold

down the costs and constraints and to maximize the benefits. Table 1-4 summarizes a number of policy options available under the associationist setting.

Table 1-4: Strategies under Association

	unilateral	bilateral	multilateral
S.D.	growth/export-promotion/ liberalization		
D.S.	item diversification/industrial deepening	contra-North bargaining/ inter-South diversification	regional integration/ collective bargaining
S.V.	stabilization/ industrial restructuring	bargaining/ diversification	collective cooperation/ bargaining

The proponents of the associationist strategy do not reject the claim that the initial phase of integration into the world economy (in terms of their colonial legacy) has created some structural distortions for developing economies. However, they do not go so far as to acknowledge the social and political consequences of the early pattern of integration. Structural distortions in this context merely denote economic backwardness originating from structural rigidity and lack of factors of production.³⁰ To overcome this distortion or dysfunctionality deriving from the previous pattern of linkage to the international economic system, it emphasizes

that developing countries must pursue more aggressive economic growth based on export promotion and a fuller liberalization of their national economies. In so doing, more active inducement of foreign capital and technology on the bilateral or multilateral level is recommended. Once growth is set in motion along with rapid industrialization, developing countries will be able to eliminate structural obstacles, and the benefits of growth will trickle down to the majority of people.

Under the associationist scheme more serious problems arise from dyadic sensitivity. Historical patterns of integration(i.e., from primary commodity, light industrial sector to heavy industrial sector) usually entail partner and item concentration in the trade sector (Galtung 1971; Santos 1974; Duvall 1978; Duvall, Jackson, and Sylvan, 1979). In particular the concentration of partners is not only limited to commodity trade but also to such sectors such as capital and technology. This concentration phenomenon puts small trading developing countries into vulnerable positions in terms of control and manipulation of large advanced industrial economic partners. Protectionism, high costs of technology and capital transfer, and selective blocking of bilateral economic transactions are examples of the costs and constraints stemming from this dyadic dependence. A classic strategy to overcome them is to diversify their exports through industrial restructuring and deepening unilaterally and to switch from large domineering partners to equal partners

on bilateral base. The latter usually involves an inter-South diversification of partners in the areas of trade, capital, and technology. At the same time, developing countries may pursue an intensive and extensive bargaining with the Northern industrial countries in lieu of trade and capital and technology transfer. Recent studies by Yoffie(1983), Gierico(1982), and Odell(1983) show that developing countries are inclined to opt for extensive bilateral bargaining with the Northern countries' over protectionist pressures or dominance of the Multinational corporations. On the multilateral level the associationists tend to rely on a laissez faire type of loose regional economic integration such as in ASEAN, the Pan Pacific Community, and the early LAFTA scheme. Or they may engage in multilateral bargaining within the existing regime structure such as that of the Multifiber Agreement and the Framework group in the GATT.

Certainly the associationist strategy risks the most structural vulnerability. Since economies under this scheme are tied to external, rather than internal, demands, and the overreall export promotion efforts chiefly financed by external sources, fluctuation in world markets and international financial instability often exposes these outward -looking developing countries to severe external vulnerabilities. Faced with this problem, they might adopt stabilization policies which would reduce the level of these external shocks, or rationalize the national

economy giving more leverage to the private sector in order to insure international competitiveness.³³ In certain cases the domestic policy option may call for an inward-looking orientation in order to insulate the economy from external shocks. In addition, efforts may be made to increase bargaining with the major international lending institutions or transnational actors. Bilateral bargaining with the IMF stand-bys and Eurodollar lenders are good examples of this tactics. Apart from bilateral bargaining, associationist countries may seek other partners who can provide more favorable terms of transactions independent of the existing regime rules and regulations.³⁴ On the multilateral level countries might pursue more cooperative attitudes toward the existing regimes. For example, instead of assuming a confrontational pose by participating in a producer cartel aimed at supply control, they might abide by the IMF compensatory financial scheme or other consumer-producer cooperative schemes. Also rather than pursuing a regime change, they could seek a regime-confirming multilateral solution to external financial problems as shown by recent efforts by the Latin American borrowers.³⁵

Explicit in all of this is the awareness that there is a wide range of possible strategies to cope with the costs and constraints. The choice of a particular strategy may be conceived of as a function of the policy makers' evaluation of the opportunity costs involved in each strategic choice. Or as Cox(1979: 231-252) has expounded, it may depend on the epistemological as well as

ideological tendencies of the decision-makers in question. For all these open-ended strategic possibilities, however, the literature in the field of international political economy appears to show a narrow trend in which scholarly investigators are preoccupied either with multilateral options to change or comply with the regime structure or with unilateral adjustment strategies in terms of the degree of openness and closedness.

The preoccupation with international systems and their rule structures is well reflected in the recent literature dealing with the problems of regional economic integration, producers' cartels, and the NIEO. In particular, the success of OPEC and its polemical linkage to the NIEO has provoked theoretical and practical concern over the utility of such multilateral-collective approaches. On the other hand, the successful entry of the NICs into the international economic system and the popularization of self-reliant strategies such as Mao's and Nyerere's has introduced a new dimension into the scholarly debates over the theoretical and practical usefulness of unilateral adjustment to the constraints and opportunities of the international system in terms of changes in development strategies.³⁶ The emphasis on these two behavioral dimensions (unilateral and multilateral) has, however, overshadowed another existing dimension, i.e., that of bilateral responses deployed by developing countries in the forms of bilateral bargaining

and diversification.

Dimensions of Third World Bilateralism: An Overview

As elucidated above, developing countries' bilateral behavior in coping with systemic constraints and opportunities is a complex phenomenon. Its nature can vary from one context to the other depending on the pattern of linkage with the international economic system. Under associationist and/or selective reassociationist strategies, developing countries may pursue a bilateral bargaining posture over the North or inter-South diversification or both, while the disassociationist pattern of integration leads to more explicit bilateral cooperation between a dyadic pair of developing countries in terms of barter arrangements and other policy coordination.

Recently several writers have begun to focus on the developing countries' bilateral bargaining behavior, particularly with industrial countries (Yoffie 1981, 1983; Gierico 1982; Odell 1982, 1983; Moran 1978; Clapp 1982). They have all analysed developing countries' bilateral bargaining behavior over protectionist measures, the dominance of multinational corporations, and other regulative and penetrative practices of developed countries. This trend reveals a sharp departure from the earlier preoccupation with systemic variables and

attempts yet have been made to understand another important dimension, namely Third World bilateralism, which is defined as economic relations between developing countries that are not necessarily bound to multilateral arrangements of rules, rights, and procedures, and that are believed to arise from deliberate inter-South diversification efforts in relation to the changing³⁷ configuration of systemic constraints and opportunities.

Inter-South bilateral economic relations in particular and intra-South economic relations as whole have been neither considerable nor dramatic in their volume compared with North-North and North-South economic relations. As Table 1-5 illustrates, intra-South economic relations evidenced by trade have shown a steady increase over the last two decades. In 1960, non-OPEC developing countries' exports to other developing countries including OPEC members was 21.9% out of total exports. But with the partial exception of 1970, the share of exports to other developing countries continued to increase, reaching 22.1% in 1974 and 29.2% in 1980. This incremental growth can be also found in the case of OPEC members. OPEC's export to other developing countries increased from 18% in 1970 to 23.9% in 1980 mainly due to the Oil Crisis.

Table 1-5

Table 1-5: Destination of World Exports

From/To	DC		DMES		CPE		World		Export as % of
	\$billion	%	\$ billion	%	\$ billion	%	\$ billion	%	Total world exports
DC									
1960	58.8	69.2	21.2	24.9	3.0	3.5	85.0	100	66.7
1970	172.5	77.0	41.9	18.7	8.4	3.8	224.1	100	71.8
1974	398.5	73.5	113.7	21.0	26.6	4.9	542.2	100	64.9
1980	911.3	70.5	300.7	23.3	64.0	5.0	1292.5	100	64.5
OPEC									
1960	n.a	n.a	n.a	n.a	n.a	n.a	8.5	n.a	6.7
1970	14.3	80.3	3.2	18.0	0.3	1.7	17.8	100	5.7
1974	95.6	78.2	24.5	20.0	1.3	1.1	122.3	100	14.6
1980	217.4	74.0	70.3	23.9	4.5	1.5	293.8	100	14.7
Non-OPEC LDCs									
1960	19.8	72.3	6.0	21.9	1.2	4.4	26.0	100	14.8
1970	26.4	70.6	7.8	20.9	2.9	7.8	37.4	100	12.0
1974	70.7	70.8	22.1	22.1	6.4	6.4	99.9	100	12.0
1980	152.8	63.2	70.6	29.2	15.8	6.5	242.0	100	12.1

Source: The US and World Development Agenda 1977 and 1982, Washington DC, Overseas Development Council

*DC: Developed Countries, DMES: Developing and Middle Income Countries (OPEC members included), CPE: Centrally Planned Economies.

One interesting aspect of Third World trade practices, however, lies in that intra-South exports have increased while the developing countries' share of total world exports decreased from 14.8% in 1960 to 12.1% in 1980. This trend implies an increasing relative weight of intra-South trade for developing countries' foreign trade. At the same time, figures in Table 1-5 indicate that while developed countries' exports to developing countries have declined from 24.9% in 1960 to 18.7% in 1970 and 23.3% in 1980 in terms of a share of total exports, both OPEC group and non-OPEC developing countries have shown constant increases in their exports to other developing countries. OPEC's exports to other developing countries rose from 18% in 1970 to 23.9% in 1980 and a share of intra-South trade for non-OPEC developing countries increased from 21.9% in 1960 to 29.2% in 1980. This phenomenon suggests that developing countries as a whole tend to seek more active trade relations with other developing countries than developed countries.

Growth in intra-Third World trade does not reveal much about the increase in inter-South "bilateral" trade. This is because many developing countries have engaged in intra-regional trade based on multilateral economic arrangements in terms of regional economic integrative schemes.³⁸ Traditionally intra-regional trade accounted for the bulk of inter-developing countries' trade. For example, in 1960 this component of the trade accounted for three-quarters of all inter-South trade. Not only because of

geographic proximity but also because of collective regional efforts to liberalize tariff and non-tariff barriers to regional trade, intra-regional trade continues to represent the major portion, 53% in 1978, of total inter-South trade in all commodity groups (Adams 1983:113). Thus, a simple way to come up with meaningful figures indicating the volume and direction of inter-South "bilateral" trade is to subtract the volume of such intra-regional trade from total inter-South trade. In other words, the volume and direction of the "inter"-regional trade, defined as flows between the major geographic regions of developing countries, can be useful indicators of bilateral economic transactions among developing countries.

Table 1-6 provides such data by delineating a changing pattern of intra-regional and inter-regional trade relations among developing countries. Explicit in Table 1-6 is the fact that inter-South bilateral trade represented by inter-regional trade is not large compared to that of intra-regional trade

Table 1-6

and to trade with industrial countries except West Asia, the Middle East, and certain African countries. One important aspect of inter-South bilateral economic relations represented by inter-regional trade is its rapid

Table 1-6: Trends in Trade among Developing Countries(1960-1980)

From/To	<u>Growth Trend in Merchandise Exports^{a)}</u>				<u>Share of Merchandise Export^{b)}</u>			
	LDCs all	Intra- region	Inter- region	Rest of world	LDCs all	Intra- region	Inter- region	Rest of the world
Latin America and Caribbean								
1960-1970	6.6	6.7	4.5	5.3	19.9	18.1	1.8	80.1
1970-1978	28.8	26.5	46.3	24.2	24.0	19.9	4.1	76.0
South and East Asia ^{c)}								
1960-1970	5.1	4.5	6.8	6.8	29.8	22.7	7.1	70.2
1970-1978	27.3	24.8	35.3	28.2	29.0	19.8	9.2	71.0
Middle East and West Asia ^{d)}								
1960-1970	7.5	8.6	6.5	9.4	18.6	7.7	10.9	81.4
1970-1978	58.0	38.5	68.2	53.4	21.9	4.6	17.3	78.1
Africa								
1960-1970	6.0	6.1	5.8	9.0	9.8	5.2	4.6	90.2
1970-1980	28.3	19.8	35.8	25.5	11.0	4.1	6.9	89.0

a) average annual percentage rate of growth, b) percentage share at the end of each period, c) entrepot trade of Singapore included, d) Northern African part of Middle East excluded.

Source: G.Mernon, Bridges Across the South(New York: Pergamon, 1980) Table 7.3, pp.56-57
United Nations, Handbook of International Trade and Development Statistics 1982 .

growth rate in both absolute and relative terms. In the case of the Latin American and Caribbean region where regional economic integrative schemes have been most active and have a long history,⁴⁰ while the share of intra-regional exports out of region's total exports had been stagnant between 1960s and 1970s(from 18.1% to 20.2%) and while the share with advanced industrial countries decreased during the same period (from 80.1% to 76%), exports to other developing regions increased sharply from 1.8% in the 1960s to 8.8% in the 1970s. The Table illustrates that other developing regions experienced almost similar trends where intra-regional trade and trade with advanced industrial countries has been either stagnant or declined over the last two decades.

The significance of inter-South bilateral economic ties can be seen through another dimension as well. The left column of Table 1-6 reveals an average annual percentage rate of increase of merchandise exports by developing countries. In the 1960s average annual growth rate of intra-Latin and Caribbean region exports was merely 6.7%. But in the 1970s, it reached 26.5%. A similar rate of growth in intra-regional trade can be seen in other developed regions: from 4.5% in 1960 to 24.8% in 1978 in the South and East Asia, from 8.6% in 1960 to 38.5% in 1978 in the Middle East, and from 6.1% in 1960 to 19.8% in 1978. Compared to this intra-regional trade, however, inter-regional trade has shown even more dramatic growth.

While its growth rate in the 1960s was less than 5% per year, it was more than 45% in the 1970s for the case of the Latin American and Caribbean region. Particularly the Middle East and the West Asian regions revealed very rapid rates of increase from 6.5% in the 1960s to 68.2% in the 1970s. Though not drastic, South East Asian and African regions also show modest yearly increases in exports to other developing regions.

This bilateral inter-Third World trade improvement is not a pervasive phenomenon encompassing all the developing countries, however. For the last decade, particularly since the oil boom, this form of economic transaction has been concentrated rather among particular groups of developing countries: that is, between capital-surplus OPEC countries and the NICs. As seen in Table 1-7, exports from the non-oil developing countries to OPEC alone increased by 637%, outpacing the growth of their exports to the rest of the world for most of the 1972-1978 period. From \$1.69 billion in 1972, exports from non-oil developing countries to oil exporters reached \$11.4 billion by 1978 in current

Table 1-7

dollar terms. For their part, the oil exporting countries increased exports to the non-oil developing countries from

Table 1-7: Regional Exports to OPEC(1972-80) and Shares of Total by Region^{a)}

	1972		1974		1976		1978		%increase 1972-1978

\$7.8 billion in 1973 to \$46 billion by 1979 (Hallwood and Sinclair 1981: 4).

However, not all developing countries shared in this strong growth in exports to OPEC members. Indeed, 13 developing countries accounted for about 90% of the overall increase in non-oil developing countries' exports to the oil exporters during 1972-1978 (Hallwood and Sinclair 1981: 132). Table 1-8 offers a list of the thirteen major trading partners of OPEC. Apart from Bahrain, all other trading partners are from non-Middle East regions. And except for Bahrain, Pakistan, and China, the remaining partners are the core or second generation NICs. Among

Table 1-8

them, the East Asian NICs (i.e., South Korea, Taiwan, Hong Kong, and Singapore) show the most remarkable export performance, constituting 42% of total. During the period of 1972-1978, Korea's export to the oil producers increased astronomically by 7,558%, followed by India (1,026%), Taiwan (2,710%), and Brazil (1,770%). Given the recent export performance of the NICs in the international economy, this OPEC-NIC trade partner concentration is quite understandable. According to Havryshylyn and Wolf's finding, the ten leading NICs of which the core countries

Table 1-8: Major LDC Trading Partners with OPEC (1972-1978, \$million)

Country/Year	1972	1974	1976	1978	1980	% share of total(1978)	% increase 1972-1978
South Korea	19	146	388	1,436		15	7,558
India	146	379	1,065	1,498		14	1,026
Taiwan	42	208	440	1,138		11	2,710
Brazil	53	461	582	938		9	1,770
Hong Kong	127	307	463	897		8	706
Singapore	132	358	795	903		8	684
China	165	515	661	865		7	524
Bahrain	31	106	244	482		5	1,555
Thailand	49	236	322	515		5	1,051
Pakistan	72	230	285	432		4	600
Argentina	24	181	198	258		2	1,075
Colombia	17	40	120	175		2	1,029
Mexico	56	49	79	123		1	220
						(100 %)	

Source: Hallwood and Sinclair, Oil, Debts and Development (London: Allen and Unwin, 1981) Table 7.2 p.134. And UNCTAD, Handbook of International Trade and Statistics, 1982.

fall into the above thirteen major OPEC's trading partners(excluding Taiwan) accounted for more than 80% of the inter-South trade in total non-fuel exports (1981:63). The increasing complimentarity between OPEC's rising demand backed up by new surplus capital and the NICs' newly diversified industrial capability might have been responsible for such a high concentration between the two groups.

As Table 1-9 indicates, the increase in these thirteen countries' exports to OPEC members had been accompanied by growth in OPEC's share of their total exports. In the case of Korea, the share of OPEC in its total exports rose from 3% in 1972 to 12% in 1978. Pakistan, India, Thailand, China, and Bahrain all indicate that OPEC members have become significant trade partners whose share goes beyond more than 10% of their total exports by 1978.

Table 1-9

Even for Brazil, Taiwan, Hong Kong, and Singapore, OPEC countries have emerged as modest trade partners accounting around 5% of their total exports. These figures explain that those thirteen major trading partners of OPEC have been able to diversify their external trade links which were mainly characterized by high partner concentration on

Table 1-9: Selected LDCs' Export to OPEC: Share of OPEC
in Their Total Exports, 1972 and 1978, by value

Country/Year	1972(%)	1978(%)
Argentina	1	4
Brazil	1	7
Colombia	2	5
Mexico	3	2
Bahrain	14	30
Taiwan	5	8
Hong Kong	5	8
India	5	14
Korea	3	12
Pakistan	11	27
Singapore	1	5
Thailand	5	11
China	6	10
EEC	4	9
All non-oil LDCs	3	7

Source: UNCTAD, Handbook of International Trade and Statistics, 1982
and Hall and Sinclair, Oil, Debts, and Development (London:
Allen and Unwin, 1981) Table 7.4, p.136

selected industrial countries, a primary cause of the dependence syndrome.

A less well known, yet significant, aspect of OPEC-NICs bilateral economic relations, in addition to the commodity trade discussed above, is a dramatic increase in the NICs' partnership in OPEC countries' construction and engineering projects. Since 1975, a large number of extremely remunerative contracts have been awarded to some selected NICs and other developing countries. Brazilian firms participated in a multi-million dollar housing project in Algeria and the construction of a Trans-Saharan road in Mauritania. Taiwan completed the al-Baha power project in Saudi Arabia, at a cost \$160 million, and now is engaged in a joint-venture petro-chemical plant in Saudi Arabia. Turkey has been an aggressive bidder in the Middle East construction market since 1978, winning more than \$3 billion in 1982 alone. For example, the developing countries' share in total contracts in the Middle East construction market (excluding Korea) reached \$ 13.2 billion in 1981. If Korea's total contracts are added, the figure goes to \$20.9 billion in 1981 (MEED August 6 :41). This figure indicates that the total from the construction sector far exceeded the total amount of commodity trade between the OPEC countries and this thirteen countries listed above.

The most striking example of the Middle East construction boom is the record of the Korean firms. From the status of a subcontractor for US and EEC companies,

Korea became the number one bidder in the Middle East construction market in 1981 outbidding its previous prime contractors. In that year alone, Korea won total contracts worth \$7.8 billion, which constituted about 50% of the total Middle East market for the year. From 1974 to 1981, the cumulative total amount of contracts won by the Korean bidders reached \$37.1 billion. In addition, Korea's construction exports to Southeast Asian countries amounted to \$2.2 billion during the same period (Korean Ministry of Construction 1982).⁴¹

Inter-South economic relations are not limited to the above mentioned sectors, but also extend to manpower migration, capital flow, and technology transfer. For example, the volume of remittances by Third World workers in OPEC countries rose from \$834 million in 1973 to \$5,368 million in 1977, and to \$9,244 in 1980 (Hallwood and Sinclair 1981:148 ; Katzousian 1982: 114). And apart from the recycling of petro-dollars to developing countries via the Eurocurrency market, OPEC countries in general and low-capital absorbers in particular have directly transferred large sums of capital to other Third World countries in terms of bilateral aid, joint-ventures in financial institutions, and direct and indirect investments. Furthermore, an increasing number of developing countries, particularly the NICs, have become a diversified source of technology transfer to the oil exporters in the fields of petro-chemical plants, steel, shipbuilding, and other consumer durable goods

industries.

Factual surveys clearly indicate that bilateral inter-South economic relations are an interesting and significant phenomenon on both the theoretical and practical level. In particular, dyadic relations between the OPEC countries and the NICs provoke curiosity as to how it was possible. Viewed from a conventional perspective, this kind of phenomenon is impossible not only because of the absence of industrial complementarity and comparative advantage derived from economic backwardness and rigidity, but also because of the developing countries' weak position in the international power structure.

In attempting to solve this puzzle, a number of theoretical conjectures can be made. One plausible conjecture is that because of geographic proximity, the opportunities for intra-industry trade, and the importance of similar demand patterns, there is a trade "bias" toward more mutual trading among developing countries (Havryshylyn and Wolf 1981:84). Apart from this economic explanation, the phenomenon might be due to psychological preference in the sense that "nations at the same level of stratification will interact with one another as equals while nations at different levels will not." (Galtung 1964:94) Or it could be a function of the 'ineffectiveness' of previous approaches: Unilateral closed options (individual self-reliance) have proven to be failures (Bierstekar 1981). Regional integrative schemes,

once highly regarded, have also been subject to various setbacks and bottlenecks(Mytellka 1979; Axline 1977 ; Nau 1981 ; Nugent 1982). Moreover, the limited success of producers' cartel schemes and the persistent stagnation of the NIEO might have induced some developing countries to search for bilateral options in terms of inter-South diversification (Rothstein 1981; Premtlau 1981; Haq 1981; Loeherand Powlson 1983). The rise of inter-South bilateralism is becoming pervasive while multilateral inter-South preferential trade arrangements proposed under the idea of collective self-reliance adopted and readopted in Arusha and Manila within the framework of the UNCTAD still belong to the realm of academic debate and policy speculation rather than actual reality.

On the other hand, it seems plausible to assert that the loosening of hegemonic power (i.e., monopoly structure) is responsible for the rise of inter-South bilateral economic relations. More specifically, the emergence of selected developing countries as significant actors in the international system (capital-surplus OPEC and industrially dynamic NICs) and the relative decline of OECD countries might have introduced a new systemic configuration and a relative comparative advantage in which these new actors can exercise more maneuverability and flexibility in enhancing their bilateral ties (Wallerstein 1974 ; Gilpin 1977 ; Krasner 1974 ; Turner and McMullen 1982 ; Haggard 1983 ; Babai and Haggard 1981).

All this is mere conjecture, however. Since there have been no serious attempts to understand this phenomenon, we cannot identify a set of definite variables responsible for the pattern of inter-South bilateral economic relations. Nonetheless, as we explained earlier, we have a notion that inter-South bilateral economic relations are a pattern of economic transactions arising from diversification efforts to reduce or eliminate the costs and constraints of deeper integration into the international system : namely dyadic sensitivity and systemic vulnerability. Keeping this in mind, the following sections of the study attempt to devise a workable theoretical model for Third World bilateralism with specific focus on the case of a dyadic interactions between the OPEC and the NICs (Chapter 2) and to apply the model to a case (that of Saudi Arabia and Korea : 1973-1982) in an attempt to understand the phenomenon more fully (Chapters 3 through 6). And finally the study seeks to address the question of permanence and the diffusion potential of this phenomenon along with assessment of its impact on stability and order in the international system broadly perceived(Chapter 7).

FOOTNOTE

1. Growth in global interdependence is a controversial topic. While Rosecrane, et.al.(1977:425-445), Katzenstein(1975: 1021-34), and Inkles (1975:467-9%) argue that there has been an increasing level of interdependence for the last two centuries, Waltz (1970: 205-223) counter-argues that interdependence is low and, if anything, is on the decrease.

2. The root of this evolutionary conversionist vision of global interdependence can be traced back to the tradition of idealism and functional and neo-functionalism. For this, refer to Etzioni(1965:131-148), Mitrany(1966), and Sewell(1966). For a comprehensive discussion of this topic, consult O'Leary(1978) and Koehane and Nye(1975).

3. An analytical distinction between "by choice" and "by necessity" is quite ambiguous. However, a liberal interpretation proposed by Balassa(1981), Krueger(1978) and Bhagwati(1978) posits that the Third World integration into the international economic system is largely a function of conscious policy choices of developing countries particularly in terms of foreign trade regime. On the other hand, Frank(1969, 1980), Wallerstein(1974), and many others following the Marxist-Dependencia tradition view that the incorporation of developing peripheral countries into the system is determined by historical necessity of capitalist development.

4. The ways and means to overcome the cost and constraint of global interdependence have been sought from the two major directions. One is to realign the modes of external links(trade and capital), and the other is to search for domestic readjustment in terms of transformation of development strategy as a whole. This research combines both aspects in a synthetic manner.

5. The theoretical aspect of conversion thesis can be found in Almond(1970:224-33, 310-331). Rostow(1960), Weiner(1966), Lerner(1967), and Morse(1969) projected this optimistic vision of the Third World future.

6. For this, refer to Balassa(1980a, 1980b), Krueger(1978), Little, Scitovsky and Scott(1970) and Bhagwati(1978). For the ideological defense of liberal economy from the neo-classical perspective, consult Johnson(1974), Freedman(1977), and Bauer(1981: 185-190).

7. This claim needs a substantial justification. Viewed from the relative terms, the goals of the three Development Decades set by the UN have not been satisfactory. For this topic, refer to various issues of the US and the Third World Development published by the Overseas Development Council.

8. The disruptive effects of interdependence have been viewed from various angles. Ruggie (1983) comes up with economic, technological, and linguistic negative effects of interdependence, while K. Holsti (1981) suggests political costs (particularly political disintegration) of interdependence. But more intense critiques of negative consequences of interdependence come from the Marxist-Dependencia tradition. There is a pool of literature dealing with this topic from the latter tradition. However, for a succinct discussion of this topic, refer to Cockcroft, Frank and Johnson (1972), Mahler (1980), and Lehman (1979).

9. Certainly the perception or calculation of the costs and benefits is contingent upon the ontological and epistemological positions of investigators. For this topic, refer to Gilpin (1976), Cox (1979) and Shaw (1979).

10. The concepts of vulnerability and sensitivity are borrowed from Keohane and Nye (1977), while the notion of structural dysfunctionality is derived from Caporaso's discussion of dependency (1978:2-6). Haggard (1983)'s initial efforts to identify the costs and constraints of interdependence in terms of sensitivity, vulnerability, and reliance helped this analytical distinction.

11. It is unpredictable because of synergistic uncertainty inherent in the international economic system. And it is undifferentiated since systemic effects are applied to all the component parts in the system, though in varying degrees. These two attributes lead to a lesser degree of control by national actors.

12. "Conditionalities" refer to the terms imposed by international financial institutions on borrowing countries as qualifications for the granting of credit. Usually they comprise a set of austere economic measures to freeze wage, to cut public spending, and to liberalize the national economy. For this topic, refer to Eckaus (1982: 767-780) and to Williamson (1982).

13. The degree and extent of structural vulnerability depends heavily on relative power of integrated country, domestic adjustment capabilities, and the ability to displace costs and risks.

14. Refer to Caporaso (1978:20).

15. For a general discussion of power relations, consult Blau(1964), Emerson(1960), and Burns and Buckley(1977). In the context of the international political economy, Baldwin(1979, 1980) and Caporaso(1978) make an excellent analysis of power and dependence relationship.
16. The NICs' major trading partners are the USA, Japan, and EC. At the same time, their exporting items are heavily concentrated in the light industrial sectors such as textile and clothing and consumer electric goods. For the partner and item concentration, refer to Harvylyshyn and Alikhani(1983) and Park(1980).
17. The conventional understanding of dependency focuses mainly on external exchange relations in terms of dominance and dependence. However, this research places its primary emphasis on internal consequences of such external exchange relations manifested in terms of limited developmental possibilities.
18. The context of dependency varies from one country to the next depending upon historical timing and domestic social formation. As Duvall and Freeman(1983) have suggested, however, the dependency context can be classified into the four major types: classical neo-colonial, enclave, associate dependent, and recurrent dependent contexts. This typology can be useful not because it informs us of the pattern of external ties, but because it identifies the types of development strategy as conditioned by external ties and domestic social formation.
19. This view follows a classical Leninist position in the sense that without a fuller maturity of capitalism in the South, socialist revolution as a historical end is not possible. Thus, in this view colonialism did not retard or distort indigenous capitalist development but rather acted as a powerful engine of progressive social change. Refer to Warren(1980:8).
20. Articles in Ruggie(1983) present various aspects of antinomical nature of interdependence in the context of developing countries.
21. For a succinct discussion of historical evolution of development strategies, consult Bloomfield(1973), Rothstein(1977), and Todaro(1981).
22. Although these authors focus on the systemic factors in the formulation of countervailing strategies, their theoretical starting points are different. While Krasner(1981:172-201) derives a regime change option out of power analysis, Inoguchi(1981:255-276) suggests exit and voice options following Hirschman(1970)'s line of reasoning. On the other hand, Hansen(1979) and Alejandro-Diaz(1978) draw strategic options from the transformation

of development strategy. Wriggins(1978:21-117) identifies six options, both economic and political, largely by analysing previous experiences of developing countries. The three types of strategy described here (associationist, re-associationist, and dessociationist) are mainly drawn from Alejandro-Diaz and Inoguchi.

23. The idea of self-reliance has been the dominant theme in the Marxist-Dependencia literature. However, there is no clear-cut consensus on strategic choice among individual, collective, and/or sectoral reliance. For a recent debate on this topic, refer to Munoz(1982:117-314). And for a critical analysis of individual self-reliance, consult Biersteker(1980).

24. Of course, it is misleading to equate self-reliance strategy with basic needs strategy. Self-reliance and de-link from the system may involve two major types of strategy: one is to follow the Maoist line emphasizing the relations of production and thereby the provision of basic needs, and the other is to pursue the Stalinist line focusing on the forces of production as can be seen in the case of North Korea.

25. Not all the proponents of this selective re-association strategy conceive the international economic system in terms of positive sum game. The proponents following the tradition of the Economic Council on Latin America and its ideologue, Raul Prebisch understand the dynamics of the international economic system from the zero-sum game perspective. For the latter, thus, the reform of the international rule structure in the direction of the positive sum game becomes the essential prerequisite for selective re-linking.

26. Selective re-linking does not spontaneously lead to balanced growth and the satisfaction of basic needs. Rather, the reverse has been the case. For this discussion of this topic within the framework of NIEO-Basic needs strategy dichotomy, refer to Galtung (1979).

27. Protective policy measures pursued under the ISI setting comprises a broad range of options including artificial ovrevaluation of exchange rate and high import tariffs.

28. Stuart Greenbaum (Time, Jan. 10, 1983 :50) succinctly summarizes the point in case as in the following: " Imagine you are a Latin dictator deep in debt. If you (accept IMF terms and) cut back on imports, you get riots in the streets. If you default, you are ostracized by the world capital markets. Now if the first approach leaves you swinging from a tree branch, you know you are going to go default route."

29. Young(1980:333) , Haas(1980:358) and Krasner(1982:186-189) offer excellent analyses on this topic.
30. There is a fundamental problem of incommensurability between liberal and dependencia interpretation of the cost and constraint of interdependence. The liberals such as Bauer, Johnson and Friedman perceive that economic backwardness in developing countries is transitional one, which can be overcome eventually as they become more integrated into the global market.
31. Mytelka(1979:9-16) classifies three different types of regional economic integrative scheme: a laissez faire type(e.g., LAFTA and CARFTA), a hybrid combining a laissez faire with compensatory elements through planning(e.g., CACM and CARICOM), and a dirigiste system linking planning to regulation within a regional context(e.g., Andean Group).
32. The Mutifiber Agreement can be regarded as multilateral reactions on bilateral regulation by developed countries, while the Framework group's efforts in the GATT are a multilateral action by the selected NICs within the existing rules of the game. Refer to McMullen (1982: 78-97) and Turner and McMullen (1982).
33. Usually stabilization measures are followed by external pressures such as IMF conditionalities. But countries may pursue such policies on their own initiatives to cope with inflation.
34. Search for petro-dollar recycle in terms of OPEC's financial assistance or concessional financing is an example for this strategy.
35. This is a loyalty option in Hirschman(1970)'s terminology or an embourgeoisement strategy in Hansen(1979)'s view. In this regard, Haggard and Babai(1981) identify four options in the existing regime structure: 1) incorporate into the existing set of regime rules. 2) increase share of benefits under the existing regime rules. 3) restructure the existing regime rules. 4) alter decision-making modalities and instruments of the existing regime.
36. The increasing preoccupation with regime change or de-linking option by the students of the international political economy has been motivated by a series of events taking place in the late 1960s and early 1970s. The politicization of global hunger and a high publicity of Mao's and Nyerere's self-reliant strategy and the success of OPEC and its diffusion effects on other commodity cartels and so on had induced scholarly as well as practical concerns on such options. Gosovic and Ruggie(1975), Christensen(1977), and Krasner(1981) treat this topic in

terms of issue-linkage and ideological bandwagon effects.

37. If we follow the Grotian interpretation of regime as postulated by Young(1982) and Stein(1982), the Third World bilateralism defined here is certainly regime-bound. However, the definition of regime used in this research is narrow and strict one based on structural realist conception (Krasner, 1982). In addition, the contents of bilateralism are not limited to trade sector alone, but extended to overall sectors of economic transactions.

38. Menon(1979) and Pavlic et.al. (1982) attempt to understand the South-South cooperation in terms of comparison of intra- vs. inter-regional economic transactions.

39. Certainly, understanding bilateral ties in terms of inter-regional economic transaction is controversial. Due to technical reason, however, this research avoids a complete disaggregation of inter-South bilateral ties. Even if we estimate the number of developing countries modestly (i.e., 130 countries), in case of disaggregation it requires a study of $130 \times 130 = 16,900$ dyadic pairs. If commodity dimension is added, it becomes much more complicated job. To avoid such a complexity, this research adopts inter-regional ties as a relevant indicator of bilateralism.

40. The African region also has numerous economic integrative schemes. However, the Latin American and Caribbean region has shown a much more active tendency. Mytelka(1979) provides an excellent review of the Latin American integrative schemes.

41. With the slow-down of the Middle East boom, South Korean government has set up so called the Post-Middle East strategy in which the South East Asian region has become the primary target.

42. More detailed examples of this case will be provided in chapter 7. Hambleton(1982) offers a good description of Korea-Taiwan-Saudi Arabian joint cooperation in the Saudi petro-chemical sector.

CHAPTER TWO

THEORIES OF BILATERALISM: SEARCH FOR INDEPENDENT VARIABLES

As we have seen in Chapter One, the scope and intensity of bilateral economic interactions between the NICs and OPEC countries is impressive. This newly emerging pattern of external economic behavior on the part of these selected developing countries poses three major questions that require further research agenda: What are the causal factors responsible for the dramatic increase in economic interactions between two groups of countries? Through what mechanism and how is this form of inter-South bilateral relations promoted or discouraged, and what are the process-level dynamics constituting these bilateral ties? And finally what are the resulting outcomes of this type of interaction, and what are the major theoretical and empirical implications that can be drawn from this phenomenon?

Finding precise explanations for this set of dependent variables is not easy, particularly since there are no readily available theories or explanatory schemes expressly designed to fit the topics of our inquiry. Nevertheless, if we treat the topic within a broader framework of bilateral economic relations defined as patterns of economic interactions between a dyadic pair of

countries which can be conceived of as not being
constrained or conditioned by collective arrangements of
rules, norms, and procedures,¹ then it does seem possible
to come up with a set of workable theories or models.
Bilateral economic relations have been the primary topic of
investigation in modern theories of international trade.
At the same time, a number of international relations
theorists and international business management scholars
have dealt with the topic in one way or another.

This chapter, therefore, is devoted to a systematic
delineation of current theories of bilateral economic
relations, the critical application of such theories to
the topic of our inquiry, and finally the identification
of a set of independent variables through the formulation
of a new eclectic theoretical model entitled the statist
model of inter-South bilateralism.

The Economic Explanations

Comparative Advantage: Most traditional theories
regarding the international economy are concerned with the
pattern of trade. They usually assume a two country - two
commodity exchange in such a way so as to explain why and
how much exchange of goods, services and capital takes
place between whom (i.e., a dyadic pair of countries) and
in what. Thus the study of the international economy
begins in a bilateral setting, a major concern of our
investigation.²

In attempting to make a qualitative explanation and prediction of the direction, volume and commodity composition of bilateral economic flows, the theory of comparative advantage has been widely used. The theory begins with the recognition that in the absence of foreign trade domestic consumption and domestic relative prices differ from one country to another. This difference makes export and import goods and services depending on their comparative advantages or disadvantages. The result is that neither country suffers by such trade and both benefit if goods and services are exchanged at some intermediate price ratio. How then are comparative advantages or costs determined?³

Ricardo argued that trade could occur even if one nation is absolutely efficient in the production of all goods. The basis for trade in the Ricardian sense stems from price (cost) differences which in turn are governed by natural or acquired comparative advantages affecting input productivities (labor). Although Ricardo's comparative advantage principle has a normative character, one would argue that the precise pattern of specialization in production and trade, which implicitly indicates the direction, volume, and composition of trade, would depend on comparative costs measured in terms of a single factor of production: labor.

The Ricardian single factor explanation of comparative costs was further modified and developed by the Heckscher-

Ohlin theorem of factor endowment. The theorem asserts that the Ricardian stipulation of labor as the single determinant of comparative costs does not fully account for the patterns of trade. It postulates that differences in comparative costs are a function of differences in the ratio of factors of production with which countries of exchange are endowed. Thus it is not only labor but also capital and natural resources endowed that determine comparative costs.

Viewed from this perspective, countries tend to export goods and services representing their relatively more abundant factors and to import goods and services embodying their relatively scarcer factors. For example, a relatively capital abundant country tends to exhibit a comparative advantage in producing capital intensive goods, while a relatively labor abundant country finds itself comparatively more competitive in labor intensive goods.

Given the assumptions of the Ricardian and the Heckscher-Ohlin theorem (particularly no-country specific resources or factors of production and two country, two factors of production and two commodities among others),⁴ these theories of comparative advantage in general do not deal with the issue of the direction of trade in goods and services explicitly,⁵ although they deal with volume and commodity composition.

Notwithstanding this limitation, Krueger(1977) and Baldwin(1979) have applied this Heckscher-Ohlin theorem to developing countries as a means of understanding or

explaining the direction of trade flows. By replacing the two-country fit by a multi-country world in which countries' relative endowments of capital and labor are on a continuum, they argued that the direction, volume and commodity composition of trade flows can be explained (or predicted) by the modified Heckscher-Ohlin theorem. According to their assertion, a country will trade in both directions, selling more labor-intensive goods to countries more generously endowed with capital and vice versa. Following this line, they inferred that developing countries, particularly rapidly growing ones such as the NICs, will export more labor intensive goods to developed Northern countries where the level of capital endowment is relatively higher and more capital intensive goods to other developing countries endowed with lower overall capital factors and vice versa for imports.

Technology and the Product Cycle: Although the theory of comparative advantage remains the chief explanation for trade patterns, it has suffered from numerous criticisms, extensions, and modifications.⁷ The most crucial criticism has focused on the assumption of the static nature of comparative advantage. As Balassa(1979) has argued, the overall pattern of comparative advantage changes as a country changes its relative factor endowment over time. For example, rapidly developing countries such as the NICs gain advantage overall in more skill and capital intensive activities while losing advantage to

slowly growing countries.

The key determinants of this dynamic change in comparative advantage are regarded as being human skills and technology which in the conventional theories of comparative advantage were assumed to be common to all countries with a universal standardization. In fact, the theory of comparative advantage treats the determinants of factor endowments as exogenous and overlooks the important fact that technologies and the quality of labor are not the same among nations producing the same goods, and this in turn greatly affects the direction, volume, and commodity characteristics of economic flows.

For instance, Keesing(1966) takes the skill-content of labor force out of the Heckscher-Ohlin theorem. According to him, the quality of labor is not homogeneous, unlike the Ricardian assumption. The quality of the labor force varies depending on the degree of training and sophistication. Thus countries that are relatively well endowed with professional personnel and highly trained labor will specialize in and export skill-intensive goods. Conversely, the relative abundance of unskilled labor promotes the export of goods produced by mostly untrained labor.

While Keesing focused on the skill-content of labor, Posner(1961:323-341) and others posited technology gap as a determinant of the patterns of trade in the process of new commodity development, growth and maturity. The proponents of the technology gap model argue that the industrially

sophisticated countries are the early producers of new products and therefore they enjoy easy access to foreign markets at an early stage of manufacture. Later a process of imitation sets in, as other countries start producing and exporting these goods by relying on lower wages or some other factor-cost advantage. In other words, the time lag involved in the imitation process largely determines the direction, volume, and commodity composition of trade flows. According to this model, rapidly developing countries such as the NICs would have a greater propensity to export those matured goods and services to other developing countries as Japan did in its earlier stage of development.

A more recent and convincing model of explaining the patterns of trade and capital flows in terms of technological factors is the product cycle theory.⁸ Instead of emphasizing the time lag in the imitation process, the product cycle theory stresses the standardization process of products. Furthermore it radically revised the static assumptions of the comparative advantage theory in such a manner that: 1) knowledge or technology is country-specific, 2) knowledge or technology is unevenly distributed over the world, and 3) knowledge or technology is slowly diffused over the world. Adding this dynamic quality of technology to the existing body of comparative advantage theories, the theory postulates that early manufacture of a new product involves experimentation with both the features of the product and the manufacturing

process. Thus in its beginning stages the good or service is non-standardized. As markets grow and the various techniques become common knowledge, both the product and the process become more standardized and perhaps even subject to internationally set standards and specifications. At this juncture, production can begin in less sophisticated countries (Vernon 1968).

This product cycle theory in particular and the skill-technology factor explanation in general offer us a number of implications to the direction, volume, and commodity composition of developing countries. First, a developing country might trade goods and services of a given level of sophistication in all directions. Second, the country would be unlikely to trade goods and services of similar level of technology with other developing countries. Third, as standardization continues, rapidly growing countries such as the NICs may pick up new products and export them (the standardized goods and services) to other developing countries until the latter begin to produce these standardized goods and services later.

Demand-Side Effects: Both the comparative advantage argument and the technology factor explanation attempt to come up with qualitative predictions of the pattern of trade and capital flows in terms of the level of inter-industrial complementarity from a supply-side perspective. In other words, international trade compensates for national deficiencies of countries involved in an exchange

of goods and services, whether in capital, labor skill, management or technological sophistication. The gain from trade derives from the fact that it enables countries to specialize in goods and services that require these factors in abundant supply. The result is that countries import and export dissimilar goods and services, dissimilar in terms of one or more factors of production mentioned earlier. Thus, the more divergent the countries' endowments and the level of technological sophistication, the more dissimilar the goods and services exchanged and the greater the gain from trade.¹⁰

In contrast with the supply-side explanation, a number of economists have conceived the issue from quite a different angle: that of demand-side and of intra-industrial competition.¹¹ According to the proponents of the demand-side explanation of trade patterns, a country's exports are merely an extension of production for the home market. Such production caters to the needs of the majority, and it is through producing for that market that the country acquires a comparative advantage in the product and then exports it. The slightly different demands of the minority of the population can be met with imports from a country where such tastes are those of the majority. But since the type of goods demanded in a country is thought to be uniquely determined by the overlap of domestic demand structures supported by the level of per capita income, most exchanges of goods and services take place between

countries of similar industrial structures.¹² This model of demand similarity (or of overlapping demands) views trade in residual terms. That is, domestic demand for a particular good is subtracted from the domestic production of the same good, and the remainder is deemed the net export of a given country. And the global market place is then a pool composed of net export supplies and net import demands. At the same time the import demand of a particular country for a given good from a specific supply country becomes a function of income and relative prices following a general Hicksian model of demand (Margee 1975 ; Pollins 1982 ; Armington 1978).

Utilizing the demand similarity model, Linder(1961) attempts to explain the patterns of trade among developing countries. Assuming that trade flows will radiate outwards towards proximate and similar markets, he asserts that the greater the similarity btween the patterns of domestic demand, the higher the trade between two countries. Since developing countries are more similar to one another than to industrialized countries, the implication is sizeable trade, other things being equal, among developing countries and relatively little trade between North and South.

Critique: The economic explanation rapidly summarized above provides us with three major independent variables to explain the pattern of inter-South bilateral relations: comparative advantage, technology, and demand-side effects. In fact, those variables are chiefly responsible for the

shifts in the direction of economic flows in Third World countries and for the rise of bilateral economic concentration between the NICs and OPEC. Structural changes in the NICs and the advent of comparative advantage in favor of the NICs with the gradual spread of technology to these countries have enhanced their international competitiveness in certain goods and sectors and have opened a way to increased economic transactions with other developing countries. At the same time, these Newly Industrializing Countries' increased demands for oil and other Ricardian goods as a result of their rapid economic growth and structural change might have contributed to the rise of inter-South bilateral relations with OPEC countries.

On the other hand, demand-side effects may account for the contents of inter-South bilateral relations, particularly the concentration of economic flows between the NICs and OPEC. The competitive formation of relative price for certain standardized goods and services originating from the NICs and a greater level of income inelasticity of demand for OPEC countries with their massive oil revenues following oil crisis might have induced such a concentration phenomenon between these two special groups of developing countries. In other words, the NICs could offer competitive prices, as a consequence of changing comparative advantage and technology, for those goods and services which OPEC countries needed. On the other hand, OPEC members could afford to purchase those

goods and services without any financial constraints while
other developing countries could not.¹³

For all this general accountability of inter-South bilateral relationships, however, economic models are not without some limitations. The first comes from their dependence on the 'aggregate explanation.' Indeed the models are able to make a qualitative prediction of the direction, volume, and commodity composition of economic flows, but only in the aggregate sense. If the Third World countries are disaggregated into sets of numerous dyadic pairs and if a prediction of and/or explanation for the specific directions of bilateral flows for those dyadic pairs is needed, these pure economic models lose their theoretical power.

For example, let us examine the demand-side explanation of inter-South bilateralism. If the pattern of trade is determined by demand similarity, income and relative price, there is no reason why the Middle East OPEC countries import more goods and services from the East Asian countries than elsewhere. There is an ample number of countries around them (Israel, Spain, Greece, and the Eastern European countries) which maintain a similar economic structure and demand taste as well as a similar level of comparative advantage as those of the East Asian NICs. If the margin of price is competitive enough between the East Asian NICs and these neighboring countries, no discernible explanation is possible for the

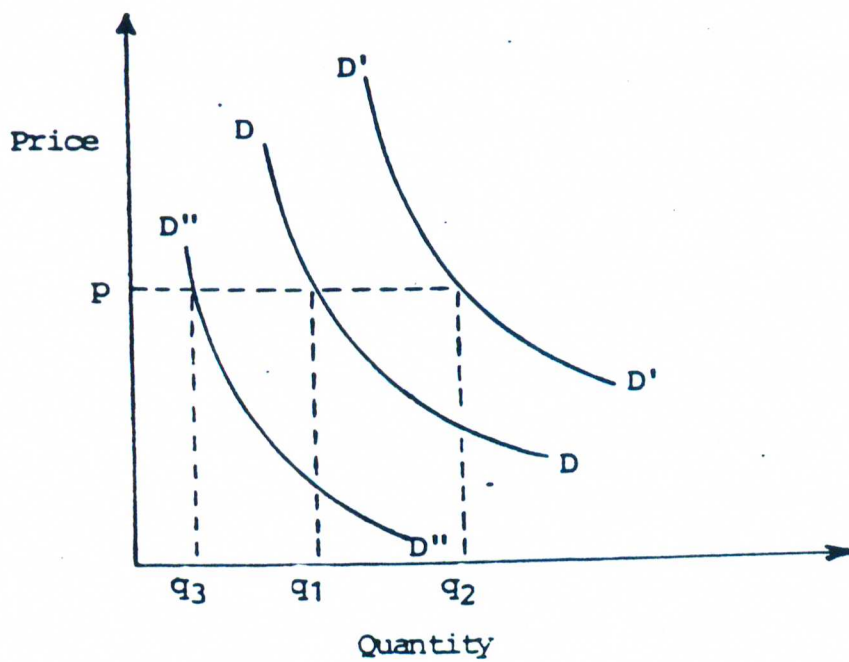
large inflow of the East Asian goods into the Middle East OPEC countries.

To elaborate this point further, consider a hypothetical situation of demand curves as in figure 2-1. While the price for a certain good is identical for these three demand curves, the quantity demanded sharply differs from one curve to the other. Here economic variables (i.e., comparative advantage and technology) determine the shape of the demand curves. But the location of the demand curves, namely quantity differentials, is largely determined by exogenous and non-economic variables such as distance, commercial policy, embargoes, and other political factors. In this diagram, the $D''-D''$ curve reflects a hostile dyadic relationship such as that between Saudi Arabia and Israel. The $D-D$ curve may indicate a neutral relationship such as between Saudi Arabia and Singapore. Finally, the $D'-D'$ curve may be found in a very congenial and friendly dyad such as the relationship between the US¹⁴ and Saudi Arabia.

Figure 2-1

What is implied here is that there is no infinite substitutability of demand in the real world. Various market imperfections, either caused by environmental factors or by the conduct of deliberate state policies, make it difficult to explain and predict the direction,

Figure 2-1: Demand Curves under Different Political Conditions



Readpated from Pollins (1983) p.30

volume, and commodity composition of trade and capital flows purely by economic variables. Thus, an economic explanation alone does not fully cover the causal factors responsible for the rise of bilateral economic concentration between the NICs and OPEC.

Another major limitation of economic explanations stems from their neglect of dynamic political factors as decisive determinants of the pattern of trade and capital flows. Although comparative advantage and technological level are important variables, they need further explanation to be proper independent variables. As Balassa(1979) points out, comparative advantages are not static, but dynamic. And this dynamic nature of comparative advantage is not reshaped only by changing the level of technology and the level of economic development. Particularly in cases of developing countries, the nature of state intervention into the market as conditioned by the state objectives greatly influences the pattern of trade and capital flows.¹⁵ For example, the state implementation of various non-discretionary macro policies such as foreign exchange policy, trade policy and the related tariff and non-tariff barriers, and interest rate policy also affects the pattern of trade and capital flows. Furthermore the state can play a more decisive role in determining specific economic partners and commodities by providing private companies interested in a specific target country or commodity with a mix of various discretionary incentives

such as tax benefits, technical and informational services,
subsidies, financial supports etc. In some cases the
pattern of trade and capital flow and the terms of market
entry may be arranged by bilateral negotiations between
governments involved.¹⁶
¹⁷ Heavily relying on purely

exogenous economic conditions and positing the market as
the sole mechanism of bilateral economic flows, these
economic models of bilateralism appear to fail fully
explain the causes, dynamic processes, and the outcomes of
bilateral economic relations in general and those among the
Third World countries in particular.

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Ecological Models of Bilateralism

Explicit in economic models is that supply- or demand-
side effects are the necessary and sufficient conditions
for the explanation of the pattern of bilateral trade and
capital flows. In reality, however, while supply-side
effects are subject to domestic policy adjustment and
change, demand-side effects are equally influenced by
various non-economic exogenous variables. It is quite
common that goods, services, and capital are usually
differentiated according to their country of origin, and
the elasticity of substitution is not infinite. As a way
of complementing these weak economic explanations, a number
of economists and political scientists have identified a
set of ecological or environmental variables that directly
or indirectly affect the direction, volume and composition
of trade and capital flows. Non-economic and non-price

variables such as the nature of political, cultural, and historical ties and geographical distance may induce each buyer or seller to discriminate among goods, services, and capital in a particular market according to their country of origin.

Distance: In discussing these ecological determinants, the physical distance and the related transportation cost is usually singled out as the primary variable. This is particularly so because transportation costs are usually assumed to be zero in conventional models of international trade. In fact, when a sector is marginally competitive, transportation costs do make a significant difference between marketing it or not (Roemer 1977:322). Certainly the closer, the more competitive. Thus, distance between traders may have a crucial effect on the direction and magnitude of trade flows. In many cases, however, physical distance alone may not have such a crucial impact. As Kindleberger(1964:15) has observed, since transportation costs, even for bulky heavy machinery goods, amount to perhaps less than 2% of delivered value, they may be safely ignored by economists.

Considering this problem, Tinbergen(1962) and Linnenman(1966) expanded the notion of distance more comprehensively and excluded prices as a key determinant of trade flows.¹⁹ To reflect the issue of distance more realistically, they came up with a "gravity design" which

attempts to locate 'trade biases' affecting gross, bilateral flow of trade. In this model the trade volume and direction between any dyadic pair of countries have been perceived to be a function of size and geographic distance. Size indicated by national income is chosen because it reflects supply potential (for exporters) and market size and demand (for importers). On the other hand, geographic distance is operationalized not only by transportation costs but also by non-economic variables such as political ties, shared colonial experiences and availability of a customs union. This gravity model was further developed by Parker(1979) and participants in the SARUM model.²⁰ In this model the size variable is further specified in terms of relative prices as well as income effects which are designated as the most important variables affecting the direction and magnitude of bilateral economic flows. As supplementary variables, historical, cultural, and political ties are incorporated into the model along with transportation costs and commercial policy.

Zone of Influence and Hegemony: The conjunction of economic factors and distance variables was a major advancement in explaining and predicting the patterns of trade and capital flows. Nonetheless, these 'distance' models gave their prime values on economic variables by treating non-economic exogenous ones as "dummy" variables.²¹ Roemer(1977) attempted to spell out this

neglect by developing a notion of "sphere of influence".

In his words:

(E)conomic distance or sphere of influence factors- which include factors beyond transportation costs, such as historical and cultural ties between traders, the tying of aid, the setting-up of multinational subsidiaries, and preferential treatment of one country's exports for other reasons- bias trade as follows: countries tend to market their weakest sectors of manufactures disproportionately in their sphere of influences. Moreover it is shown that this biased pattern of trade cannot be explained solely by distance between traders, but must result in part from causes that are not economic in the narrow sense (1977 : 318).

The above statement indicates that market imperfections are the salient feature of international economic transactions and that the trade biases resulting from non-economic factors greatly affect the direction, volume, and composition of trade and capital flows. Roemer(1977: 322-323) identifies five major non-economic variables shaping the trade biases between a dyadic pair of countries in addition to economic variables indicated by transportation costs. They are: communication channels represented by the level of business and information connection, preferential tariffs and other forms of discrimination, aid policy such as conditional exchange of goods and services for aid given, multinational subsidiaries and intra-firm trade, and finally consumer tastes shaped by historical and cultural factors.

The Roemer thesis of 'zone of influence' matches well with various arguments advanced by the students of dependencia, world system, and power exchange theories.

For example, it summarizes neatly Hirschman(1981)'s idea on the political power basis of economic dependence in such a manner that politically powerful countries market more of their competitively weak sectors in areas where they have influence, for historical and political reasons, than they would otherwise. At the same time, this zone of influence thesis epitomizes the arguments raised by dependencia and world system theorists. Colonial legacies and the resulting pattern of the peripheral countries' integration into the international division of labor led to a vertically structured hierarchical relationship between former colonizers and the colonized. This rigid vertical relationship manifested itself in forms of dependence-dominance and the related unequal exchange between the two (Galtung 1971: 89; Wallerstein 1979, Prebisch 1971; Stewart 1975; Frank 1980).²⁴ The 'zone of influence' scheme, however, is not limited to a dyadic pair of the influencer and the influenced. To expand this notion a little further in terms of hegemonic leadership or world system perspective,²⁵ it helps to delineate additional systemic factors which affect or determine the patterns of trade and capital flows. The domination of financial and trade networks by the multinationals, the oligopolistic pricing of international shipping conferences (Yeats 1972; Laing 1977), variable currency clearing arrangements tied to the core countries' currencies, and other marketing, production and financial barriers, are greatly shaped by the

intentions and operational modes of influencer countries at
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the core of the global economic system.

This 'zone of influence' or hegemony perspective provides us with ample insights for the understanding of international economic transactions. However, it is largely limited to cases between North and South where the relationship of influencing and influenced is much more clearly demarcated. When applied to inter-South economic behaviors of developing countries, it appears to have very narrow implications mainly because the inter-South relational dimension is treated as trivial and therefore omitted.²⁷ Nonetheless, it is still possible to draw some guidelines by which the patterns of inter-South bilateral relationships can be examined. First, the economic flows between a random dyadic pair of developing countries are likely to be low due to a lack of channels of communication and information. Second, the direction of economic flows of developing countries is largely shaped by the level of commonality tied to different zones of influence. Shared colonial experiences between a pair of developing countries such as former British or French colonies may promote a higher level of economic transactions between them than they would otherwise. Finally, it is less likely for developing countries to develop their economic ties with other developing countries solely on their own initiatives. Inter-South bilateral relations are more apt to be conditioned or determined by the mediating role of multinational corporations and/or

international financial institutions in terms of intra-firm trade, international subcontracting, financial recycle, and information sharing.

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Political Determinants: Only recently have political scientists singled out the pattern of bilateral trade and capital flows as a dependent variable (Pollins 1982). Prior to this new trend, most political scientists treated economic flows as an independent variable to explain certain political phenomena, namely integration. A pioneering work along this line was done by Savage and Deutsche (1960: 551-572). By postulating transaction flows as indicators of the level of integration between two countries, they asserted that the larger the trade over what would be randomly expected, the larger the relative acceptance (RA),²⁹ and the more integration between the two countries. In the Savage-Deutsche model, differentials in relative acceptance are explained by economic (transportation and resources differences) and political (common cultural background, treaties, and colonial experiences etc.) factors (1960: 551-552).

This model was further developed by Russett (1967), who along with Savage and Deutsche, believed that the level of economic transaction flow can be a proper indicator of integration. However, he went much deeper in the sense that he identified a set of background conditions affecting the level of economic transaction flows. Russett (1967: 123-5)

suggested that cultural similarities, the nature of political bonds (e.g., converging or opposing) and the related external economic policies , and geographic proximity have major effects on commercial choice in terms of partner and commodity. These cultural and political background conditions continued to be singled out as important factors influencing the pattern of economic transactions not only in the Deutche-Russet transactionist model but also in the functional and neo-functional integrationist models.³⁰

Instead of relying on these background conditions, on the other hand, Rosenbaum and Taylor(1975:254-265) attempted to explain the pattern of economic relationships between countries from an alliance-system perspective. Specifically focusing on the pattern of interactions among developing countries, they argued that relations vary according to association with different political subsystems and the dominant political system. By dividing the current international system in terms of intra- vs. extra- dominant systems and sub-systems, they asserted that developing countries belonging to the same dominant or sub-system are likely to engage in more cooperation and thereby a higher level of economic transactions. For example, North Korea and Brazil are very unlikely to engage in a high level of economic relations because they belong to the different dominant systems as well as sub-systems, North Korea being an ally of the Eastern bloc located in the East Asian subsystem, while Brazil an ally of the Western bloc

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in the South America subsystem (1975: 253-5). However, they postulated that there has recently been an increase in the quantity and visibility of South-South relations and that this comparatively new phenomenon is the result of a decline in great-power capabilities and the loosening of the alliance system which in turn allowed developing countries to re-interpret their interests and policies and³² to take initiatives to pursue such interests.

While Rosenbaum and Taylor emphasized system-level political impacts on the pattern of trade and capital flows, Polachek (1980: 550-78) and Arad and Hirsch (1981) tried to examine the statistical relationship between conflict or hostility and trade patterns (trade creation and diversion / trade level) between a dyadic pair of countries.³³ For example, Polachek's hypothesis is that "dyads with the most trade are expected to exhibit the least conflict (and most cooperation)" and vice versa (1980: 560). And he gave the following rationale for this formulation: " --Greater levels of conflict make conflict more difficult. Reasons include retaliatory tariffs, quotas, embargoes, and other trade prohibitions. Conflict thus raises the cost of trade, thereby making at least one of the countries worse-off (in a welfare sense). The implicit price of being hostile is the diminution of welfare associated with potential trade losses." (1980: 560) Explicit in the above argument is that the level of conflict and cooperation directly affects the terms of

trade.

Combining some of the above arguments, Pollins (1982; 1983) under the Globus Project of the Berlin Science Center recently attempted to model bilateral trade flows in six commodities between twenty five countries. His basic contention was that " dyadic as well as historical, cultural, geographical and perhaps contractual relations will lead each buyer to discriminate between goods in a particular market according to their country of origin (1982:6-7)." Specifying each bilateral trade flow, Pollins (1983:13) identified five major political determinants: 1) the nature of external behaviors measured by friendly or hostile actions of one country toward another, 2) the general political affinity or enmity between two countries, 3) co-membership in an economic union such as the EC, LAFTA, or COMECON, 4) linguistic, cultural, or former colonial ties, and 5) geographic distance separating them.

Critique: The ecological or environmental explanation of bilateral economic relations, which comprises a wide range of divergent and convergent assertions, provides us with a set of implications for the systematic understanding of inter-South bilateralism. First, the direction of trade and capital flows of developing countries is more likely to be shaped by the nature of their ties with developed countries or the international economic system. Given the existing zones of influence and the resulting pattern

of a hierachical North-South relationship, developing countries tend to involve themselves in economic transactions more with developed countries than with other developing ones. Second, the degree or extent of inter-south bilateral relations appears to be influenced by geographic distance, political similarity, and socio-cultural homogeneity. Usually these factors in commonality lead to regional integration schemes such as customs unions and free trade zones under which bilateral ties are promoted. The volume of trade and capital flows into other developing countries located beyond certain regional contexts is expected to be low due to various institutional and policy barriers. Third, the pattern and content of these inter-regional trade and capital flows is affected by the nature of external alliance relations and the intervening and mediating roles of core countries or their transnational actors such as the multinational corporations.

Viewed from this perspective, the pattern of economic interactions between the East Asian NICs and the Middle Eastern OPEC countries, the primary unit of inquiry in this study, should be neither convergent in direction, nor high in volume. It is not only because these two groups of countries are geographically far away, but also because there is a very low degree of mutual complementarity in background conditions. These two regions have had different historical and colonial experiences, and lack

socio-cultural homogeneity (one belonging to the Chinese socio-cultural sphere and the Japanese zone of influence and other to the Islamic culture and the Franco-British zone of influence).³⁵ At the same time, the level of transaction and of mutual knowledge is extremely low. No previous or current attempts to set up an integrative scheme can be found. There is a low degree of political similarity between these two groups of countries as they are constituted by various heterogeneous countries ranging from traditional monarchical regimes to socialist revolutionary regimes. Furthermore, these two regions maintain loosely defined alliance connections, and the level of conflict and cooperation in the direct terms is totally non-existent except for some diplomatic entanglements around the Arab-Israeli conflict. Again given this ecological consideration, the level of economic interaction between the East Asian NICs and the Middle Eastern oil producers should have been very low or non-existent, which is quite contradictory to the empirical findings provided in Chapter One.

This grave incongruity of ecological models with actual reality is largely a function of their reliance on aggregate data analysis based on static circumstantial conditions. Ecological variables may offer a set of parameters conditioning the pattern of trade and capital flows among developing countries, but not causally determine their direction, volume and composition. These environmental variables are simply a set of input factors

to be translated into actual decisions and behaviors of the private businessmen and governmental officials. Thus these variables should be interpreted and re-interpreted within specific contexts of countries involved in dyadic interactions. To locate the causes, processes, and consequences of dyadic intreconnectedness, "one must examine pairs of states and avoid the ecological fallacy" (Holsti 1981: 28) of arguing that system properties or circumstantial conditions pervade the relationships in all dyads. Depending on the internal political and economic conditions and on the nature of the state and private business' objectives, external ecological variables may turn out to have quite different policy outcomes (i.e., direction, volume, and composition) that cannot be properly explained by the present models. Indeed as in case of economic models of bilateral relations, the ecological perspective falls short in coming to terms with a set of dynamic factors directly responsible for the formation, maturing, and decline of inter-South bilateral relations.

Entrepreneurial Dynamism and Bilateral Ties

What is apparently lacking in these economic and ecological perspectives is an adequate identification of the actual agents which shape the process and outcomes of bilateral ties. Supply and demand-side effects and ecological variables are necessary but static conditions

whose impact on the nature of bilateral ties can be understood only in terms of images, perceptions, decisions, and actions of the actors involved in bilateral economic ties, whether they are private entrepreneurs or state traders.³⁶ Despite the importance of these actors, both economic and ecological explanations ignore or omit their role in explaining the direction, volume, and composition of bilateral economic flows. While in economic models, such actors are assumed that they are rational profit maximizers common to all countries, ecological models treat them as a partial factor as discussed in terms of the level of communication channels or business connections (Roemer 1977).

In reality, however, the role of these actors, particularly private entrepreneurs, is very important. Leibenstein emphasizes their role in explaining the pattern of market transaction by stating:

If all inputs are marketed and their prices are known, and if all outputs are marketed and their prices are known and if there is a definite production function that relates inputs to outputs in a determinate way, then we can always predict the profit for any activity that transforms inputs into outputs. If net profits are positive, then this should serve as a signal for entry into this market. The problem of marshalling resources and turning them into outputs appears to be a trivial activity. From this point of view it is hard to see why there should be a deficiency of entrepreneurship. The answer is that the standard competitive model hides the vital function of the entrepreneur (1968: 72).

Explicit in this statement is the importance of the entrepreneur in compensating for market deficiencies. In

the dynamic world of market exchanges, as a matter of fact, there is no such thing as perfect information on a set of demand and production functions and of prices. Imperfections and uncertainties prevail. It is much more so for the cases of developing economies and of market exchange relationships between them. The markets of developing economies provide very little information of this sort, and the perception of market opportunities and acting and deciding thereupon becomes more than a trivial task. Emphatically put, such entrepreneurial functions may become the crucial factors in reshaping the direction, volume, and composition of bilateral economic flows in the strict sense.

Theories of entrepreneurship have been developed within the framework of issues covering economic development but so far no theoretical attempts have been made to apply them to the study of bilateral economic flows.³⁷ Given the centrality of entrepreneurship in an integrated model of economic development (Schumpeter 1934: 34), however, it appears possible to apply theories to the object of our inquiry. According to Schumpeter, an entrepreneur is an innovative organizer of "new combinations of means of production" (1934: 34) whose major functions are: 1) to introduce a new good, 2) to open a new market, 3) to assure a new source of supply of raw materials or half-manufactured goods, and 4) to implement a new organization of an industry such as the creation of a monopoly position or the break-up of a monopoly position (1934:66).

In line with Schumpeter, but in more comprehensive manner, Kilby (1971) developed four categories and 13 roles to be performed by entrepreneurs. The first category is related to the exchange relationship of entrepreneurs whose major functions include: the perception of market opportunities, gaining command over scarce resources, the marketing of the product and responding to competition, and the purchase of inputs. The second entrepreneurial function comprises both the external political administration capabilities dealing with the public bureaucracy, concessions, licenses, taxes and so forth and intra-firm management of human resources and supply and consumer relations. The management and control of financial and production matters constitutes another important category of entrepreneurial functions. Kilby identified the technological function as the fourth category which involves acquiring and overseeing the assembly of the plant, industrial engineering, upgrading processes and product quality, and the introduction of new production techniques and products (1971: 27-28).

Although Schumpeter's and Kilby's descriptions chiefly concern the roles and functions of private entrepreneurs in the domestic economic setting, they offer rich implications for the study of inter-South bilateralism. For example, a private entrepreneur's ability to perceive and monitor new markets in other developing countries and to come up with new products and new processes of production

can significantly affect the direction, volume and composition of bilateral economic flows. This is particularly true given the fact that most developing countries suffer from entrepreneurial scarcity and thereby from a low level of market and product information exchange (Hirschman 1958: 16-19; Myint 1966:173; Meier and Baldwin 1957:299). If private entrepreneurs in a dyadic pair of countries involved in mutual market exchange are competent enough to monitor information on new demands more effectively and to develop corresponding products, the level of bilateral ties between the two countries should be higher than it would otherwise be. Thus the monitoring function of private entrepreneur in a bilateral setting is one of the crucial factors influencing the nature of dyadic economic transactions between two countries.

The perception and monitoring of new markets by itself may not adequately promote bilateral ties. Perception should be translated into specific market acquisition. At this point the second important entrepreneurial function comes into play in the context of inter-South bilateralism: market penetration and setting up of solid business connection.³⁸ In many cases, new markets in developing countries are not easy to develop by other developing countries' firms. This is true either because local businessmen under the umbrella of import protection or tied to multinational firms from the core countries maintain monopoly or oligopoly market structures for certain

commodity markets or because consumers as a whole may have a bias against goods and services originating from other developing countries. In this sense, effective market penetration into other developing countries, in addition to the timely monitoring of new markets, is determined by the eventual shaping of the nature of bilateral ties between the two countries. In other words, breaking-up the existing monopoly or oligopoly structure, transforming the consumer or buyer's image of goods and services to be sold, and consequently increasing the market share emerge as important tasks for private entrepreneurs.

This market penetration task involves a number of entrepreneurial functions such as flexible price-setting,³⁹ aggressive corporate strategy, co-opting local buyers or agents in terms of side-payments, kick-backs, persuasion, and a mix of other tactics to gain market entry and to increase market share.⁴⁰ However, this supply-side unilateral approach to new market alone does not solve all the problems. Above all, this unilateral approach should be matched with the profits for or other motivations of the demand-side entrepreneurs. The complementarity between these two types of entrepreneurs should be more than that which can be found in an auction market.⁴¹ It should be enduring and solidified in terms of a tight business bond between the two in order to promote continued business cooperation in other market areas. In addition, these business ties should be correct in the sense that supply or

demand-side entrepreneurs find well-placed and efficient counterparts in their business transactions. This is particularly so given the fact that in the developing countries' market context information is very unevenly distributed among private entrepreneurs and correct business connections are essential to the timely and effective acquisition of such information and acting on it.⁴²

Effective market penetration and the establishment of firm business connections are in turn contingent upon entrepreneurs' ability to deal with governments of both sides. This political management capability constitutes the third important element of private entrepreneurship affecting the level of bilateral economic flows. In most developing countries, governments tend to monopolize all the necessary information on new markets or new demands since a great portion of market demand comes from the public sector.⁴³ In addition, governments directly or indirectly are involved in the regulation of the market in general and of the behaviors of private entrepreneurs in particular by issuing licenses, imposing taxes, and making concessions etc. Or in many cases, governments themselves become traders in terms of public enterprises. Given these crucial roles of governments, private entrepreneurs should know how to handle the bureaucrats in charge not only to tap new market information but also to ensure the smooth functioning of market entries, payments, and other necessary (or unnecessary) regulations. In many cases, of

course, local business partners handle these domestic problems. However, for new market demands which emanate from the state authorities for large scale infrastructure projects in the service sector such as the construction of roads, dams, ports and schools, supply-side private entrepreneurs must directly encounter governmental officials in order to settle any possible business entanglements.

This may be done through lawfully established channels as in the advanced industrialized countries. Often, the relative position of supply-side entrepreneurs may be enhanced vis-a-vis host governments by diplomatic support of the investors' governments. In reality, however, these two options are rarely workable in the context of developing countries. More aggressive cooptation and covert persuasion are needed to buy "official favors" from host governments. In so doing, the deployment of various non-conventional means of entrepreneurship becomes essential from time to time. These often include bribery and side payments of all sorts. In "dependencia" jargon, supply-side entrepreneurs must set up a "tri-pe" coalition with the host government (or state) and local counterparts to initiate market penetration and to expand market share (Evans 1979).⁴⁴ Viewed from this perspective, the political management capability of both entrepreneurs can be very critical in the final shaping of the direction, volume and composition of bilateral economic flows between

any dyads.

This private entrepreneurship approach to the study of bilateralism complements the economic and ecological models in a very important way. By placing entrepreneurial functions at the center, it activates the static causal or background conditions and helps us to understand the pattern of bilateral economic flows more dynamically. When private entrepreneurs monitor or perceive new market opportunities (i.e., demand-side effects) and decide to penetrate these markets, they must rationally assess the organization of supply-side capabilities and evaluate the ecological variables. In this sense, private entrepreneurs become integrative monitors, organizers and performers configurating these three clusters of variables (i.e., supply-, demand- side, and ecological). For example, if Northern industrial countries raise tariff and non-tariff barriers, private entrepreneurs will seek markets in Southern developing countries where protective barriers are low and various incentives are provided. At the same time, if their home countries are on the verge of conflict with their host countries, private entrepreneurs will pull out of these markets and diversify into other markets where demand, supply, and ecological variables are more favorable. The entrepreneurial pursuit of profits then plays the crucial role in determining the nature of bilateral economic flows.

Indeed focusing on private entrepreneurship explanation is a great theoretical advance for the study of inter-

South bilateralism. Growing protectionism and tightened business opportunities in North, the opening of new markets in selected developing countries such as OPEC, and the increase in supply capability on the part of the NICs may have pushed private entrepreneurs in the NICs into OPEC markets. As a result, it may be expected that bilateral economic ties between OPEC and the NICs should be high.

In reaching this conclusion, however, one caveat is in order. The approach has not taken into account the relationship between private entrepreneurs and the state. In a laissez-faire market setting, private entrepreneurs may pursue whatever they want. However, where mixed economies are involved as in the majority of developing countries, the private sector cannot make independent and autonomous decisions. They are largely constrained and their decisions filtered through the objectives and preferences of the states on both sides of demand and supply. On the supply side, the private sector in the developing countries, especially in the external sector, is weak and fragile in terms of finance, organization, management and industrial capability. Unless governments become directly involved in facilitating these factors, thereby reducing production costs and enhancing international competitiveness, the private sector cannot⁴⁵ effectively penetrate the desired markets.

In addition, there is a growing tendency to politicize economic flows between a dyadic pair of countries whose

reach extends beyond the private sector. Political concessions, bargains, and advantages emerging out of the linkage between economic and political issues affect the level of the private sector's success in certain markets. An additional missing element in the private entrepreneurial model is the fact that the state's direct involvement in trade and capital transfer is ever increasing. Today not only socialist states but also capitalist developing as well as developed states directly engage in the actual exchange of goods and services by determining price and volume or by specifying destinations. Faced with these weaknesses and defects, we need to develop a more viable theory of inter-South bilateralism.

Toward an Integrated Theory of Bilateralism:

The State Entrepreneurship Perspective

The three perspectives described in the previous sections, namely the economic, ecological, and entrepreneurial models, are not mutually exclusive, but supplement each other in explaining the phenomenon of bilateral economic flows. Diagram 2-1 is a schematic presentation of such an integrated model which is composed of four modules: demand, supply, ecological, and entrepreneurial. A basic theoretical assertion which can be derived from this model is that the pattern of bilateral economic ties is a function of the level of the

complementarity in demand- and supply-side effects and ecological variables , and of the nature of the private entrepreneurship involved.

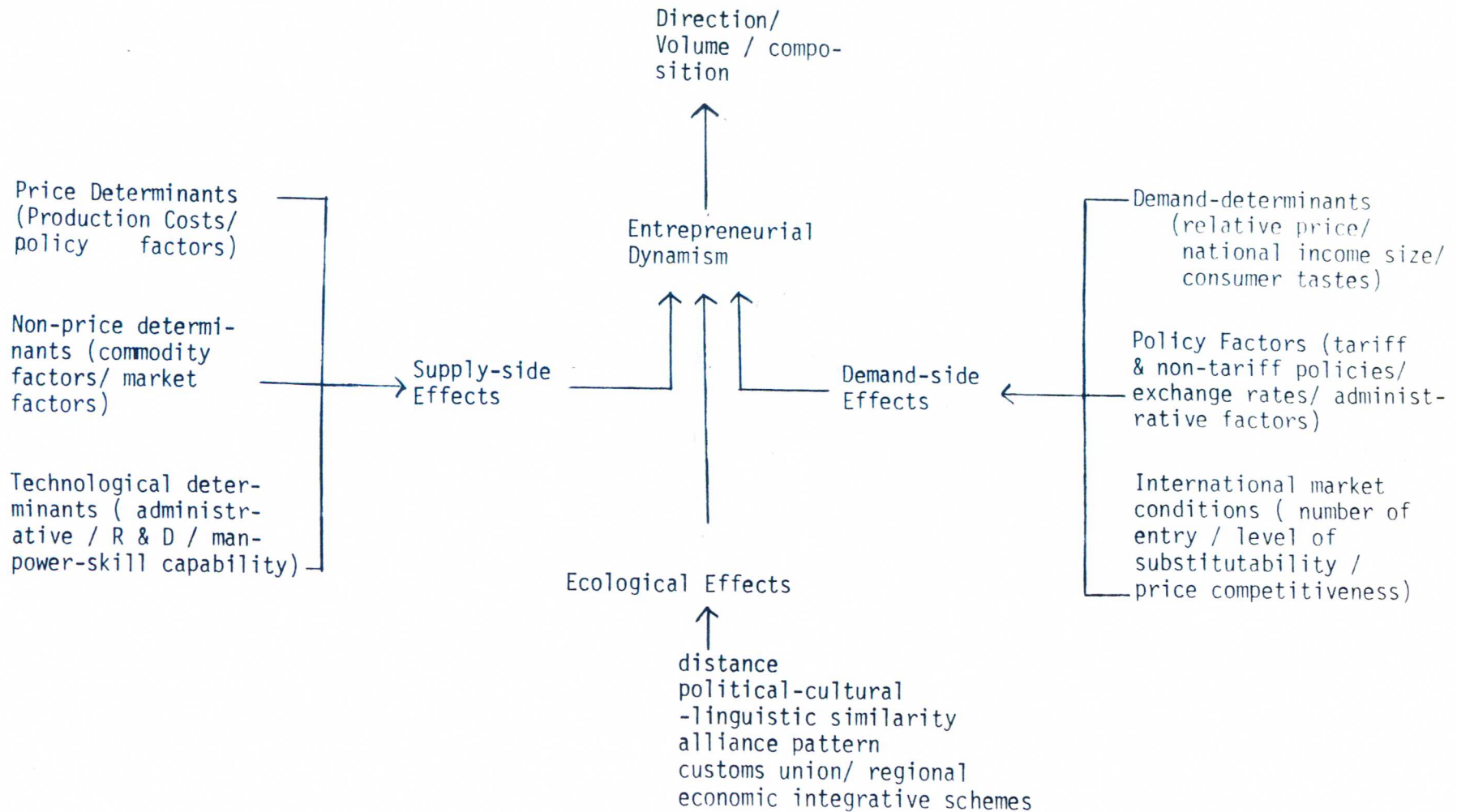
Diagram 2-1

As we have already noted, this way of conceptualizing the empirical universe (i.e., inter-South bilateral ties) entails a serious theoretical and empirical problem. The problem comes from the inability of these four variables (demand, supply, ecological, and private entrepreneurial) to qualify as the appropriate independent variables. In order for these variables to explain or predict the direction, volume, and composition of bilateral economic flows, they themselves need to be explained by something else.

For example, the supply-side module is composed of three sub-modules: price determinants, non-price determinants, and technological determinants. None of these determinants are, however, endogenous to the market and require no further explanation. The price determination (production cost and extra-firm policy factors) itself is shaped by the nature of state intervention ranging from the direct or indirect control of labor, capital, and public utility costs to a set of public policies such as

Diagram 2-1

Existing Models of Bilateralism:
A Schematic Integration



trade, foreign exchange, and other macro-economic policies. Non-price and technological sub-modules are also subject to similar kinds of state intervention. Thus without clarifying the nature of state intervention vis-a-vis the supply-side module, the latter cannot properly qualify as an explanatory variable. The same can be said of the other three modules as were noted in the previous section.

The important point here is that the aforementioned four variables do not causally determine the nature of bilateral economic flows by themselves. They serve as necessary conditions to the analysis of inter-South bilateral relations (with a partial exception of private entrepreneurship)⁴⁶ whose explanatory contents can be meaningful only in relation to the nature of state intervention revealed in specific cases of bilateral economic ties. To put it differently, the basic theoretical contention to be explored in this section is that inter-South bilateralism can be better explained by carefully examining the nature of state strategy or entrepreneurship deployed which is based on the state's careful monitoring and rational calculation of changing market conditions, non-economic circumstantial constraints and opportunities and on the effective utilization of private entrepreneurship to accomodate the state objectives. To carry this point further, it may be argued that the rise and expansion of inter-South bilateralism is neither a natural extention of economic interdependence between a

dyadic pair of countries nor the deterministic outcome of the nature of these countries' integration into the international division of labor.

Why this concern about state objectives? What is the rationale behind organizing the state as the primary unit of analysis in the study of inter-South bilateralism? What characteristics make the state in question so central to our present inquiry? Wasn't the state downgraded as one of many competing actors on domestic and international political scene with the recognition of the spread of complex interdependence?⁴⁷ Or to borrow another argument, isn't the state simply a mere reflection of what is going on in the system, whose policy outcomes are wholly dictated by the internalization of systemic factors (e.g., logic of world capitalist system)?⁴⁹

My assertion is that the state is not merely a concept whose role is determined by dominant class interests tied to the international division of labor, nor can it be placed along a continuum of tiny domestic and international actors such as interest groups, companies, and labor unions. As Krasner (1978:33) succinctly argues, the state as an autonomous actor pursues goals associated with the general interest of the society. This goes beyond the Smithian minimalist vision of the state whose functions are limited to providing collective goods and infrastructures (neutral administrative, institutional and physical) enabling the market to function. Whether it relates to power, stability, welfare, or security, the

state as an autonomous realm of public authority creates and maintains national or public interests that cannot be reduced to the narrow interests and goals of any group or coalition (Stephan 1977 ; Krasner 1977 ; Smith 1979; Nordlinger 1981).

Nor is the state " an executive committee for domination by ruling class" as instrumentalist Marxists claim.⁴⁰ In her recent study of macro social change in China and Russia, Skocpol (1979) argues that "any state first and fundamentally extracts resources from society and deploys these to create and support coercive and administrative organizations" (1979:29) which in turn enable it to act against the preferences and wills of the most powerful societal actors. In her view, the state is far from being absorbed into society and maintains a more fundamental interest than that of the dominant classes.⁵⁰

Even for some Marxists, this instrumental vision is flatly rejected. Presenting a new concept of the 'relative autonomy' of the state, Poulantzas(1974) asserts that the state in the capitalist mode of production has an objective function to perform in manipulating social cohesion so that capital accumulation can proceed unhindered. The overall capitalist system needs 'autonomy' of the state in order to handle various contradictions inherent in the system in a more flexible and adaptable manner. Yet its autonomy is relative in the sense that the basic 'template' or socio-economic context of the capitalist mode of production

limits the parameters of variation in state policy formation. In other words, capitalism is neither self-regulatory nor self-sufficient. Its characteristics are manifested in terms of successive contradictions and crises. Without adequate state intervention, these contradictions and crises weaken the legitimation of the state, threaten the very foundation of the capitalist system and interrupt the accumulation process. In this sense the state can function on behalf of capital only if it can equate the needs of capital with the national or public interest and secure popular support for measures that maintain these conditions necessary for accumulation while respecting its private sector (Offe 1975; Offe and Range 1975).

For all the theoretical differences and the alleged epistemological incommensurability of the above critiques of the conventional notion of the role of the state in the capitalist system,⁵¹ they share a common tone in reaching the following set of assertions:

1) The state has its own autonomous objectives and preferences which could either converge with or diverge from those of the social forces.

2) The state is endowed with a set of intrinsic and autonomous capabilities described as insulative (Krasner 1977), extractive (Skocpol 1979), regulative or balancing (Poulantzas 1974; Offe 1975; O'Connor 1974), and facilitative or accumulative (Hirschman 1979, Frank 1980, Baran 1956) in translating its objectives and preferences into authoritative policy outcomes and implementing them.

3) The state's preferences, decisions, and actions are, however, not totally free from a set of interactive or structural constraints. The state's behavior is constantly conditioned, if not determined, by internal and external constraints.

Although this way of conceptualizing the nature of the state derives from public and foreign policy debates in advanced industrial countries,⁵² it finds a convenient theoretical application in the case of developing countries. Relatively speaking, the state in developing countries has much clearer objectives and preferences or at least a stronger necessity for articulating them than developed countries mainly because of situational imperatives. Economic backwardness, ethnic fragmentation, external and internal fragility, and chronically pervasive distributional inequality in developing countries shape the state's objectives (i.e., growth, integration, security, stability, and redistribution respectively). Preference ordering out of this matrix of objectives is also done more discernably since the ordering itself is so closely and explicitly tied to the legitimation and the survival of the state.⁵³

Second, the state in developing countries, defined here as public authority and its occupants whose core is executive authority or political leadership in power,⁵⁴ appears to take more autonomous decisions and actions than in advanced industrial countries because of the enormous concentration of power. Viewed from Myrdals' observation of hard and soft states in developing countries, it could be a controversial argument.⁵⁵ From an empirical point of view, however, the structure of public authority in developing countries represents concentrated power,

dominates private-civil society, and is active interventionist rather than neutral and arbitratative. This is so either because the authoritarian and coercive form of governance easily allows the "statization" of society (O'Donnell 1974), or because of the historically and cuturally structured concept of political community which facilitates such power concentration, as can be seen in the idea of organic corporatism (Stephan 1977). Or it may be due to situational imperatives such as the necessity for rapid growth or radical redistributive reforms both of which require the heavy centralization or monopolization of coercive power and resources in the hands of the state. On this aspect of the state's role in developing countries, Tony Smith provides a concise description:

State power must be both concentrated and expanded in a complex process that will depend in each case on specific configurations of social forces. Different regimes will choose to promote different sectors of their populations, and a variety of political structures may be used to the same functional ends. **But the final product must be a state apparatus that can effectively knit together the social forces under its jurisdiction, and provide for future growth** (1979:281 my emphasis).

The two characteristics listed above, namely the autonomous realm of state preferences and power concentration in executive authority, in turn are apt to make the state in developing countries more interventionist vis-a-vis the market and the national economy. Rather than leaving the market untouched as in a classical laissez-faire setting, the state politicizes as well as depoliticizes it

to serve the state objectives as they are perceived. When rapid economic growth is perceived to be a crucial political objective, the state attempts to depoliticize and insulate the market and private sector from the immense swirl of competing social forces. On the other hand, if the pursuit of rapid economic growth becomes a destabilizing force undermining the legitimacy of the state, the state may politicize the market and the national economy in terms of bargaining and concessions so as to enhance equity and redistribution (Hirschman 1979; Olson 1964; Illchman and Uphoff 1969). In this sense, unlike most advanced industrial countries, developing countries lack a clear demarcation between the state and market. This lack of the clear division of labor between the state and the market, which might be a reflection of relative weakness of the private sector, tends to place the state in the position to command, coordinate, and tame the market and the national economy as it feels necessary.⁵⁷

This interventionist nature of the state offers an important implication for our inquiry. That is, foreign economic relations in general and inter-South bilateral ties in particular are subject to the intentions, calculations, and the decisions of the state. This increasing state intervention in external economic relations is well summarized by Zysman:

Nation states increasingly act to control and direct trade, conducting exchanges and directly influencing patterns and terms of exchange, rather

than simply maintaining a system for private trade. These direct and political arrangements have moved the state to the center of the stage (1977: 265).

It is from this observation that we come to an assertion that inter-South bilateralism is largely a function of foreign economic policy of the state. Of course, this is not to deny the essential role played by private entrepreneurs in shaping the nature of bilateral economic flows. As discussed earlier, they are an important agent, but not an exclusive one. Furthermore, the scope, direction, and mode of their business conduct in the bilateral setting can be understood only in relation to the nature of foreign economic policy pursued toward a specific target country and in a given time framework. This is mainly because their perceptions, decisions, and actions in choosing partners and commodities are filtered, managed, and directed by the state authorities especially in the case of developing countries.

The above discussion now helps us to identify a set of research tasks in locating independent variables accountable for the rise and decline of inter-South bilateralism. The first task is to investigate the variables affecting the nature of foreign economic policy-making in a given country and its relationship to the choice of inter-South bilateralism. The task of elucidating this cluster of variables may be done by identifying the following factors:

First, what are the internal and external conditions

affecting foreign economic policy-making? More specifically what kinds of systemic constraints and opportunities do decision-makers face and what are their domestic consequences and how do they affect the structure and process of foreign economic policy-making?

Second, these internal and external conditions are not straightforwardly translated into policy outcomes or strategic choices. They are filtered through images or perceptions of authoritative decision-makers with regard to a set of state objectives situationally defined and the availability of domestic resources and strategies to cope with the constraints and to exploit the opportunities. This in turn requires us to examine the decision-making structure (i.e., perception, assessment, and strategic choice) which leads to the selection of inter-South bilateral policies vis-a-vis a specific target country.

Third, although state autonomy has been assumed, the decision structure leading to the choice of inter-South bilateralism is not totally free from domestic political constraints. The domestic political structure conditions, if not determines, such a decision structure. Thus, it is necessary to discuss the pattern of power distribution among major social forces and to trace the nature of the relationship between their interests and the state's choice of an external partner in a bilateral setting.

The second major task is to delineate the nature of the state-business relationship in bilateral economic flows. Although the state may designate a specific target country

and commodity items with a view to diversifying external economic ties, such a strategic choice alone does not tell as much about the actual process of a bilateral tie. Of course, the state itself may intervene in such a process by playing such roles as trader, investor, and capital inducer. However, in many cases its magnitude is relatively limited, with the exception of centrally planned economies. Instead the state tends to utilize private entrepreneurs as dynamic agents in bilateral economic flows. Or private entrepreneurs themselves may directly initiate, promote or discourage such a process in consultation with public authorities of both countries. Thus, it becomes essential to examine the intentions, decisions, and behavioral modes of the private sector and its relationship with public authorities of both sides.

For example, what is the pattern of market penetration strategy and the receptivity to it in host countries? What is the nature of business connections between private entrepreneurs of both sides? What is the nature of the political back-up structure surrounding such a connection on both sides? To what extent is it effective in collecting information, expanding market shares and breaking up the existing monopoly structure? How or through what mechanism do private entrepreneurs manage their political connections? Do bribery, side payments, and other non-conventional instruments work in buying political influence for business interests?

The last crucial task in this inquiry is to spell out

various entrepreneurial behavior patterns (or policy mixes) employed by the state to promote or curtail bilateral economic flows. They are important not only because they shape the process and outcome (e.g., volume or contents) but also because they indicate a set of signals portending possible changes in the direction of bilateral flows. The state can deploy a wide range of entrepreneurial behavioral patterns to influence bilateral economic flows. These can be properly understood by examining the three major dimensions: the facilitative or coordinative function, the external political management function, and the insulative function.

The facilitative or coordinative function refers to a state policy behavior that enhances or facilitates any specific bilateral ties in terms of the provision of incentives or disincentives. For example, what kinds of supply-side incentive policies are deployed to promote a specific bilateral economic flow? More specifically, what sorts of taxation, administrative, financial, and other macro-economic policies are provided to boost international competitiveness in general and a specific bilateral economic flow in particular? The same can be applied to the demand side. What kinds of preferential treatment are extended to a specific supplying country in tariff and non-tariff policies? What sorts of administrative and taxation benefits are available to a specific economic partner? Are there any restrictive policies affecting market entry?

The second important function comprises a set of explicit political management policies of the partner country. This external political management involves diplomacy, bargaining, issue-linkages, bluffing and cheating, and political concessions, etc. For instance, a country may make a huge political concession to gain economic interest in the target country. Or a country may show political support over certain issue areas implicated by the target country. Sometimes the home country may extend a series of goodwill gestures by establishing a technical and educational assistance agreement with host countries to facilitate the market entry of its private sector. Likewise, a variety of explicit political management tactics to enhance a country's economic interests in the host countries could be introduced. The examination of these tactics and bargaining strategies will help us to understand the dynamic process and the outcome of bilateral economic flows.

The third major entrepreneurial function is that of insulating the bilateral selection and its promotion from competing internal and external political pressures and demands. The pursuit of preferential policies toward a specific country may incur political opposition from social sectors which would be deprived of benefits by such a choice. Alternatively enhancing supply-side competitiveness, the home country may involve suppressing wage costs or disproportionally allocating financial and

administrative resources to a certain private sector which the state favors. These kinds of discretionary policies and their implementation may bring about complaints from the labor sector and other affected social sectors. Such pressures may also come from external forces. For example, if dominant monopoly actors in certain developing economies' market are deprived of their market share with the new entry, they may use political influence directly or through their home countries' governments to deter or suppress the business activities of their competitors. If a certain country is able to insulate its bilateral choice from these internal and external pressures, the resulting outcome would be a high level of bilateral transactions with the target country on a continuous basis. If not, the level may be lowered. Thus, this insulative function of the state becomes an important variable to trace the outcome of bilateral economic flows.

To summarize, this statist model of bilateralism starts with the three basic assumptions: 1) the state in developing countries is autonomous and interventionist: 2) the state is a unitary rational actor, ('unitary' in the sense that the state is conditioned by competing domestic political claims, but not mechanically determined by them, and 'rational' in the sense that the state calculates the costs and benefits in line with a set of objectives and preferences with expected pay-offs) : 3) the nature of inter-South bilateralism is thus largely a function of foreign economic policy (or rationally caculated state

stragety) of the state.

Diagram 2-2

A schematic presentation of this statist model based on these three assumptions in Diagram 2-2 provides us with five major assertions which will guide our inquiry by linking the existing theoretical models (i.e., economic, ecological, and entrepreneurial) in a coherent and comprehensive manner. Those assertions are:

Assertion 1: The rise of inter-South bilateralism is a function of the state's strategic choice evolving out of the interplay of the decision structure and surrounding internal and external constraints and opportunities.

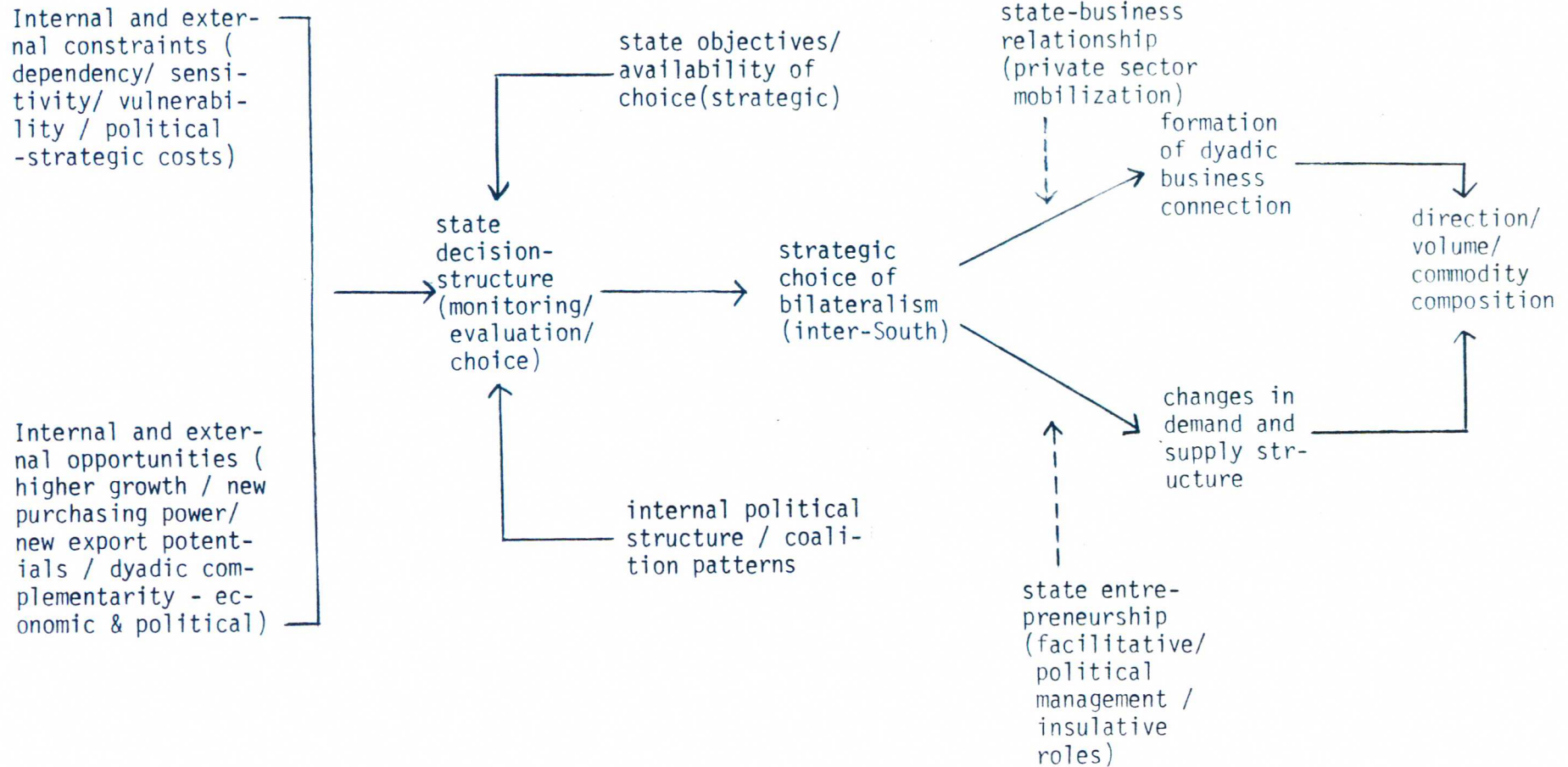
Assertion 2: The channel and process-level dynamics of inter-South bilateralism is a function of the state-business relationship in general and the nature of the business connection in particular.

Assertion 3: The outcome of inter-South bilateral economic flows is largely a function of the level of complementarity in entrepreneurial functions (facilitative, external political management, and insulative) deployed by the states involved.

These assertions are mere conjectures yet to be tested. As a way to test or explore the theoretical viability of these assertions, this study presents a case study : bilateral economic relations between Saudi Arabia and South Korea 1973-1983. The rationale behind this methodological choice stems from the fact that the empirical universe (i.e., inter-South bilateralism) is yet to be firmly

Diagram 2-2

Statist Model of Bilateralism:
A Schematic Presentation



structured and that it might be better explained by examining the micro-level working mechanisms of a single case, rather than an aggregate data analysis.⁵⁸ We are aware of the pitfalls of using a case study in testing theoretical assertions. However, the aim in this inquiry is not to confirm or generalize the theoretical construct, namely statist model of bilateralism, from a single case. Its aim is to further explore the viability of the theoretical conjectures made above and to open a new horizon of understanding the foreign economic behavior of developing countries. It is our belief that an empirical demonstration from a single case, though narrow, can serve the purpose of our inquiry.

The case of Saudi Arabia and South Korea has been chosen chiefly because of its salience. As illustrated in the empirical data in Chapter One, there is a high concentration of bilateral economic flows between these two countries. This salience, which implies a solid case of inter-South bilateralism, induced us to select the Saudi-South Korean connection as the primary unit of investigation. Of course, this salience may lead us to speculate that the case might be "unique" or "deviated" from the standard cases. Given the immaturity of the phenomenon in terms of the empirical contents (e.g., volume), however, this deviated case may be able to offer us a better proto-typical scheme by which we can measure the distance of deviation from other yet-to-mature cases.

The following Chapter deals with empirical dimension of the Saudi-South Korean connection in terms of volume, composition, and gains and losses. Chapter Four focuses on the interface between decision structure and internal and external constraints and opportunities and traces the causal structure responsible for the rise of the Saudi-Korean connection. Chapter Five examines the nature of the state-business relationship in both countries, the resulting formation of business connection, and its impact on bilateral tie. Emphasis will also be placed on corporate strategies and entrepreneurial behaviors such as corruption, bribery, and other non-conventional business practices through empirical case studies. Chapter Six devotes to the analysis of entrepreneurial functions deployed by both states in promoting their connection. This chapter mainly centers around the examination of various policies employed and some empirical cases related. Chapter Seven, as a way of concluding this inquiry, discusses the general theoretical and empirical implications drawn from this case study and briefly tries to project the durability and pervasiveness of inter-South bilateralism in lieu of the Saudi-Korean connection.

FOOTNOTE

1. Bilateralism is usually understood as a pattern of economic relations between a dyadic pair of countries governed by a set of rules, norms, and procedures intentionally agreed upon between the parties concerned. The principle of reciprocity, barter arrangement, and other formal institutional agreements between two parties are designated as components of bilateralism. In this research, however, the notion of bilateralism is broadly defined in such a way that any economic transactions between two countries, be it via institutional arrangements or market, are bilateral as long as they are not tied to explicit multilateral arrangements.
2. In a realistic sense, all the economic transactions are virtually bilateral when they are disaggregated.
3. Theories of international economy begun with comparative advantage are not limited only to international trade. They are now being applied to international factor movement (Ozawa 1979; Purvis 1972, 991-999; Schmitze and Helmberger 1970, 791-797; Mundell 1957, 321-335; Rybczynski 1955, 336-341) as well as to services sector (Lutz and sapir 1981, 1983).
4. Other assumptions include: constant returns to scale, a common world stock of knowledge and a standard technology, and identitital consumption tastes. As shall be discussed in the following section, this static theory of comparative advantage is substantially modified complementing various drawbacks in these assumptions. For a brief discussion of this topic, see Kindleberger (1973: 53-69) and Kreinin (1978: 214-253).
5. For a succinct discussion of the directions of trade, refer to Havryshylyn and Wolf (1981: 6-10).
6. Keesing (1978:15), Hughes (1980), and Rhee and Westphal (1980) offer a similar finding.
7. For this, refer to Samuelson's extension and modification of idealistic assumptions of the Heckscher-Ohlin theorem : the conditions of competitive equilibrium with many traded goods and services / the effects of various domestic distortions and imperfections including monopoly power and fixed factor payments/ the effects of distortions stemming from tariffs and quantitative restrictions / the implications of trade for outputs of non-traded goods and customs unions. See Baldwin and Richardson (1974) and Kindleberger (1973).
8. For a detailed discussion of product cycle theory, see Vernon (1966: 190-207), Vernon (1970), and Wells (1972: 3-33).

9. Besides aforementioned technology factors, R & D factor, economies of scale, and industrial policy etc. are regarded as variables affecting supply-side competitiveness of international trade. For this topic, see Watanabe (1966), Kindleberger (1973: 53-69), and MITI (1977).
10. On the issue of complementarity vis-a-vis competitiveness of intra-South trade, refer to Amsden (1976; 1980).
11. For an overview of demand side theories of international trade, refer to Kindleberger (1973: 35-52).
12. As shall be discussed in the following section, international relations scholars have mainly focused on this demand side of international trade as a primary unit of analysis. See Pollins and Kirkpatrick (1983).
13. Demand inelasticity of import of OPEC countries is certainly a function of enormous oil wealth accumulated since the first oil crisis. However, recent oil glut and diminishing oil revenues for these countries are imposing various constraints on demand pattern.
14. This is borrowed from Pollins and Kirkpatrick (1983: 18)'s discussion of Armington (1971).
15. State intervention in foreign trade is not unique to developing countries. The states of OECD countries show a similar pattern of intervention to a varying degree. Katzenstein (1977) provides different patterns of state intervention in foreign trade among advanced industrial countries.
16. Balassa (1981) offers a succinct description of developing countries' export promotion policies. Haggard (1983) and Haggard and Moon (1983) also discuss the patterns of state intervention in foreign trade in selected NICs.
17. A typical case of state trading can be found in COMECON member countries, whose trading pattern is chiefly based on barter arrangements. For the practices of state trading in advanced industrial countries, refer to Zysman (1977).
18. "Ecological" connotes environmental factors affecting the patterns of economic transactions.
19. For this issue, refer to Poyhonen (1963: 93-99), Kuznets (1964: 1-106) and Kindleberger (1973: 89-106).
20. SARUM is an abbreviation of Systems Analysis Research Unit Model. The significance of this model consists in the fact that it incorporated non-economic factors into a pool of variables affecting the direction of trade along with economic factors such as relative prices and income.

21. The major drawback of previous models of bilateral trade flows is that although they recognize the importance of non-economic variables, they do not specify the political contents of 'bias' co-efficients by treating them as 'dummy' variables. For a concise critique, refer to Pollins (1982; 1983).
22. Classical cases of dyadic pairs within the zone of influence can be found in pairs such as Korea-Japan, Algeria-France, and Philippine- Amercia etc.
23. For a comprehensive discussion of dependencia, world system, and power-exchange theories, see Caporaso (1978:130-143).
24. There is no a single unified theory in explaining the pattern of dependency in the North-South relationship. At least, three versions within the same tradition can be delineated: unequal exchange school following the lead of Prebisch (1954) and Singer (1966), classical dependencia school under the influence of Frank (1969) and Baran (1956), and finally a revisionist view expounded by Cardoso and Faletto (1979) and Evans (1979). For a general overview, see Palmer (1977) and Chilcote (1981).
25. Regarding the thesis of hegemonic stability, refer to Kindleberger (1974), Gilpin (1975), Krasner (1976 :317-347), and Koehane (1980:131-162).
26. On the monopoly structure of the world capitalist system and its impacts on inter-South economic intercourse, there are diverse opinions. For a factual survey, see Havrylyshyn and Wolf (1981: 5-19).
27. Galtung (1971:89) is a perfect example where the relationship between peripheries is blurred. The same drawback can be found in world system theory (Wallerstein, 1974).
28. These issues constitute the core of the NIEO debates. For an overview of this topic, refer to Savaunt (1982).
29. Relative Acceptance is defined as an expected value of trade between two countries where the proportion of country i's exports which go to country j will correspond to the mean of the proportion of i's exports in all world exports and j's import in all world import (Savage and Deutche 1960: 551-2). For an application of this model, see Alker and Puchala (1968: 315).
30. Major common background conditions include: social and cultural homogeneity, political attitudes or external behaviors, a network of supranational or inter-governmental and political institutions, and geographic proximity (Russet 1967: 123-5). For a critique of these background conditions, see Myltelka (1973).
31. Rosenbaum and Taylor make a dualistic argument. According to them, while the nature of the East-West system (dominant system) shapes political parameters of inter-South interactions, a

central dimension of South-South relations is that they are normally determined by North-South relations (1975: 244).

32. In a sense, their argument resembles to structural balance theory which refers to a greater inter-alliance conflict will produce a greater intra-alliance cohesion, both strategically and economically (Hoppmann 1967: 212-236). Also refer to Sullivan (1976: 226), Coser (1956:88), and Simmel (1955:92-93).

33. While Polachek concerns about the reciprocal relationship between dyadic conflict-cooperation and trade ties, Arad and Hirsch (1981) attempt to measure the effects of a cessation of hostilities between two countries upon trade creation and trade diversion. Besides trade area, a number of studies has been made to trace the relationships between political instability and direct investment in terms of political risk analysis (Kobrin 1980, 1982; Sneider 1984).

34. His model is a partial modification of Armington (1971)'s.

35. As shall be discussed in Chapter 5, the intermediating role of the US as a hegemonic power should not be overlooked in linking OPEC countries and East Asian Nics.

36. The rationale behind distinguishing private and state entrepreneurship comes from the fact that the state in developing as well as developed countries acts like an entrepreneur. Thus, our position here is that the notion of state entrepreneurship goes beyond the traditional definition based on the state ownership of the means of production. It connotes profit or interest maximizing behaviors of the state in lieu of capital accumulation or welfare protection. For a related discussion, refer to Haggard and Moon (1983), Kaminski and Moon (1984), and Moon (1984).

37. Traditional approach to private entrepreneurship chiefly focussed on risk-taking behaviors of entrepreneurs (Baumol 1968: 68). But few paid attention to external economic aspects of private entrepreneurship.

38. This business connection can be compared with the notion of elite socialization, though different in form and substance. For the concept of elite socialization, see Nye (1971: 69-73) and Lindbergard and Scheingold (1969).

39. "Flexible" in the sense that entrepreneurs do not necessarily pursue profit-maximization or risk minimization behaviors in setting prices. Rather with the perception of uncertainty condition, they set the prices more flexibly.

40. They include advertisement, public relations, and after-services etc.

41. The essence of auction market is chaotic, undifferentiated, and one-shot, while routine business connection is durable,

orderly, and highly differentiated.

42. Since open bidding for procurement or project contract is quite infrequent and the nominated bidding is a routine form of business in many developing countries, the accessibility to information becomes the key criterion on which business partner or sponsor is selected. Chapter Four will discuss this aspect of business practice in Saudi Arabia.

43. For example, in the case of Saudi Arabia about 90% of business transactions is government related. Many OPEC countries show a similar structural pattern.

44. For an interesting discussion of this topic, refer to Jacoby et.al (1977).

45. A similar role of the state can be applied to advanced industrial countries. In particular, France and Japan among them reveal this mercantilist policy attitude (Zysman 1977; Johnson 1980; Pempel 1977).

46. Private entrepreneurship is an exception since it serves as a sufficient condition to the shaping of bilateral economic ties between a dyadic pair of country by directly involving in the process-level dynamics.

47. This view of the state is held by interdependence theorists. See Cooper (1968), Morse (1969), Koehane and Nye (1977), and Rosecrane (1979).

48. This view has been advanced by the first and second generation dependencia and world system theorists. Refer to Frank (1969; 1980) and Wallerstein (1974; 1979) as exemplar works.

49. For a comparative and comprehensive debate on the nature of the capitalist state, see Stephan (1977), Held (1983), Jessop (1981), and Crouch (1978).

50. This structuralist version of Marxism can be found in Gramsci (1971), Althusser (1967), and Poulantzas (1974; 1975). For a comprehensive review of this version, refer to Jessop (1976; 1981). Hamilton (1980) attempts to apply this version to the case of Mexico.

51. This incommensurability is elegantly discussed in terms of the whole and parts relationship by Olmann (1974) and Unger (1975). Stephan (1977) is also a good source to consult with regard to developing countries.

52. The recent theoretical polemics on the nature of the capitalist state were a theoretical as well as ideological response to the changing characteristics of the state at a time of transition from the late stage of monopoly capitalism to welfare state in advanced industrial countries. However, this debate was

soon diffused into the Third World countries with the polemicization of dependencia paradigm. For an introductory overview of this topic, refer to Held (1983).

53. This preference ordering in the context of developing countries is well discussed in Uphoff and Illchman (1971), Rothchild and Curry(1978), and Almond (1971).

54. This is strictly a Weberian interpretation. See Krasner (1977:33) and Nordlinger (1981:25-26).

55. Myrdal (1968: 935) argues that most developing countries are 'soft' state in the sense that there is a huge gap between planning and implementation. However, his assertion does not seem universally valid. In terms of domestic political structure and potential for implementative capability, developing countries can be viewed as having 'hard' state, especially compared with advanced industrial countries where pluralism prevails.

56. On this 'late-comer' thesis, refer to Gerschenkron (1964) and Kurth (1979).

57. Of course, this does not mean that the state in developing countries are totally free from internal and external constraints. The state is constrained by a number of internal and external factors, but neither subjugated nor determined by them.

58. To borrow Lijphart (1971 : 691-693)'s justification, the case study method employed here may perform the functions of theory-confirming or informing within a framework of newly established assertions (or asserted generalizations) and of studying a single case that deviates from established generalizations.

CHAPTER THREE

THE SAUDI ARABIAN-KOREAN CONNECTION: AN OVER- VIEW OF HISTORICAL AND EMPIRICAL DIMENSIONS

The Background

South Korea (henceforth refered to as Korea except to distinguish the two sectors of the divided country) and Saudi Arabia are two extremely heterogenous countries. Geographically far removed from one another, they do not share any common political, cultural, historical, or economic denominators. Politically Saudi Arabia is a conservative monarchy where one family (the House of al Saud) rules the entire country. Islamic law (Sharia) provides all the societal rules, and political ideology is largely derived from Islamic precepts filtered through the fundamentalist Wahabbi tradition.¹ Political leadership is embodied by the monarch (Malik), supreme leader of the Islamic community (Imam al Mu'minien), and the de jure as well as de facto head of all tribal leaders (Shaikh al Mushayikh) (Spencer 1962: 308). There are neither formal electoral procedures nor political parties or interest groups in the Western sense.

Korea, on the other hand, is a secular state. Though limited by a number of authoritarian rules, political parties and interest groups and the their interactions shape the process and structure of Korean politics.

Political ideology in Korea is derived from a mixture of secular ideas and notions such as nationalism, modernization, anti-communism etc. Perhaps the single commonality between two countries may lie in the mode of governance through which political power is concentrated in the hands of executive authority and a bureaucracy.²

Culturally and historically a much wider gap exists between the two countries. While Saudi Arabia can be characterized by the interplay of Islamic and Arabic cultures, Korean culture represents a mix of Confucianism, Buddhism, Taoism, and even Christianity. There is no linguistic tie.³ Viewed from an historical perspective, nothing is shared between two countries. Until her formal unification and the creation of the Kingdom in 1932 by King Abdul Aziz al Saud, Saudi Arabia was a primitive multi-tribal society under the Ottoman rule and later British influence. In contrast, Korea had been a highly homogeneous country in terms of race, language, and communal ties until the division into north and south in 1945. Traditionally influenced by China, Korea was also colonized by Japan from 1910 to 1945.

Although both countries belong to the Group of 77 and share nominally common strategic interests vis-a-vis the Northern industrial countries, no explicit consensus on multilateral economic arrangements such as the New International Economic Order exists between two countries. Because of different structural positions in the international division of labor (e.g., Saudi Arabia is a

producer and exporter of oil and Korea an exporter of manufactured goods and an importer of raw materials), both countries adopt from time to time mutually conflicting⁴ postures in international economic fora. Although neither is tied to specific security arrangements, they are both strong allies of the US. Nonetheless, this does not mean that they share a strategic consensus. The Koreans' traditional tie with Israel, shaped by American influence, has produced some precarious political tension with Saudi Arabia with regard to the Arab-Israeli conflict.

The most striking dissimilarity between the two countries lies in their economic structures. Saudi Arabia, with a population of 7 million, functioned on a backward one crop economy until the oil boom of the early 1970s. Nomadic agriculture in the Nejd and Asir, coastal commerce in the Hejaz, and the ARAMCO-based oil economy in al Hassa characterized the economic geography of the Kingdom. Even throughout the 1970s, a sharp economic dualism (traditional backward sectors in the rural areas and hinterland and modern sectors in the urban areas) marked the economic structure of Saudi Arabia. Recently thanks to its enormous surplus capital, Saudi Arabia has attempted to enhance her industrial capability and to diversify her industrial base not only by promoting the agricultural sector via new sedantization policies but also by broadening her hydro-carbon related industries (Mallakh and Mallakh 1982; Mallakh 1982; Wells 1976; al-Qushaibi 1979).

Korea, by contrast, is a new dynamo in the international economic system. Over the last two decades, it has pursued rapid industrialization which has resulted in a relatively well diversified economic structure and remarkable industrial capability. Because of this, Korea has become one of the most rapidly growing exporters of manufactured goods in the world. Such export-led industrialization has reduced the importance of such traditional sectors as agriculture and light industry, making more capital and technology-intensive sectors (heavy industry, semi-conductor, etc), the new leading sectors of the Korean economy. In sharp contrast with capital-abundant, yet labor-scarce Saudi Arabia, Korea has low capital and natural resource endowments, and a plentiful supply of skilled labor (Hassan and Rao 1978; Westphal 1979; Mason 1980). In this sense, the economic structures of Saudi Arabia and Korea are complementary rather than homogeneous-competitive.

Given the fact that the two countries share virtually no similarity or homogeneity in background conditions which allegedly lead to higher levels of political and economic intercourse,⁵ it seems natural to expect a low level of bilateral ties between the two countries. This expectation holds true in the areas of historical and political interactions. However, the picture changes when we examine the economic dimensions of the bilateral ties between the two over the 1970s.

The Historical Evolution of Bilateral Ties

Contrary to the popular assumption that the Korean connection with Saudi Arabia is quite recent and originated with the growth in economic interdependence following the oil crisis, the interaction between Koreans and Arabs dates back to the 11th century. According to one historic source, some 500 Arab merchants visited the Korean peninsular in the early 11th century to promote commercial exchanges via China (Koryosa Book 5; Sega Book 5). They brought mercury, spices, and medicines, and brought back gold, silver, and silk in exchange.⁶ According to historical records, however, that there were no further visits by the Arab merchants of the 1040.

Two centuries later during the period of Mongol domination over the Koryo dynasty (1274), an Arab named Samka who came to Korea as a servant to a Mongolian princess (Jekuk) from China settled on the peninsular, leaving his Arab descendants, the Duksu Chang family (Choi 1971 / Kim 1979 / Koryosa, Yulchun Book 36) which had been completely assimilated into Korean culture and society.

In spite of these hoary antecedents, it would be extremely misleading to suggest that Korea and Saudi Arabia have had a history of extensive and intensive interactions. Rather these two examples are illustrative of paucity rather than the richness of the historical relationship between the two. For a variety of reasons, this relationship never developed in breadth or intensity. As

listed in above, the distance between the two countries was one obvious hurdle precluding the development of greater ties. Another impediment was their cultural heterogeneity, most importantly a lack of religious tie. Yet another was the absence of economic complementarity, for in fact both areas were largely isolated from the mainstream of international trade with the weak purchasing power. Later, their diverse colonial experiences also played a role in preventing Korea and Saudi Arabia from promoting mutual interaction.

It was only after the 1960s that both Saudi Arabia and Korea began to develop significant mutual interaction. Throughout the 1950s, Korean tie to the Middle East in general and to Saudi Arabia in particular was minimal. In the aftermath of the devastating experience of the Korean War, Korean foreign policy was dominated by North Korean, American, and Japanese issues. Indeed, in the 1950s, a period of continued and rapid decolonialization in the Middle East, Seoul maintained full diplomatic relations with only one country in the entire region--Turkey. Turkey was the window through which Korea saw the Middle East.⁷ Saudi Arabia was totally out of the scene.

While Korea's interest in the Middle East remained passive, and its policy virtually non-existent, in the 1950s, the same cannot be said of North Korea which had already undertaken a major diplomatic offensive in the area. The North recognized the anti-colonial forces in

Algeria (the FNL) at an early date, and provided arms and other support. Pyongyang also moved actively and rather effectively consolidated its backing from among the "progressive" countries of the region--Egypt, Iraq, Syria, and Yemen. By the late 1950s and early 1960s, these countries cooperated extensively with North Korea on bilateral as well as multilateral bases. In particular, these progressive Middle Eastern countries' support of the North in various international fora including the United Nations made North Korea victorious in the diplomatic battle over international recognition and legitimacy in lieu of the representation⁸ship of the Korean peninsular.

It was North Korea's diplomatic success in the Middle East that triggered the South's new foreign policy orientation toward the region. In sharp contrast with North Korea, South Korea targeted the 'conservative' monarchies, i.e., Saudi Arabia, Morocco, and Jordan, in its initial diplomatic counter-offensive in the region. In August 1961, the South Korean official delegation led by Ambassador Chichang Yoon stationed in Turkey paid its first visit to the Kingdom of Saudi Arabia and succeeded in obtaining the Saudi ruler's agreement to normalize diplomatic ties with South Korea. In the following year (1962) a cultural delegation was dispatched to the Kingdom. Until the formal opening of a residential embassy in Jeddah in 1973, however, only seven official delegations visited Saudi Arabia.⁹

This weak political link during this period, along with

the complete absence of economic transactions between the two, was primarily attributed to the lack of mutual interest in the political and economic arena. Furthermore the Saudis were somewhat reluctant to promote bilateral ties between the two countries because of the South Korean attitude on the Arab-Israeli conflict. Largely uninvolved in the region, South Korea had formally recognized the State of Israel in 1962, and permitted the Israeli government to establish a full embassy in Seoul in 1969. The agreement to allow an Israeli embassy in Korea in 1969--two full years after the June 1967 war, when virtually all Arab countries broke diplomatic relations with the United States--aggravated the Saudi attitude toward South Korea delaying the latter's request to open¹⁰ its residential embassy in the Kingdom.

The East Asian region in general and Korea in particular were simply not of any political and economic importance to Saudi Arabia at that time. Driven into the swirl of a regional hegemonic power struggle by Nasser, Fiasal's foreign policy was limited to the consolidation of regional power and status under the banner of pan-Islamism (Abir 1974; Gaspard 1969; Sultan 1981; McLaurin 1982). The Saudi pursuit of political relationships with other Third World countries beyond the Arab region was chiefly focussed on the Muslim states in Africa, West Asia and South East Asia. Given its limited resource base and the foreign policy objectives it faced at the time,

Saudi Arabia did not pay any "special" attention to Korea. The Saudi lack of interest in Korea is well revealed in the fact that throughout the 1960s the Saudi government sent only one delegation to Korea led by the Saudi Ambassador stationed in Tokyo in December 1965, who was in charge of Taiwan and Korea simultaneously.¹¹

The major event that led to a fundamental change in the Korean-Saudi Arabian relationship was undoubtedly the oil crisis of 1973-1974. The rapid industrialization of Korea during this period had produced a new and dangerous economic vulnerability--the dependence on Middle East oil. Because of the petroleum supply equation and the rapidly changing demand situation created by a skyrocketing increase in worldwide oil requirements, South Korea found itself heavily dependent on an Saudi Arabian oil. Quietly, almost imperceptibly, the pricing, availability, and security of oil had become a critical component of Korea's national security. This economic vulnerability was further menaced by the partial embargo during the October 1973 war and drove the Korean government for the first time to adopt a policy line overtly sympathetic to the Arab¹² position.

At the same time, Korea began to pursue intensive diplomatic efforts to promote bilateral political ties with the Kingdom by dispatching highly regarded diplomatic¹³ delegations to Saudi Arabia. Finally, in 1973 Korea opening its embassy in Jeddah in 1973. As a result of persistent diplomatic efforts, Korea was able to persuade

the Saudi government to open a consular office in Seoul in 1975 and a full embassy in 1982.¹⁴ It is interesting to note that while the Korean approach to Saudi Arabia in the 1960s was motivated by political goals in terms of diplomatic competition with North Korea in the Arab region and international fora, the approach in the 1970s was enhanced by economic interests arising not only out of the need for a stable supply of oil but also because of the perception of an enormous potential market in the kingdom.

Korea and Saudi Arabia: the Economic Context

There can be no doubt that the essence of Korea-Saudi Arabian relations is mutually beneficial economic interactions. Few people outside the group immediately involved in managing these interactions realize its magnitude, either for South Korea or for Saudi Arabia. Nor do many understand the multi-dimensionality of the economic relationship between Korea and Saudi Arabia. A simplistic model of Korea's economic linkages with Saudi Arabia might suggest that they feature the exchange of Saudi oil and capital for Korean goods. In many respects such a model would not be far from the mark, but in truth the relationship is far more dynamic.

From the Korean side, the exports involve not only merchandized goods but also services, mostly construction and engineering related, that account for the presence of extremely large numbers of Korean workers in Saudi

Arabia. Apart from the commodity trade, construction, and manpower/services sectors, the economic relationship is also characterized by close and growing cooperation in industrial joint ventures and financial recycling.

Commodity Trade: In the first business transaction between Saudi Arabia and Korea which took place in 1966, Korea exported tires and tubes valued at only \$ 17,000. As figure 3-1 indicates, commodity trade between two had been stagnant throughout the 1960s and the early 1970s. By 1971 although Korean exports to the Kingdom reached \$ 3.7 million, this constituted less than 0.01% of the Korea's total exports. This low commodity trade may be attributed to two major factors: First, Saudi Arabia was not yet a capital surplus country with a national income large enough to allow massive imports. Second, Korea was not fully diversified in its selection of external economic partners and commodity composition.

Figure 3-1

But the oil crisis in 1973-1974 reshaped the entire Saudi-Korean connection. In 1974, Korean exports of \$31.5 million to Saudi Arabia approached 1% of total Korean exports. Since 1978, the share of the Saudi market in Korea's total world exports has been maintained at

Figure 3-1: Patterns of Commodity Trade: Korea-Saudi Arabia

Year	Export			Import		
	Korea-Saudi	Korea-Middle East	% increase (K-S.A.)	Korea-Saudi	Korea- Middle East	% increase (K-S.A.)
1970	0.31 ¹⁾	7.9	177.9 ²⁾	38.3	191.5	75.8
1972	3.7	22.9	200.1	87.7	295.2	86.4
1974	31.5	141.3	203.1	670.5	985.7	334.9
1976	326.5	749.5	193.4	714.6	1,641.3	18.0
1978	717.1	1,445.6	6.8	1,280.7	2,233.3	14.0
1980	946.1	2,066.0	34.4	3,288.4	5,445.0	107.4
1982	1,300.0	2,544.0	4.9	3,751.0	5,058.0	-10.5

1) million US dollars, 2) % increase vis-a-vis the previous year

Sources: KOTRA, SuChul ChongRam (Overview On Export) (Seoul: KOTRA, 1982)
Office of Commercial Attache, Korean Embassy in Jeddah, Saudi Arabia.

approximately 6%, which is quite a significant increase given Korea's trade dependence on its two major partners, the US and Japan. In particular, data in figure 3-1 show that a rapid expansion of Korean exports to Saudi Arabia took place during the 1970-1976 period with a triple digit rate of growth. Since 1978, however, the rate of growth has been rather incremental perhaps signifying that Korean exports had reached a certain threshold level.

On the other hand, Saudi exports to Korea have constantly increased except for the two soaring points, one in 1974 (334.9%) and the other in 1980 (107.4%). These two soaring points reflect increases in prices of the Saudi exports (mostly oil) rather than in volume following the two waves of the oil crisis. It is apparent from these statistics that a tremendous trade imbalance existed between Saudi Arabia and Korea. Since 1970, Korea experienced trade deficits with Saudi Arabia every year. At the same time, the Saudi share of Korean total imports has been constantly increasing hovering around the 15% level. In 1982, Korean imports from Saudi Arabia dropped for the first time due to the adoption of energy conservation policies and oil import diversification policies, which coincided fortunately with the global oil glut.¹⁵

Figure 3-2 illustrates the commodity composition of Korean exports to Saudi Arabia (the composition of Saudi exports is omitted because one single item, oil, dominates the entire export sectors, approximately 98%). Over the last decade, major Korean exports include construction

materials such as steelpipe, cement, plywood, and related machinery. These construction related exports peaked in 1976 and 1977 and have declined since then probably because of scarcity in the supply of these goods in Korea, the emergence of competitors from India and the Eastern

Figure 3-2

European socialist countries, and the gradual Saudization¹⁶ plans pursued by the Saudi government since 1979. On the other hand, the general merchandise sector (e.g., textiles, garments, general machinery, consumer electronics etc.) shows a gradual increase since 1976 compensating for the losses in construction materials exports.

Saudi Arabia's import composition by country over the 1970s is illustrated in figure 3-3. Until 1977 the share of Korean goods in Saudi Arabia's total imports was negligible. The US, Japan, and EEC countries dominated the Saudi commodity market. Since 1978, however, Korea rapidly increased its share of the Saudi market. From a rank of 14th comprising less than 1% of the Saudi total imports in 1977, Korea has emerged as the largest exporter to Saudi Arabia next to the US, Japan and the EEC countries since 1978. Its share increased from less than 1% in 1977 to more than 3% of Saudi total imports since 1978. Two

Figure 3-2: Composition of Commodity Trade: Korea-Saudi Arabia

composition/year	1976	1977	1978	1979	1980	1981	1982 ¹⁾
Construction materials (steel/ plywood/ steel pipe/ machinery/ cement/ etc)	153.2 ²⁾	466.9	417.3	335.5	489.7	519.2	520.1
Increase in %	157.9	204.8	-10.6	-19.6	46.7	10.1	8.2
Share (%)	46.9	69.5	58.2	47.6	51.8	50.2	50.1
General Commodity (textile/ garments/ general machinery/ consumer electronics/ ship / auto/ etc)	173.3	204.5	300.3	368.7	456.4	534.7	508.3
Increase in %	101.3	69.9	87.7	22.8	23.2	17.2	1.7
Share (%)	53.1	30.5	44.8	52.4	48.2	49.5	49.9
Total	326.5	671.4	717.1	704.2	946.2	1,073.9	1,028.4
Increase in %	193.4	105.6	6.8	-1.8	34.4	13.5	4.9

1) As of November, 1982, 2) In Million US Dollars

Sources: Korean Institute for International Economics (Jeddah Office)
Office of Commercial Attache, Korean Embassy in Jeddah.

noteworthy points here are: Kuwait and Syria, which served as major trade platforms to Saudi Arabia, lost their advantage to South Korea. At the same time, Korea was able since 1978 to surpass Saudi Arabia's two major traditional trade partners, the Netherlands and Switzerland.

Figure 3-3

Construction and Service Sector: Although commodity trade between Saudi Arabia and Korea has increased significantly over the last decade, its magnitude is still minimal. It would be difficult to allege that Saudi Arabia and Korea have sufficiently enhanced their bilateral trade to diversify their dominant Western and Japanese trade connections. Each is still dependent upon its major suppliers. However, this merchandized goods trade is rather secondary to the Saudi-Korean connection. The most important bilateral economic relations between these two countries take place in the construction-service sector, where prior to 1973, there was virtually no activity. At this time Korean overseas construction firms were chiefly engaged in the Vietnam market as subcontractors for US firms such as Bechtel and Vinnell and on a smaller scale in South East Asian markets.¹⁷ Ever since the Korean firm Samwhan Construction Co. initiated its first \$ 25 million highway project in December 1973, however, Korean penetration in the Saudi construction market has been

Figure 3-3: Composition of Saudi Arabian Imports by Country

country/ year	1976	1977	1978	1980	1982
U.S.A	1,627 (1)	2,730(1)	3,956(1)	6,087(1)	8,989(1)
Japan	1,057 (2)	1,699(2)	2,857(2)	5,452(2)	7,687(2)
W.Germany	719 (4)	1,225(3)	1,967(3)	2,761(3)	4,299(3)
Italy	426 (7)	899(5)	1,291(5)	2,226(4)	2,595(5)
U.K.	514 (6)	903(4)	1,383(4)	1,971(5)	2,682(4)
France	233 (10)	490(9)	707(8)	1,648(6)	2,159(6)
Netherlands	322 (8)	646(7)	851(6)	962(7)	1,001(8)
S. Korea	62 (21)	189(14)	717(7)	946(8)	1,304(7)
Taiwan	N.A.	N.A.	427(9)	678(9)	N.A.
Syria	572 (5)	515(8)			
Kuwait	762(3)	652(6)			

#:Figures are in US million dollars. Number in bracket indicates rank.

Source: IMF, Directions of Trade: Yearly Report (Washington, D.C.: IMF, 1983) pp.456-457

phenomenal. Boosted by the oil boom and subsequent massive development plans, Korean construction firms literally created a new myth in the desert of the Arabian Peninsular.

As seen in figure 3-4, regional composition of Korean overseas construction was highly concentrated in the Southeast Asia till 1974. However, since the oil crisis and the massive inflow of surplus capital into the hands of

Figure 3-4

the Middle East OPEC countries, the Korean construction activity began to shift rapidly from Southeast Asia to the Middle East. Nearly all the construction contracts (97.1% in 1976, 98% in 1978, and 94.7% in 1980) came from the Middle East, cumulatively totalling \$ 37.1 billion as of 1980. Yet a great portion of the Middle East market was heavily concentrated in a single country, Saudi Arabia (figure 3-5), which accounted for more than 70% of the Middle East contract total during 1973-1981, amounting to \$27 billion. Compared with the volume of commodity trade during the same period, the magnitude of this construction sector is quite impressive.

Figure 3-5

Figure 3-4:

Regional Composition of Korean Overseas Construction

<u>Region</u>	<u>1966-73</u> <u>%</u>	<u>1974</u> <u>%</u>	<u>1976</u> <u>%</u>	<u>1978</u> <u>%</u>	<u>1980</u> <u>%</u>	<u>Total</u> <u>Cases</u>	<u>Contract</u> <u>Amount (US\$1,000)</u>
Middle East	5.7	34.1	97.1	98.0	94.7	1,034	37,154,654
Southeast Asia	71.0	55.8	1.4	1.1	5.0	316	2,206,966
Pacific area	22.3	8.7	0.7	0.2	0.1	114	178,223
Africa	0.6	1.4	0.6	0.3	0.2	16	241,162
Latin America	0.4	-	0.3	0.4	-	5	53,950

Source: Hui-Woo Kim, Our Country's Construction Export to the Middle East and Supporting Policies (Seoul: Korea Institute for Industrial Economics and Technology, 1982), in Korean, pp. 20-21, Tables II-1 and II-2.

Figure 3-5:

Korean Construction in the Middle East by Country
(Selected Countries)

Unit: US\$ million

Country	1973-76	1978	1980	1981	Total	% Mideast Construction
Saudi Arabia	2,752	6,404	5,238	5,888	27,435	73.8
Libya	-	168	1,366	1,689	3,446	9.3
Kuwait	205	528	379	85	1,917	5.2
Iraq	-	30	431	764	1,277	3.4
U.A.E.	16	113	227	126	856	2.3
Iran	54	282	63	-	601	1.6
Bahrain	173	69	7	23	382	1.0
Qatar	8	89	33	7	334	0.9
Jordan	58	79	18	82	324	0.9
Yemen A. R. (North)-	-	86	23	37	225	0.6
Egypt	10	31	107	16	186	0.5
Sudan	-	88	-	10	120	0.3
Oman	-	0.2	52	-	52	0.1

Source: Republic of Korea, Ministry of Construction, Present Status of Overseas Construction Export (Seoul), October 31, 1981.

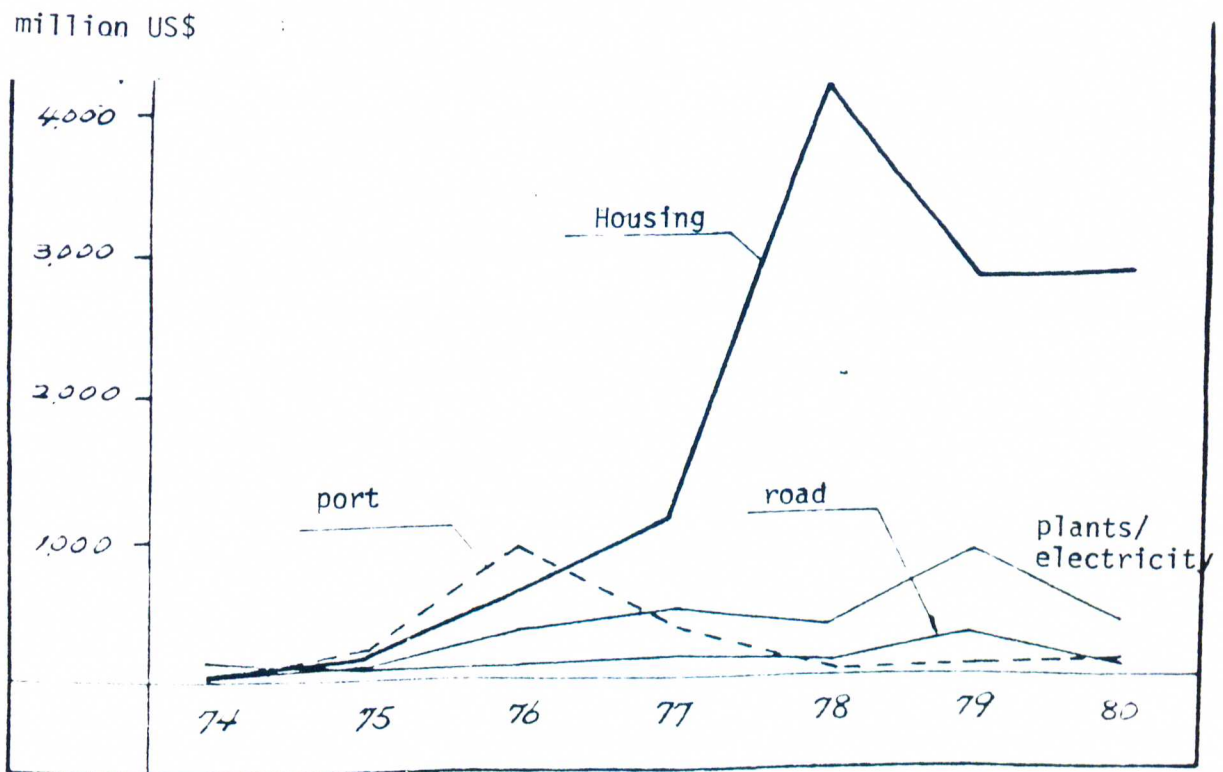
As figure 3-6 indicates, the contracts won by Korean firms called mainly for the construction of physical infrastructure (ports and roads), social infrastructure (housing and hospitals), and plants and engineering services. Until 1977, the major component of these contracts was physical infrastructure, while in the post-1978 period the construction of social infrastructure, mostly housing projects, and of plants and engineering services constitutes the major portion of contracts awarded. The changing nature of the contracts largely

Figure 3-6

reflects the sequencing pattern of the Saudi development plans whose initial emphasis was placed on physical infrastructure and later on social overhead sectors and industrial projects.

The extent of Korean penetration into the Saudi market can be easily understood by examining two major factors. Figure 3-7 illustrates the Korean share of total Saudi contracts annually available under its development expenditure. In 1975, the first year of the second five-year development plan, Saudi Arabia's total government expenditure was \$131 billion out of which \$ 75

Figure 3-6:
Sectoral Composition of Contracts in the Saudi Market



Source: Ministry of Construction,
Present Status of Overseas Construction

Figure 3-7

billion was allocated to the development budget. The Korean contract share out of this \$ 75 billion development budget was 6.8% in 1975. From this modest ratio, the Korean share in the total development budget gradually increased until it peaked in 1978 with a share of 22.9%. During 1976-1982, Korean firms annually won on average at least 14% of the development budget (the total available public sector contract amount). Since defense and industrial development related projects in addition to those contracts originating from the private sector are not included in this development budget, the share of Korean contracts in the Saudi construction market is substantial, especially given the fact that a large portion of contracts came from the defense sector, mostly from the US Army Corps of Engineers and the National Guard.

When compared with the commodity trade, an interesting aspect emerges in the construction and service sector. While the dominance of the US, Japan, and EEC countries in the Saudi commodity market has been stable in terms of share and ranking, there was a sharp reversal in the construction sector. Traditionally the Saudi construction market was a monopoly of US firms. The deep involvement of ARAMCO, the US Army Corps of Engineers, and other US

Figure 3-7: Saudi Development Expenditure and
the Share of Korean Overseas Construction

Unit: 100 million US\$

	1975	1976	1977	1978	1979	1980	1981	1982
Total Public Expenditure	131	317	375	384	425	499	881	914
Development Expenditure	75	213	271	279	291	413	609	594
Contract amount awarded to Korean firms	5.1	21.5	24.1	64.0	47.4	52.4	77.6	83.5
Share (%)	6.8	10.1	8.9	22.9	16.3	12.7	12.7	14.1

Source: Data supplied by the Office of Contrsuction Attache, Korean Embassy in Jeddah, Saudi Arabia.

academic and research institutions in the formulation of development plans and consulting in the Kingdom had paved the way for American firms in the Saudi market. As a result, the contracts awarded to US firms until 1977 constituted almost half of the Saudi total construction market, with West Germany and France in second and third place. This monopoly structure was reversed by the entry and expansion of Korean firms. By 1981 Korean firms became the number one contractors in the Saudi market, taking more than 30% of the total contracts, when amounts of principal as well as sub-contract projects are combined (ENR Nov. 1982; MEED August 1978 ; MEED Jan. 1982). The exponential growth of Korean firms in the Saudi market is indicated by the fact that by 1982 30 Korean firms operating in the Saudi market were placed on the list of world's top 200 contractors (ENR Nov. 1982). Among these Korean firms, Hyundai International ranked 10th, topping a number of the US, Japanese, and EEC firms.

Korean Manpower in Saudi Arabia: Saudi Arabia occupies a vast geographic area, but is a small state measured by the size of its population (about 7 million). About half of the population is either under the age of 20 or above 50 (Sinclair and Birks 1982). Thus, Saudi Arabia severely lacks a sizable manpower to initiate and implement its massive development projects. This manpower shortage had led Saudi Arabia to depend on an expatriate workforce.

Jordanians for the ARAMCO projects, upon Egyptians for other skilled professional jobs including doctors, nurses and engineers, and on the Yemenis for unskilled labor (Lackner 1978: 193-5; Salameh 1982: 115; Abir 1983). Figure 3-8 projects the past, present and future trends of expatriate workforces in the Kingdom.²² Data in this figure indicate that even prior to the oil boom there was a sizable number of expatriate workers, mostly from the

Figure 3-8

Arab states (345,000). However, in 1981 the number of foreign workers rapidly increased. Most Arab workers come from North-South Yemen (about 1 million) and Egypt (about half million). At the same time, the number of Asian workers has substantially increased reaching more than half million.²³

As a part of the expatriate labor force, Korean manpower, known for its strong discipline, productivity, and hard work has contributed substantially to the development of Saudi Arabia. Starting with 3,003 workers in 1975, the Korean labor migration into the Kingdom has shown a phenomenal growth. As Figure 3-9 shows, the total Korean work force in Saudi Arabia increased almost 900 % from 16,812 in 1976 to 116,075 in 1982. Of course, migration of Korean workforce is different in its nature from other Arab migrants. Korean workers are a part of a

Figure 3-8: Expatriate Manpower in Saudi Arabia

(in thousands)

Ethnic / year origin	1963	pre-1973	1975	1980(est.)	1985(projection)
Arab	----	345	699.9	1540-1571	1810-2245
Asian ¹⁾	----	----	38.0	85-100 ²⁾	140-195
Other ³⁾	----	65	35.5	78-90	107-140
Total ⁴⁾	237.5	400	773.4	1703-1761	2057-2580

1) Asian ethnic origin includes Koreans, Indians, Pakistanis, Taiwanese, Philipinos, and Thais.

2) This figure derived from Kerr and Yassin (1982). But this figure seems too conservative.

Shaw and Long (1982) estimate 792,000 Asian expatriate workers as of 1980. This approximates with author's finding from the Saudi Ministry of Interior.

3) This label includes Africans, Europeans, Turkishes, and Americans.

4) Figures in this total section are not authoritative ones. Many different figures have been suggested.

Sources: M. Kerr and E. Yassin, Rich and Poor States in the Middle East (Boulder, Co.: Westview, 1982)

ILO, Manpower and Employment (Geneva: ILO, 1975)

Birks and Sinclair, International Migration and Development in the Arab Region (Geneva: ILO, 1980) pp.134-135

J. Turner, Middle East Business Exchange, Jan. 1983, p.25

contract package, their duration of stay being usually limited to 1-2 years of project period, while Arab workers are rather individually employed under Saudi sponsors, thus having more permanent employment. The rate of change in

Figure 3-9

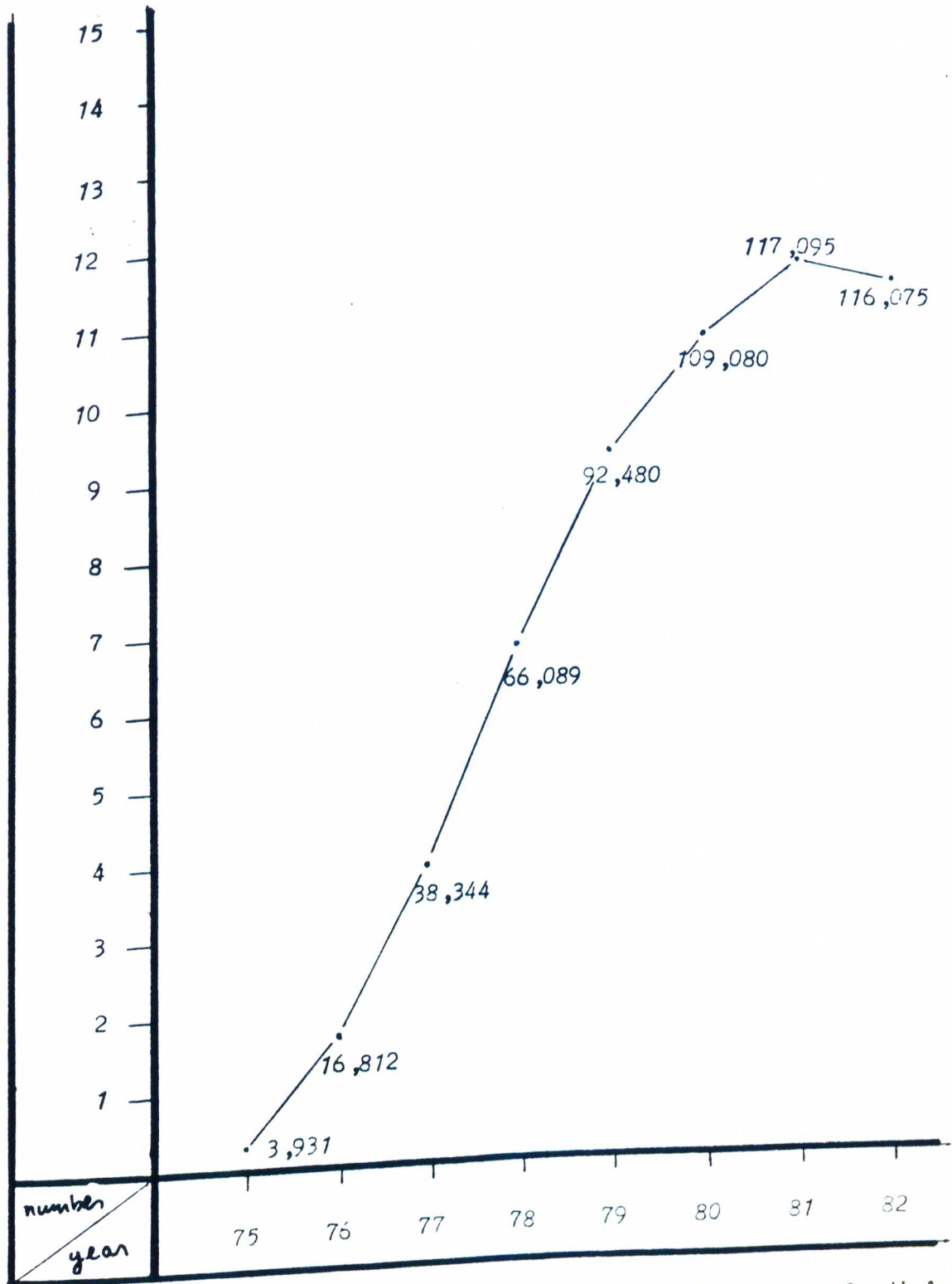
the Korean workforce in Saudi Arabia is contingent upon the size of the contracts awarded to the Korean firms. As shall be discussed in Chapter Five, however, there is a tendency to decrease the number of Korean workers as Korean firms seek cheaper labor from other Third World countries due to a rising wage demands of Korean workers.

Joint-Ventures, Capital Recycling, and Technical Cooperation: As we have shown above, the main elements of the Saudi-Korean connection can be found in the construction and commodity trade. However, we should not overlook other newly emerging dimensions of bilateral economic relations between the two countries. These new dimensions are industrial joint-ventures, financial recycling, and technical cooperation.

Traditionally Saudi Arabia has tended to prefer package or turn-key base deals as the primary form of foreign participation in Saudi development plans. Recently, however, both the private and public sectors in Saudi

Figure 3-9: Korean Manpower in Saudi Arabia
Annual Trend

Unit: 10 thousands



Source: Office of Labor Attache, Korean Embassy in Jeddah, Saudi Arabia

Arabia have begun to advocate industrial joint-ventures between local and foreign firms. Given the nature of the package deals, it seems quite natural for the Saudis to prefer such a form of business participation through which they can promote the transfer of technology and skills to locals in a constructive manner. This trend toward 'partnership' with foreign companies has increased as the pattern of development plans has shifted from physical and social infrastructural projects to more technology-intensive industrial projects.²⁴

Responding to this policy shift in the Kingdom, Korean firms and the Korean government have begun to promote these industrial joint-ventures. This positive response by the Koreans was quite understandable. The shifting pattern of development plans from labor- to technology-intensive projects began to bring about the loss in competitive advantages of Korean firms which depended primarily on cheap labor. In addition, in order to overcome various barriers to expand the market share in Saudi Arabia such as preferential treatment to local firms and the technological supremacy and market dominance of Western firms, Korean firms had to form an industrial alliance with local entrepreneurs via joint-ventures, no matter what the terms.²⁵ Up to 1980 only 14 joint-ventures between Korean and Saudi firms had taken place and these were predominantly concentrated in the construction sector(11 out of total 14 ventures). There was only one joint-venture in the manufacturing sector. Since 1982, however,

the nature of joint-ventures has changed. Out of 8 joint-ventures concluded in 1982, only three was located the construction sector while the other five projects were in the manufacturing sector. At the present time, 11 Korean firms are engaged in a feasibility survey of joint-ventures with Saudi local firms in the industrial sector ranging from a PVC plant, a steel pipe plant, a concrete pre-cast plant, ship repairing facility and a furniture plant.

Compared with the US, Japan, and the EEC countries, the share of Korean participation in joint-ventures is minimal, representing less than \$ 100 million in total investment. Yet, the future potential of this kind of economic cooperation appears to be quite significant in terms of diversification of capital and technology for both Saudi Arabia and Korea. This is particularly true since Saudi local entrepreneurs have begun to recognize the technological competence of Korean firms in the engineering and industrial plant construction fields. As seen in figure 3-10, over the last three years Korean firms have successfully completed the construction of complicated plants which were previously the monopoly of Western and Japanese firms. Their demonstrated ability to build desalination plants and to participate in the construction of petro chemical industries, both of which are essential to the future industrial development of the Kingdom, might have induced the Saudi government to encourage Korean joint-ventures with locals.

Figure 3-10

Although operating at a low level, the recycling of surplus capital has been taking place between Saudi Arabia and Korea. Indeed foreign exchange earnings from the commodity trade and construction exports themselves are an apparent pattern of such recycling. However, Korea wanted more from Saudi Arabia than that, partly because of a worsening bilateral trade balance derived from the second oil shock and partly because of a need for foreign capital to pay for a rapid industrial drive begun since the mid-1970s. While Korea has badly needed capital investment and other types of capital transfer from Saudi Arabia, the Saudis began to feel a growing need to divert their foreign capital investment from the Eurodollar market.²⁶ In this setting it was the Triad Holding Company, a firm belonging to Adnan Khashoggi, a controversial Saudi businessman, that joint-ventured an investment and holding company in Korea with some \$10 million. This was then followed by a Saudi government investment in Korean government bonds (\$ 15 million). At the same time Korean parties were successful in securing private as well as public loans from Saudi Arabia. In 1979 the Korean government received a \$70 million public loan from Saudi Arabia for port construction and is currently negotiating for additional

Figure 3-10: Major Plant Projects by Korean Firms (selected)

Unit: \$ US million

Type	Projects	Amount	Contract-type	Firm-name	Project-nature
Cement Plant	Jizan Cement Plant	235	principal	Korea Heavy-Machinery	turn-key base
Gas Plant	Usmania LNG Plant	119	"	DaeLim	infra/ electricity/ installation of machinery
	Yanbu LNG plant	200	"	"	"
De-salination plants	Al-Khoba De-salination plant	373	"	Hyundai	consortium
	Jubail De-salination plant	37	"	"	
Steel Plant	Jubail Steel Plant	126	sub-contract	DaeLim/Jungwoo	infra/ electricit / machinery installation
Fertilizer Plant	Jubail Fertilizer plant	33	principal	DaeLim	"
Power Plant	Assir Power Plant	183	"	Hyundai	Turn-key base

Source: Office of Construction Attache, Korean Embassy in Jeddah.

loans of \$ 125 million from the same source. The Korea Industrial Bank is also opting for a \$250 million commercial loan from a Saudi bank, while the Sunkyung Conglomerates have obtained a \$ 78 million private loan from Saudi Arabia. Currently, active negotiations are under way to establish one or two commercial banks in joint-venture form with the Saudi National Commercial Bank and the Riyadh Bank.²⁷

Finally, along with these commercial transactions, more explicit technical cooperation has begun to take place between the two countries via government-to-government agreements. In order to correct the Saudi perception of unilateral Korean gains from the Saudi connection,²⁸ the Korean government has been actively involved in promoting technical cooperation with Saudi Arabia since 1979. Over the years it has dispatched 51 agricultural technicians, 29 railroad system experts, and small number of scientists and economic planning experts to Saudi Arabia. Keeping pace with governmental efforts, Korean private firms have invited 120 petro chemical technicians and 200 engineering students of the King Abdulaziz University for training over the last three years (Korean Embassy in Jeddah 1983).

Given these few mutual political, economic, and cultural interactions between the two countries, the economic dimensions described above deserve some further analysis. The volume and range of bilateral economic ties between Korea and Saudi Arabia is of considerable

magnitude compared with any other bilateral relationship in the Third World. Such magnitude and intensity can be perhaps better understood in relation to the various positive and negative impacts that have accompanied these transactions.

Impact Analysis of the Saudi-Korean Connection

Korea: The impacts of Korean economic activities on Saudi Arabia can be seen in many areas. But the most important impacts manifest themselves in domestic macro-economic indicators. The boom in the desert Kingdom has substantially contributed to the improvement of the Korean balance of payments position. As Figure 3-11 illustrates, the net foreign exchange earnings from the Saudi

Figure 3-11

construction market alone constituted a substantial portion of foreign reserves: from 10% in 1977 to 25% in 1979 and an average of 17.3% through 1977-1981. The first surplus current account balance of 1977 in Korean economic history was also largely due to unexpected major foreign exchange income from the Saudi construction sector. Furthermore the consecutive surplus in services and transfer accounts through 1977-1979 was also the result of the earnings from the overseas construction sector in general and the Saudi

Figure 3-11: Balance of Payment and Overseas Construction Sector (1977-1981)
Unit: US\$ million

	1977	1978	1979	1980	1981
Foreign Reserve	4,310	4,940	5,710	6,560	
Merchandise Trade	-447	-1,781	-4,395	-4,384	-2,958
Services and Transfers	489	472	244	-937	-1,520
(Overseas construction balance)	(634)	(1,008)	(1,395)	(1,355)	(1,738)
(Saudi construction balance)	(446)	(885)	(1,138)	(1,134)	(1,300)
Earning from Saudi construction as a share of Foreign Reserve	10%	17.9%	25%	17.2%	
Current Account Balance	12	-1,085	-4,151	-5,321	-4,478

Source: Korean Overseas Construction Association, Five-Year History of Korean Overseas Construction (Seoul: KOCA, 1982) p.5 / Data provided from the Office of Financial Attache, Korean Embassy in Jeddah.

market in particular. The sharp reversal of this trend in 1980 and 1981 caused by second oil shock, worsening economic conditions and the related heavy foreign debt services virtually nullified the importance of continuously sizable receipts from the Saudi market. If commodity export income is combined with construction income from the Kingdom, the extent of the contribution to the Korean balance of payments position made by increased economic transactions with Saudi Arabia would be much greater.

The bilateral economic tie with Saudi Arabia has also substantially contributed to the remarkable economic growth rates Korea has recorded over part of the last decade (Figure 3-12). The gross construction earnings from Saudi Arabia have over the last seven years marked nearly 11% of Korean GNP when combined with commodity export earnings. And net earnings have constituted more than 2% of GNP on the average during the same period, adding to the over-all GNP growth rates (i.e., increase in net foreign earnings from the Saudi commodity and construction market divided by the amount of increase in GNP). At the same time, these earnings aided the rapid expansion of capital formation as

Figure 3-12

well as export promotion through industrial linkage effects (as was indicated in the increase of construction

Figure 3-12: National Income and the Saudi Construction Sector

Unit: US\$ 100 million

	1976	1977	1978	1979	1980	1981
Gross National Product	274.2	351.7	473.5	600.7	574.3	
Net Foreign Exchange Earning from Saudi Arabia		4.5	8.9	11.3	11.3	13.2
Ratio		1.3%	1.9%	1.8%	1.9%	

Source: Calculated from data provided by Office of Financial Attache, Korean Embassy in Jeddah, Saudi Arabia.

materials exports).

One of the mixed impacts derived from the Saudi connection occurs in the labor sector. Saudi construction activity had a favorable impact on overall employment creation in the construction sector and other sectors through industrial linkage effects. However, there were some adverse effects. The average monthly wage for Korean workers in Saudi Arabia was \$ 765.00 in 1980, almost double the average wage for Korean workers employed in other sectors. This high wage trend in the Saudi construction area entailed two negative consequences: one was the acute shortage of skilled labor that resulted in the domestic market, and the other was the related wage increase pressures on other sectors which aggravated inflationary trends already in evidence.

In general, the Saudi connection was crucial in helping Korea to overcome sporadic balance of payments crises, to boost its growth rates and to emboss its international image, which in turn was instrumental in building political legitimacy for the Park regime then in power. At the same time, the Saudi boom provided a way for the Korean public and private sectors to further their political and economic objectives in other Middle Eastern oil producing countries, especially those progressive Arab states traditionally maintained strong diplomatic ties with North Korea, such as Libya and Iraq. These positive impacts are not limited to macro-economic and political indicators. They significantly appear on the micro-level too. The

growing ability of Korean firms to win large-scale projects (e.g., over \$100 million per project) and the severity of international competition in the Saudi contracting market have forced Korean private firms, backward and traditional in management style, to be more efficient and innovative with the internationalization of management styles. As shall be discussed in detail in Chapter Five, the Hyundai International, perceived to be the Korean corporate miracle by Western observers, was chiefly a creation of this Saudi Arabian boom.

Notwithstanding all these positive impacts, the Saudi connection was not without drawback. In the wake of the boom, various negative impacts began to emerge. The first and most serious has been the aggravation of foreign exchange-induced inflation throughout the latter part of the 1970s. Because of the massive inflow of foreign exchange earnings from Saudi Arabia in 1977, 1978, and 1979 the Korean government increased the monetary supply more than it had planned. This increased money supply plus wage remittances coupled with rapid investment in the heavy industrial sector brought about serious inflationary pressures during this period and was responsible for the partial economic collapse in 1980 that produced the first negative economic growth rate (-5.5%).

Second, as mentioned earlier, the Saudi boom provoked an acute skilled labor-shortage as well as an escalation of wage demands across the various economic sectors. This

later produced declining international competitiveness in the commodity export sectors (due to overall wage pressures) and constituted an additional inflationary source.

Third, heavy Korean concentration in the overseas construction market in Saudi Arabia later made the Korean economy uniquely vulnerable. Easy entry into the Saudi market and the rapid expansion of market share led the Koreans to overlook classical business risk diversion strategies of market diversification. This heavy reliance on the Saudi market produced the following: a loss of bargaining power over the Saudis, consecutive bankruptcies of Korean firms (due to sharp competition from other Third World firms based on cheap labor), the negative repercussions of these on the Korean economy as a whole and on the financial sector in particular and unrealistic price competition by Korean firms and the consequent burdens on the Korean government and on labor (this will be dealt with in Chapter Six in detail).

Saudi Arabia: Due to the unavailability of concrete data, it is quite difficult to analyse the impact of the Korean connection on Saudi Arabia with the same precision. Nevertheless, it seems plausible to suggest a number of positive as well as negative impacts. First, it is an undoubted truth that Korean participation in Saudi development accelerated the overall rate of the development process in the Kingdom. As shall be discussed in Chapter

Five, more than 90% of development projects won by Korean firms were completed earlier than the original contract schedule, thus contributing to the accomplishment of the annual development plan earlier than targeted. This efficient initiation and implementation of development projects by Korean firms carried significant political implications, especially the timely alleviation of the severe housing shortage which was then a source of socio-political discontent in the Kingdom.

Another important contribution to Saudi development by Korean firms was their role in reducing inflationary trends rampant in the Kingdom over the mid-1970s. There were multiple causes for this inflationary surge. One of them was the expansion and/or wasting of public expenditure. As mentioned earlier, until 1975 the Saudi market, both construction and commodity, was dominated by Western firms which used to indulge in intentionally high price escalation (Mallakh 1982; Lackner 1978; MEED May 1979). For example, for a project that would normally cost less than \$ 100 million Western firms charged more than double or triple that amount, partly because of excessive overhead costs or profit considerations endemic to a monopolistic market structure.³⁰ The prevalence of this type of business practice was partially responsible for the demand-pull inflation. The entry of Korean firms with competitive prices reversed this trend, which in turn saved the wasting of public resources and reduced the demand-pull

inflationary pressures.

Third, the massive influx of skilled Korean workers compensated for severe shortage of local labor. Furthermore, the discipline and effectiveness of the Korean workforce relieved the Saudi rulers of potential political anxieties over labor disputes and political unrest that was often traced to expatriate labor forces.

Finally, the Saudi choice of Korea as a reliable economic partner has produced a number of political pay-offs to the Saudi rulers. First, such a policy orientation reversed a widely held impression that the Kingdom functions as a mere rentier economy totally dependent on Western firms. The Korean connection demonstrated that the Saudi government was capable of diversifying its economic ties in its own national interest. Second, the entry of Korean firms created new business opportunities for a large pool of growing middle class entrepreneurs, traditional actors and bureaucrats who had felt deprived by the traditional allocation of business opportunities. Western firms keen to political risks and therefore concerned about the selection of local sponsors and agents preferred to choose their counterparts chiefly from well established Hejaz merchants or from royal family members and their immediate associates. Thus, there was little room for the newly emerging middle class merchants and local elites to develop business connections with Western firms. At this juncture, the entry of the Korean firms and their aggressive business practices created an opening for these

isolated middle-level businessmen and bureaucrats. This in turn helped to assuage the growing political grievances from this sector.

It is equally difficult to measure any negative impacts of the Korean connection on Saudi Arabia as in the case of positive side analysis. However, the decade-old bilateral tie between these two countries began to create some problematic issues on the Saudi side. One of these issues was the Saudi's dislike of the Korean government's manipulation of private Korean firms operating in the Saudi market. As shall be discussed below, the Korean government became actively involved in coordinating the business practices of Korean firms in Saudi Arabia in order to prevent excessive competition among them in that market and thereby to enhance the gains from Saudi Arabia. Faced with such behavior, the Saudi government accused the Koreans of forming a new monopolistic market structure in Saudi Arabia under the government umbrella. The Saudi position was that the Saudi market was laissez-faire and the Korean firms had to compete with each other, thus enhancing the Kingdom's gain.

In addition, contrary to earlier discipline and effectiveness, a growing number of labor disputes by Korean workers in the Kingdom following the assassination of President Park in 1979 gave the impression that the Korean government was losing control over labor and that such labor disputes in the Korean work camps might affect other

expatriate workers. Added to this were rumors about Korean businessmen's mal-practices such as bribery and kickbacks, the consecutive bankruptcy of Korean construction firms operating in the Saudi market as a result of irrational pricing, and the delay in contract schedules caused by the increasing sizes of contracts (e.g., over \$ 100 million).

The above examination of historical, political and economic dimensions of the Saudi-Korean connection raises a number of theoretically interesting points. First, despite a lack of complementarity in 'background conditions', the bilateral economic tie between Saudi Arabia and Korea is impressive in its magnitude and range. Second, in a sharp contrast with recent dependencia literature, both Saudi Arabia and Korea show a high level of flexibility and resilience in the formation of foreign economic policy in general and in the shaping of bilateral tie in particular. Third, inter-South bilateral ties typified by the Saudi-Korean connection indicates that bilateralism may be able to produce positive economic impacts (especially productivity measured by macro-economic indicators and welfare measured by employment effects and wage levels) on the parties concerned without necessarily getting involved in multilateral-collective arrangements of rules and procedures). Finally, viewed from the Saudi-Korean case, inter-South bilateralism is not exempted from the syndrome of complex interdependence (Bergsten and Nye 1975; Cooper 1969; Koehane and Nye 1977) in the sense that mutually

beneficial exchanges did lead to a new set of costs and constraints such as sensitivity and vulnerability.

Keeping these points in mind, the following chapters attempt to trace the causal variables leading to the rise of the bilateral economic tie between Korea and Saudi Arabia, to examine the dynamics of process-level interactions between these two countries, and finally to analyze the outcomes of such a tie in a broad framework of the international political economy. In pursuing this inquiry, a primary emphasis will be placed on the role of the state and the entrepreneurial dynamism of the private sector within theoretical parameters of the statist mode of explanation identified in Chapter Two.

FOOTNOTES

1. The Wahabbi tradition is an offshoot of the Hanbalite school whose founder is Mohammad Abdul Wahab in the 18th century. This tradition reveals the most fundamentalist aspect of the Sunni sect which strongly adheres to the Quran and Sunna as the basic sources of Islamic law and which refutes any innovations or deviations from these two sources. For a succinct discussion of this topic, see Arberry (1973) and Hynat (1982).
2. For a general overview of Korean politics, refer to Kim and Wright (1977), A. Kim (1973), and Kihl (1984).
3. As of 1975, there was not a single Korean who could speak Arabic fluently. Even today, a number of Koreans who can command good Arabic is very limited despite huge economic and personal transactions.
4. For example, Korea strongly opposed the supply control scheme of Integrated Program for Commodity (IPC) within the NIEO debate, which was proposed by primary commodity producing countries including Saudi Arabia (S. Kim 1979). For the topic of internal fragmentation of the Southern bloc in the NIEO forum, see Rothstein (1981), Loeher (1982), and Ajami (1980).
5. For the concept of background conditions, refer to Haas (1966), Russet (1966), and Caporaso (1970). And for its critique, Mytelka (1973), Axeline (1978), and Nau (1981) are good sources to consult.
6. The visit of Arab merchants to Korea was facilitated by a unique policy of the Mongolian rulers during the Won Dynasty which favored and utilized the non-Han Chinese in foreign trade as a counter-balance to the dominance of the Han-Chinese (J. Kim 1979).
7. The close tie between Korea and Turkey was chiefly shaped by the US. President Truman's strong defense of Turkey in 1947 from the Soviet Union and subsequent alliance formation between Turkey and the US made Turkey dispatch its troop to Korea during the Korean War. The troop dispatch by Turkey played the essential role in promoting friendly tie between two countries in the later period.
8. North Korean diplomatic initiative had coincided with the emergence of anti-imperialist and nationalist ideologies and movements in the Middle East as was

manifested in the full blossom of Nasserism and the Asian-African Bloc movement. This overall political mood in the Third World helped North Korea to maintain its edge over South Korea. See McLaurin and Moon (1984) and MOF (1979).

9. Except one case in which foreign minister led official delegation (Nov. 1966), other delegations were low weighted ones primarily led by Korean ambassador stationed in Turkey (KMOF 1979).

10. According to an interview with Saudi Ambassador to Japan, Zein Dabbagh, who was then in charge of Asian bureau in the Ministry of Foreign Affairs, this Korean's pro-Israeli policy was not a serious obstacle. He argued that it was rather a function of Korean government's lukewarm attitude in making such a request (Interview at his residence in Tokyo, Jan. 23, 1983).

11. Low profile in the Saudi's diplomatic efforts in East Asia was primarily a result of financial and manpower shortage in the area of foreign affairs. In addition, Korea was not the country which drew any significant political and economic attention from Saudi Arabia which led to the Saudi's insensitivity to Korea (Interview with Ali al-Ghamdi, who was a Third Secretary at Saudi Embassy in Tokyo from 1968-1973).

12. Korea's new position was an overt recognition of the UN Resolution 242 epitomized in the following statements:
1) The Arab-Israeli conflict must be resolved on peaceful and equitable terms. 2) Conflict settlement must involve the withdrawal of Israel from the Arab territories the Jewish state occupied during the June 1967 War. 3) The national rights of the Palestine people must be recognized in any Arab-Israeli settlement. 4) Korea supports the sovereignty, independence, existence, and territorial integrity of all the countries of the Middle East. Dong Ah
11 Bo Dec. 16, 1973.

13. Since 1973, Korean delegations to Saudi Arabia were elevated to the ministerial level including one led by prime minister (May 1975) and other by foreign minister (March 1975) (KMOF 1979).

14. Until 1982, Saudi ambassador to Japan was in charge of Korea. The status of Saudi embassy in Korea has later become an interesting political debate between two countries. Details on this will be documented in chapter 6.

15. There was another factor contributing to this drop in oil demand from Saudi Arabia. That was the payment of deferred contract expenses to Korean constructions firms in the form of oil by Iraq and Libya that suffered from oil glut.

16. As shall be discussed in Chapter 6 in detail, the Saudization plan (protective policies) which allowed more leverage in import business to Saudi locals brought about negative impacts on Korean export performance to Saudi Arabia.
17. As will be seen in chapter 5, the Korean connection with these American firms ripened during the Vietnam boom played a substantial role in penetrating the Saudi market.
18. Chapter 4 documents sequential pattern of the Saudi development plans in detail from the first five-year plan to the third five-year plan.
19. Defense contracts from the National Guard were a recent phenomenon only after prince Abdullah, commander of the National Guard, had become Crown Prince. For detail, refer to chapter 6.
20. The Stanford Research Institute, Ford Foundation, and the US-Saudi Joint Economic Commission have deeply involved in the shaping of the Saudi development plans. For this topic, refer to Lackner (1978:151).
21. A more conservative estimation shared by Saudi locals identifies the size of Saudi population as about 4 to 4.5 million, far short of the official figure of 7 million.
22. There are many different projections. For this, refer to the Economist (13 Feb, 1982), Shaw and Long(1982), Kerr and Yassin(1982), World Bank (1981), Birks and Sinclair (1980), and ILO (1975).
23. According to a Saudi source, there are 300,000 Pakistanis, 150,000 Philipinos, 110,000 Koreans, 100,000 Indians, and 50,000 Taiwanese as of 1980 (SMOI, 1982).
24. As Saudi Arabia entered the third five-year development plan which emphasized both manpower development and industrialization, this form of industrial joint-venture began to rapidly increase (SMOP 1982; SAMA 1982).
25. As shall be discussed in chapter 7, the Saudi's extremely protective posture vis-a-vis foreign direct investment began to accompany a number of negative effects on the Korean efforts to promote industrial joint-ventures.
26. For the Saudi diversification strategy, refer to Babai (1981), Ward (1980), Birks and Sinclair (1981), and various issues of MEED.
27. The negotiations for this banking joint-venture were abruptly dropped by the Saudi parties, primarily due to political instability followed by the assassination of late president Park.

28. This 'unilateral' gain has become one of major foreign policy disputes between Korea and Saudi Arabia. Citing worsening bilateral balance of trade, Korean government has argued that its gain is not unilateral and that Saudi party should make more concession. However, the Saudis were reluctant to accept this Korean claim. Chapter 7 documents this debate in detail.

29. Despite ideological differences, such progressive Arab states as Libya and Iraq began to recognize economic benefits by having Korean firms involved in their development projects. The Korean success in Saudi Arabia had induced these countries to allow Korean firms to do business in their countries in spite of absence of formal diplomatic ties with Korea (McLaurin and Moon 1984).

30. The most notorious case was a telecommunication project scandal in 1978 in which the Dutch Phillips and prince Faisal (son of then Crown Prince Fahd) inflated project cost almost by US \$ 1 billion (MEED Nov. 1978).

31. As will be seen in chapter 5, in the initial stage of Korean penetration in the Saudi market, the Saudi agents for Korean firms were chiefly from middle-level merchants and bureaucrats. However, as Korean firms began to engage in huge projects, the socio-political character of the Saudi sponsors have changed.

32. The rationale behind the Saudi position was very clear. The Korean government's regulation of over-competitive business practices among Korean firms in the Saudi market and the exclusion of certain firms from the entry list created political grievances from the Saudi sponsors of these excluded firms. In addition, oligopolistic pricing behavior under the control of Korean government began to produce diplomatic protest from the Saudi side.

There is no page 156 in this dissertation.

CHAPTER FOUR

PRECONDITIONS FOR THE RISE OF THE SAUDI-KOREAN CONNECTION

The previous chapter illustrated the scope and magnitude of the Saudi Arabian and Korean bilateral economic relations over the last decade. Within a short time span, Korea became an important economic partner of Saudi Arabia. While commodity trade flows and industrial joint-ventures were incremental, Korean contractors emerged as the most successful in the Kingdom, outpacing American and other Western firms. Defying a commonly accepted interpretation of inter-South collective action based on Marxist-dependencia theories, this phenomenon not only reveals a new dimension of inter-South cooperation on a bilateral basis, but also poses a serious challenge to the existing modes of explanation of the foreign economic behavior of developing countries.

What were the pre-conditions for the emergence of this phenomenon? In Chapter Two, we asserted that the rise of inter-South bilateralism is a function of strategic choice evolving out of the interplay of the decision-making structures of a given country and of the surrounding opportunities and constraints stemming from the particular types of development strategy. This assertion in turn leads us to examine the following components:

- 1) the pattern of development strategy pursued and the resulting relative position of the country in the international division of labor;
- 2) the nature of internal and external conditions (opportunities and constraints) derived from development strategies and the pattern of integration into the international economic system;
- 3) images and perceptions of authoritative decision-makers regarding the internal and external conditions within the context of a set of state objectives situationally defined;
- 4) the nature of the domestic political structure (defined in terms of distribution of capabilities among major socio-political actors) which affects policy outcomes vis-a-vis bilateral choices.

A primary hypothesis deriving from these assertions is that the higher the level of complementarity in development strategy, patterns of constraints and opportunities, and in the state's foreign economic policy between a pair of countries, the more extensive and greater the volume of bilateral economic transactions between them. Keeping these factors in mind, the following sections deal with development strategies, economic and political environmental settings, and the foreign economic policy-making mechanisms of Korea and Saudi Arabia.

Patterns of Development Strategies

Korea and Saudi Arabia have pursued quite a diverse patterns of development strategies. Being poorly endowed with natural resources and capital, but rich in manpower, Korea chose a development strategy sharply different from that of Saudi Arabia where the opposite was the case. This

difference in factor endowment and pattern of development strategy created a high level of industrial complementarity between two countries, as we shall explain later.

Korea: As is the case with many other newly independent countries, the Korean economy from 1945 to 1950 presented a bleak picture. The political disorder and chaos that prevailed earlier in the country deepened economic uncertainty. Furthermore, the Korean War (1950-1953) completely devastated any potential for economic modernization. Economic malaise in Korea was wide-spread immediately following the Korean War, with triple digit inflation. The annual average GNP growth per capita was a mere 0.4% per annum (Rhee and Hong 1975: 4956). At the same time, the industrial structure revealed a rigid one crop economy pattern where over 65% of the labor force was employed in agriculture, producing 42.5% of GNP from this sector alone. US economic aid played a substantial role in improving these trade imbalances by covering almost two thirds of needed imports. In general, the Korean economy in the 1950s can be described as backward, stagnant, dualistic, and foreign aid dependent. Indeed none had then ever expected Korea to escape from the devastating aftermath of the war and from the vicious circle of poverty and backwardness.

Despite these initial liabilities, the Korean economy over the last two decades has performed what Western

observer described as a 'miracle', elevating itself to a new status of a NIC in the international division of labor. The average annual growth rate of real GNP during 1962-1979 was 9.4%. Per capita GNP increased dramatically from less than \$200 in 1962 to \$1,579 in 1979. In the same period, exports increased by 40% per year and industrial production by 20% per year. The share of GDP rose from 14% in 1960 to 28% in 1981, while the share of manufactured goods in these exports reached nearly 90% in 1980.

Development economists have come up with a plethora of reasons: labor quality, market size, Confucian work ethic, flow of external resources, and development sequencing (Balassa 1981; Krueger 1978; Westphal 1979; Hassan and Rao 1978; Adelman 1978). All these factors were responsible for the Korean success in one way or another. Among them, however, two factors appear to be most crucial: appropriate sequencing of development strategies and state intervention in terms of consistent economic plans. Under Park's military government, Korea had formulated and implemented five year economic plans of which medium-term plan methods are still sustained. As illustrated in Table 4-1, the Korean economic development strategy reflected through these medium-term plans is characterized by the three features: a big push for growth, a strategic choice of industrialization as the engine of growth, and finally, export promotion as an instrument of industrialization.

Table 4-1

As shown in Table 4-1, each five year plan set up relatively high growth rate targets. The highest priority of all planning efforts was given to the achievement of these growth targets. The line of reasoning behind this growth orientation corresponds to the Gershenkronian 'big spurt' thesis.² To catch up with developed economies, the Korean government committed itself to the acceleration of economic growth at any expense. Following basic principles of development planning, resources had been concentratedly allocated to the leading industrial sectors, and the government adopted the policy of 'growth first and redistribution later'.³ It was this strong governmental commitment that allowed the country to exceed its target rates. Except for the fourth plan(1977-1981) which emphasized stability, the first three plans exceeded their original goals by almost a 2 % margin.

The second important feature of Korea's development strategy consisted of a policy decision to industrialize rapidly. Perceiving that the way to escape from structural poverty and to realize rapid growth on a self-sustaining basis was industrialization, the government focused attention and directed resource allocations preemptively to the industrial sector. Following Hirschman's unbalanced growth strategy, each development plan singled out key strategic sectors which were perceived

Table 4-1: Economic Development Plans in Korea

	Ist Plan (62-66)	2nd Plan (67-71)	3rd Plan (72-76)	4th Plan (77-81)	5th Plan (82-86)
Plan Goals	1) Correcting socio-economic malaise 2) Preparing self-sufficiency	1) modernization of industrial structure 2) accelerating economic self-sufficiency	1) Harmonious pursuit of growth, balance and stability, 2) realization of self-sufficient economy	1) promotion of balance via social development 2) technological innovation and emphasis on efficiency	1) stabilization of economy, 2) promotion of social development, 3) institutional reform and emphasis on productivity
Growth-Rate: target (achieved)	7.1% (7.9%)	7.9% (9.7%)	8.6% (10.2%)	9.2% (9.1%) 1)	
Strategies (intermediate objectives)	1) correcting structural imbalances, 2) technological promotion, 3) balance of payment improvement	1) self-sufficiency in food, 2) preparing industrial deepening, 3) employment creation, 4) balance of payment improvement	1) food self-sufficiency, 2) expansion of social overhead sector, 3) industrial deepening, 4) expansion of qualified manpower, 5) balance of payment betterment	1) self-supply of investment capital, 2) balance of payment improvement, 3) industrial restructuring and enhancement of int'l competitiveness	1) overcoming inflationed economy, 2) recovery of int'l competitiveness in heavy industry, 3) pursuit of economic liberalization, 4) expansion of social development
Sectoral emphasis	key industrial sectors (cement, fertilizer, etc.) / physical infrastructure	light industry / labor intensive heavy industry	high value-added heavy-chemical industries (steel, shipbuilding, electronics etc.)	high-value added heavy industrial sectors (heavy-machinery, shipbuilding, auto, etc.)	technology-intensive sectors (semi-conductor, communication, genetic engineering)
Foreign Trade regime	Import-substituting	export-promotion	export-promotion	export-promotion	

(continued---)

- 1) The achieved growth rate of 9.1% during the fourth plan is only for the period of 1977-1979. In 1980, Korea showed its first negative growth of -5.5%.
- 2) It is usually difficult to differentiate strategies from intermediate objectives of economic plans. However, these intermediate objectives are the means by which ultimate plan goals are to be achieved, they are treated as strategies in this table.

Source: Byungrak Song, Thesis On Korean Economy (Seoul: Bak Young Sa, 1982) p.273 in Korean Economic Planning Board, The 4th Five-Year Economic Plan (Seoul: EPB, 1977) in Korean

to be high in forward and backward linkage effects. The industrial sequencing pattern through each plan period was well articulated. As Table 4-1 indicates, the first plan period (1962-1966) emphasized essential industrial items such as cement and fertilizer and social and physical infrastructure such as roads, ports, and housing.

With the anticipation that concentrated development of these key or leading sectors would generate backward and forward linkages, the second plan (1967-1972) was geared toward the enhancement of labor intensive light industrial sectors such as textiles, garments, and other consumer durables and toward the initiation of heavy industrial sectors (e.g., petrochemicals and steel). The massive and speedy modernization of the industrial structure fueled by the success in labor intensive light and heavy industries was linked to industrial deepening phases in the third and fourth plans (1973-1981). The direction of industrialization shifted into technology-intensive and high value-added industries such as chemical industries, electronics, shipbuilding, and even semi-conductor industries. What is distinctive about the Korean industrial development strategy is a clear sequencing of strategic sectors in line with product cycle patterns.

The last important aspect is that this industrialization process based largely on outward-looking or export promotion policies. After having experienced an economic crisis in 1962-1964, Korea pursued major policy

reforms in 1964-1965. Partly to overcome economic stagnation and partly due to the IMF and US government pressures, the Korean government adopted massive stabilization and liberalization policies, which signalled an apparent transition from import-substituting industrialization to an export promotion strategy. Foreign trade and exchange regimes were realigned to accomodate a new emphasis on exports. The influx of foreign capital, spurred by the enactment of the Foreign Capital Inducement Law of 1966 began to expedite investments in key industrial infrastructural sectors and light-industry based export sectors (Balassa 1981; Krueger 1978; Haggard and Moon 1983). This outward-looking strategy worked out well, matching the then burgeoning world economy.

Saudi Arabia: While Korea successfully pursued its economic development with a mix of timely industrial sequencing and aggressive export drives by fully exploiting comparative advantages (e.g., labor abundance), Saudi Arabia followed quite a different path of economic development. As Waterbury and Mallakh have noted, "without oil, it (Saudi Arabia) would have as much economic viability and regional clout as Mauritania." (1978:35) More than two thirds of its vast land (over 1 million square meters) is barren desert area chiefly occupied by the Rub al-Khali (the Empty Quarter). The hot and dry year round temperature, along with this geographic topology, limited substantially opportunities for viable economic development (Mallakh

1982; Long and Shaw 1982; Farsy 1982).

These ecological constraints prevented the Kingdom from achieving a modern and unified economy. Rather, the economy was a collection of several more or less developed, isolated economic regions tenuously linked by air and some improved, hard surface roads (Knauerhase 1974: 127). The Pilgrim economy and coastal trading around the Hejaz (Mecca, Medina, and Jeddah), oasis agriculture around the Nejd (Riyadh), ARAMCO related cities in al Hassa (Dammam, al-Khobar, and Dharan), and mountain agriculture and an inland trading base with Yemen around the Asir area were the only viable economic regions. The regional disparities created by ecological barriers had deepened the pattern of a dual economy in the Kingdom, the petroleum-based modern sector on the one hand, and primitive agriculture and bedouin animal husbandry on the other (Wells 1977:4-6; Johany 1982:1-14).

It was with the discovery of oil in 1938 that the Saudi economy underwent a substantial transformation. In the initial stage, the oil sector contributed to the change in the Saudi economy in two ways: first, it raised substantial revenues for the Saudi government,⁵ which was then totally dependent on the Haji economy. Especially after the conclusion of the 50-50 profit sharing agreement and on the imposition of a tax on each barrel of oil produced by ARAMCO in 1951, oil revenues rose from \$56 million in 1950 to \$341 million in 1955 (FAI 1977:219-244; Mallakh 1982:

141-144; Lackner 1978: 60-64). Since then, the oil sector has become dominant in the Kingdom's foreign exchange earnings, government revenues, and as a source of growth of national income. Even in the mid-1970s, petroleum contributed more than 80% of GDP, more than 90% of government revenues, and 99% of foreign exchange earnings (SAMA 1979). Second, the exploration of oil by ARAMCO entailed the construction of infrastructure. Although it was mainly related to the oil sector, ancillary construction of roads, ports, housing, electric generation plants, and water systems began to produce some linkage⁶ effects to the local economy (Mallakh 1982: 142).

Despite the increased oil revenues, the Kingdom was in the throes of a financial crisis by 1956. The random budgeting system, the uncontrolled government spending tied to the whims of the royal family, and ARAMCO's reduced production caused by the Suez Crisis and the entry of new⁷ independent oil companies placed Saudi Arabia on the brink of collapse (Lackner 1978:60-64; Adam 1965). Government employees were erratically paid, and the public debt rose by late 1957 to 1,800 million riyals. Gold and foreign reserves fell to their lowest point, and the riyals' market value sunk to half its official value (Lackner 1978: 62; Mallakh 1982: 141). The World Bank/IBRD finally intervened and suggested a set of financial⁸ and institutional reforms. . At the same time, the crisis gave birth to a major political change in the Kingdom. King Saud was replaced by the reformist Prince Faisal after

a series of politically traumatic incidents.⁹ It was King Faisal who initiated the Kingdom's major economic modernization under the tutelage of his reformist leadership. In the early 1960s, he announced Ten Point reform programs which were instrumental in setting the overall rate and direction of socio-economic-political change in Saudi Arabia.¹⁰

However, it was not until 1970 that Saudi Arabia pursued systematic economic development through the introduction of medium-term economic planning methods. For all King Faisal's efforts to diversify the economy and to create physical and social infrastructure, oil revenues during this period fell short of forming the critical mass necessary to realize a 'big spurt'.

With the help of an American consulting firm, Saudi Arabia completed its first five-year economic plan in 1969.¹¹ As indicated in table 4-2, since then, the Kingdom made consistent efforts to develop the economy through planning methods. Some major characteristics revealed in Saudi development strategies are: the pursuit of rapid growth, the drive for industrialization, the promotion of social welfare, and the development of endogenous human resources and the acceleration of infrastructure creation (Wells 1976:53-60).

Table 4-2

Table 4-2: Economic Development Plans in Saudi Arabia

	pre-plan period		1st plan (70-75)	2nd plan (75-80)	3rd plan (80-85)
Plan Goals	economic diversification/ preservation of Islamic values		preserving Islamic values/preparing economic diversification/ increasing defense capability	preserving Islamic and moral values/ increasing defense capability/ pursuing rapid growth/diversifying oil economy	Defense and security/ balanced growth/ social welfare/ pursuit of economic diversification/ preserving Islamic values
growth rates	oil sector non-oil total	10.34 ¹⁾ 6.96 10.34	14.80 11.66 13.41	4.78 15.13 8.04	1.34 ²⁾ 6.19 3.28
strategies (intermediate objectives)	3) infrastructure creation/ human resource development/ preparing industrialization		institutional restructuring/ reducing dependence on oil/ enhancing physical infrastructure	human resources development/ expanding physical and social infrastructure/ efficient regional allocation of economic and social programs	inducing structural change in the economy/ intensifying human resources development/ increased economic and administrative efficiency
public expenditure	N.A.		\$92 billion	\$198 billion	\$235 billion ⁴⁾
sectoral emphasis	petroleum/ mineral sectors		physical infrastructure/ oil related sector	physical and social infrastructure/ hydrocarbon related heavy-chemical industries	agriculture/ non-oil light industries/ other non-oil productive sectors
Foreign economic regime	open		open	selective liberalization ⁵⁾	selective liberalization and export promotion in petro-chemical sector

(continued---)

- 1) Growth rate in the pre-plan period is derived from 1966-1970.
- 2) Figures in the 3rd plan are planned ones.
- 3) As in the case of Korea, intermediate objectives of each plan are regarded as strategies.
- 4) This figure does not include defense expenditure.
- 5) By "selective liberalization" is meant to recent Saudi-ization policies pursued by Saudi government which reflect some protectionist elements in imports, contracting, and foreign investment.

Sources: Ministry of Planning(Saudi Arabia), The 2nd and 3rd Five-Year Economic Plans, 1975 and 1980.
al Mallakh (1982) pp.141-251, Wells(1976).

Like many other developing countries, Saudi Arabia was obsessed with the idea of rapid growth. The Saudis wanted to "catch up" but within the constraints and parameters¹² created by the Wahabbi ideology. Ghazi Alqusaibi, the then minister of Industry and Electricity, explained it as follows:

I know many economists tell us we cannot compress the century long process of development-- industrialization, infrastructure creation, and manpower training- into a few decades. But since no nation with our resources has ever tried to do so, no one really knows if it can be done. We shall try (Washington Post, Feb. 13, 1977).

The rationale behind this emphasis on growth seemed quite natural: Do all we can, while the oil lasts. As shown in table 4-2, the Kingdom was quite successful in pursuing this goal. Except for the 3rd plan, the targets for growth were set at a relatively high levels, and the actual achievements exceeded the targets. During the 1st plan (1970-1975), the growth target was set at annual average of 9.8% per year and the oil sector 9.1%. But the actual growth rate turned out to be 10.34%. This was chiefly due to the multiplication of oil revenues following oil crisis.

However, high growth performance continued during the 2nd plan(1975-1980). A planned target of an average annual growth rate of 10.2% was exceeded by more than a 3.4% margin. The ambitious development program was initiated and implemented during this period with a view to increasing absorptive capacity. An amount of \$143 billion, which is almost ten times larger than allocated in the 1st plan at

1974-1975 prices, was scheduled for this plan. The pursuit of rapid growth began to entail a number of unexpected side-effects, however. Spiraling inflation, heavy dependence on foreign labor, regional and sectoral imbalances, and growing opposition from traditional actors such as ulama and tribal leaders led Saudi political leaders to re-think the rate of development and to check the overheating of the national economy. Reflecting these constraints, the growth rate was targeted at an average annual rate of 3.2%, the non-oil sector GDP growth at 6.2%. The oil sector was expected to grow at a much slower pace (1.3%).¹³

The second salient feature of the Saudi development strategy is its unique industrial sequencing. When Saudi Arabia launched its 1st development plan, there was virtually no infrastructure. Neither roads, ports, public utilities, nor water systems essential to industrial development were available. Thus, major attention was paid to infrastructure-creation whose share in total expenditure was 29.2%, exceeding the defense budget (23.1%). While the 1st plan was exclusively geared toward the alleviation of infrastructural bottlenecks, the 2nd plan placed its emphasis on the dual fronts of economic development. One was to further expand the physical and social infrastructure, and other was to expedite hydro-carbon-related industrialization. Even at the risk of galloping inflation, nearly 80% of the 2nd plan budget was

put into creating physical and social infrastructure. Mass-telecommunications systems and massive de-salinization and power plants were begun during this period. At the same time, transportation systems were substantially improved with the construction of 13,000 paved roads, 10,000 agricultural roads, commercial ports of Jubail and Yanbu,¹⁴ and the expansion of Riyadh and Jeddah airports.

At the same time, the government ruthlessly pursued hydro-carbon based industrialization. The rationale behind this was two-fold : first, diversify the national economy in order to transform the rentier economy, and fully exploit comparative advantages stemming from unique factor endowments (i.e., oil) (Al Qusaibi, 1979 ; Turner and Bedore 1979: 19-20). To activate this petro-chemical industrialization, the two most ambitious development projects were attempted: the creation of industrial cities at Jubail and Yanbu to accomodate a full range of refinery, gas gathering, and petrochemical manufacturing entities together with a full blown steel plant (Shaw and Long,¹⁵ 1981:15-16; Halberton 1982; Third Plan 1980).

As Saudi Arabia began its 3rd Plan, its industrialization policy became much more elaborate. In pursuing economic diversification and petroleum-based industrialization, the Saudi planners began to think about more efficient linkages between the oil sector and non-oil industrial sectors. In line with this inter-industrial linkage concept, a strong emphasis was placed on light industry, agriculture, and non-oil mining sectors. This

re-orientation in industrial strategy attempted through a structural change of the national economy was further facilitated by reduced investment in infrastructural sectors. The ultimate goal of the 3rd plan was to reduce Saudi's dependence on the oil sector and to change the structural composition of GDP into a balanced proportion between the oil and non-oil sectors which the Third plan set its planned ratio as oil sector 56.6 vis-a-vis non-oil sector 43.4 (MOP, Third Plan 1980). To achieve this goal, the Saudi government tried to persuade the private sector via subsidies etc. to enter into as many areas of manufacturing as possible in order to reduce the heavy burden of imports.

The last important aspect of the Saudi development strategy was a shifting of its external economic posture from an open pattern to a closed one. During the 1st plan and in the early period of the 2nd plan, there was no substantial domestic industrial sector other than oil. This rentier economic structure forced Saudi Arabia to import virtually every item from abroad and export petroleum alone. Low tariff rates were imposed on these imports and non-tariff barriers did not exist. During the 2nd plan, however, Saudi Arabia began to produce some aluminium, steel, cement, and fertilizer under the import-substituting industrialization scheme. Along with aforementioned items, 32 other goods, domestically produced, were placed under 20% import tariff (KTA 1982;

KIIE 1982).

At the same time, the Saudi government began to pursue a positive inducement policy to promote foreign direct investment in joint-ventures with local firms. The policy was based on the realization that the combination of foreign technology and Saudi financial resources could contribute to the Saudi goal of sustainable economic diversification. To expedite this policy, a wide range of incentives were provided to foreign investors. However, this openness was protected by the Saudis in such a way that foreign investors were not allowed to acquire majority equity shares.¹⁹ This protective attitude was exemplified in Saudi manpower and contracting policies. Under the slogan of the Saudi-ization, the influx of expatriate manpower was strictly limited. And the Saudi government is obliged to award contracts to local firms even if they are not the lowest bidders. Furthermore, in those cases where foreign contractors are awarded, some of the work must be subcontracted to Saudi firms. In addition, foreign contractors must procure equipment and other materials from Saudi import agents (MEED July 1980: 14 ; Mallakh 1982).

Opportunities and Constraints

Considering the rate, direction, and scope of development strategies, Korea and Saudi Arabia share more dissimilarities than similarities and create a unique

pattern of mutual complementarity. This dissimilarity or heterogeneity is chiefly shaped by different sets of opportunities and constraints endemic to each country in the process of economic development, which in turn drives each country to adjust and realign its internal and economic policies.

Opportunities as a NIC and an OPEC: In case of Korea, its export-led industrialization coincided with favorable world market conditions. During the period 1962-1970 in which a major strategic shift in the direction of outward-looking policies was initiated and actively implemented, the rate of growth in the world economy averaged more than 5% annually. This expansionary trend in the world economy in turn triggered strong overseas demand for Korean goods. During 1962-1972, growth in the volume of world trade reached 8%, dramatically reversing the record low growth rate of 0.9% between 1913 and 1939 (Anell 1981: 33-39). The synchronization in the timing of the strategic shift with an unusually buoyant world market sustained and expanded Korea's export-led industrialization of Korea. 20

In addition to this external market factor, Korea experienced another developmental opportunity stemming from the international economic system. As the country began to pursue an outward-looking development strategy via industrial restructuring, liberalization and stabilization, it was able to induce foreign capital in the form of direct investment and commercial as well as public loans. In

particular the normalization of ties with Japan, a decreasing demand for capital in advanced industrial countries, and industrial relocation efforts by multinationals in the developing countries facilitated in one way or another the massive inflow of foreign capital essential to the pursuit of industrialization (Frieden 1980; Haggard and Moon 1983; Caporaso 1981; Lee 1979). The Vietnamese boom in the latter part of the 1960s eased the foreign exchange burden and helped smooth the development²¹ phase of the 2nd plan and the early part of the 3rd plan.

Besides these favorable external conditions, the availability of a pool of abundant and qualified manpower enabled the Koreans to exploit aggressively those newly emerging comparative edges in the nexus of spreading product cycles of standardized goods and services (Adelman 1974; Westphal 1979; Westphal et.al 1983). Furthermore, the existence of a strong, though authoritarian, government under the reformist leadership facilitated the implementation of consistent and articulate development policies without major interruptions from socio-political pressures (Haggard and Moon 1983; McMullen 1982; Turner et.al 1982; Krueger 1978; Chennery 1979). In all, Korea rose quickly to the status of a NIC and is still perceived to be a major challenger to the advanced industrial countries in the area of export competition.

Saudi Arabia, on the other hand, followed quite a different path. Its opportunities derived chiefly from

the oil sector. As of 1973, the Kingdom's oil reserves were estimated at 136.8 billion barrels which accounted for 36% of the Middle East total and 24.5 % of OPEC total (MEES April 26, 1976:8 ; Oil and Gas Journal Dec. 25, 1979: 102). Saudi Arabia had the highest level of proven oil reserve of the world.

However, this bounty from heaven was not quickly transformed into real opportunities for the pursuit of a rapid economic development. Until the onset of the oil crisis in 1973, the Kingdom still suffered from financial constraints. However, the collective actions taken by OPEC members since the Teheran conference in 1973 signalled a new chance for the Kingdom. The growing power of OPEC and the subsequent decline of the oil majors' bargaining power brought about the dissolution of the international oil regime governed by multinational oil companies (Barnett 1974 ; Odell 1978 ; others). The immediate outcome of this regime collapse was a sharp increase in oil revenue. As can be seen in table 4-3, the Saudi oil income comprising royalties, income tax, oil product tax, tapline fees, and profits out of the equity participation in ARAMCO production facilities increased astronomically from \$1.2 billion in 1970, the first year of the 1st plan, to \$25 billion in the beginning of the 2nd plan (1975).²² Of course, this jump in oil income was a joint result of price hike and of production increases. As oil prices increased, the level of production rose as well from 3.8 million b/d in 1970 to 8.48 million b/d in 1975. Within a

four year period, the production level more than doubled (SAMA annual report 1979:137).

Table 4-3

As can be seen in the cases of Iran, Iraq, and Nigeria, a great increase in oil revenue itself does not necessarily guarantee the acceleration of the development process. The relationship between oil revenue and investment in development is largely determined by the level of the absorptive capacity of a given country. In other words, it depends upon "how much of total oil income at a given price and export volume of oil will be absorbed in the current account balance of payments in the form of imports of goods and services, including remittances abroad of immigrant workers." (Habluetzel 1981: 10). The absorptive capacity of Saudi Arabia during the period of the 1st plan and the early part of the 2nd plan was very low, compared with other OPEC members. This created the problem of excessive surplus capital. Low absorptive capacity in turn facilitated the diversion of a massive amount of capital into investment in the development of social and physical infrastructure. This was particularly true given the fact that the value of the dollar, the instrument of oil payment and foreign investment of surplus capital, was depreciating rapidly in the 1970s along with a growing instability in

Table 4-3: Saudi Arabia: Oil Revenue by SourceUnit:US\$ million

Year	Aramco ^a	Getty Oil Co.	Arabian Oil Co.	Other cos.	Total	Index (1970 = 100)
1939	3.2	—	—	—	3.2	0.26
1946	10.2	—	—	—	10.4	0.86
1950	56.7	—	—	—	56.7	4.67
1955	338.2	2.6	—	—	340.8	28.07
1960	312.8	18.4	2.5	—	333.7	31.10
1961	352.2	22.9	2.5	—	377.6	—
1962	381.7	25.0	3.0	—	409.7	33.75
1963	571.1	23.0	13.6	—	607.7	50.06
1964	482.1	23.7	17.4	—	523.2	43.10
1965	618.7	23.8	20.4	1.2	664.1	54.70
1966	745.8	20.6	21.4	2.1	789.0	65.07
1967	859.2	17.8	31.8	0.8	903.6	74.43
1968	872.0	13.6	34.3	6.5	926.4	76.31
1969	895.1	15.2	37.1	1.7	949.2	78.19
1970	1,148.4	17.2	40.3	8.1	✓ 1,214.0	100.00
1971	1,806.4	20.6	44.2	13.7	1,884.9	155.26
1972	2,643.2	28.0	68.7	4.7	2,744.6	226.08
1973	4,195.0	22.0	91.4	31.7	4,340.0	357.50
1974	22,375.0	53.3	113.6	31.6	✓ 22,573.5	1,859.43
1975	24,838.6	191.1	642.7	3.8	25,676.2	2,115.01
1976	29,937.3	254.7	559.2	3.6	30,754.9	2,533.35
1977	35,703.8	263.4	571.6	1.2	36,540.1	3,009.89
1978	31,609.0	286.6	338.2	—	32,233.8	2,655.17
1979	47,590.1	277.8	575.2	—	48,443.1	3,990.37

Note. a. Including the value of royalty oil payments in kind and Saudi Arabian government's share in the Abu Sa'fah oilfield.

Source: al Mallakh(1982: 62)

international financial markets.

Internal and External Constraints: Owing to a set of favorable international and external conditions, Korea was successful in its export-led industrialization program. As the country accelerated its development phase and became more integrated into the international division of labor with a new structural position called a NIC, however, it was faced with a number of obstacles and constraints. One of the most salient constraints was a growing systemic vulnerability derived from its aggressive pursuit of an outward-looking strategy.²⁴ The increased openness of the Korean economy in terms of trade and capital inflow created numerous channels through which international disturbances were transmitted to the domestic economy. While in 1960, two-way trade (import and export) was 16% of GDP, it had risen by 1975 to 64%, making this small open economy more susceptible to the boom and bust cycles of international business. While all developing countries rely on external inputs such as capital, technology, and raw materials, Korea's export-led growth proved to be import and debt intensive. This pattern of openness has entailed many unexpected economic costs. When the deep recession and weak recovery hit the world economy, export performance staggered and the balance of payments position was jeopardized. International financial instabilities and soaring interest rates shook the national economy by adding an excessive burden of debt-service. Roller-coast

effects of international primary commodity markets imposed a cyclical pattern of economic uncertainty on Korea which relies on imported raw materials to a great extent.

The most dramatic example of systemic vulnerability was provided by the Korean economy in the vortex of the oil crisis. As noted previously, Korea shifted its industrial sequencing from labor-intensive light industry to energy and capital intensive heavy-chemical industry in the middle of the 2nd plan. In pursuing this industrial restructuring, the degree of reliance on imported energy substantially increased from 16.8% in 1966 to 55.1% in 1974. In addition, the composition of energy consumption had been drastically changed from coal as the major energy source to oil all of which had to be imported (EPB 1978: 244-247)²⁵. This changing pattern of energy consumption dealt a severe blow to the Korean economy during oil crisis of 1973-1974. As figures in table 4-4 illustrate, foreign exchange payments for oil during the oil crisis rose from \$305 million in 1973 to \$1.1 billion in 1974, representing almost a 300% increase in foreign exchange payments within a one year period, although the volume of oil imports was lowered during the same period. This tripling of the oil import bill was chiefly responsible for the record balance of payments deficit (\$1.9 billion) in 1974, which almost paralysed the Korean economy. The economic trauma caused by the oil shock was coupled with the onset of a global recession, weakening the Korean economy even further.

Table 4-4

As Korea pursued further integration into the international economic system, the second major external constraint began to emerge which we have identified as dyadic sensitivity arising from economic partner and item concentration.²⁶ Toward the end of the 2nd plan (1970), 46 % of Korean exports were going to the United States with another 28% going to Japan. On the import side, dependence on Japan was extremely heavy, creating trade imbalances. In the same year, textile and garments and other light industrial goods accounted for almost 62% of export composition. This partner and item concentration produced two visible constraints: one was the mounting protectionist pressure from these countries, and the other was the creation of bilateral dependence which tied the fate of the Korean economy to the economic performance of its major trading partners, Japan and the US. In fact, in the early 1970s, the US began to widen its quantitative restraints on textiles and apparel affecting \$ 517 million worth of trade value in 1972 and 1974 under the umbrella of the MFA (Odell 1984). Despite the politicization of trade imbalances between Korea and Japan, Japan maintained protectionist stance.²⁷ Furthermore, with the onset of the worldwide recession in 1974, the subsequent shift in the direction of restrictive import policy in OECD countries

Table 4-4: Foreign Exchange Payments for
Oil Imports and Balance of Payments in Korea

Year	Total Amount (oil import)	Import Price (oil)	Current account balance	trade balance	Export	Import
1965	23.6 ¹⁾	13.33 ²⁾	9.0 ³⁾	-241	175	416
1967	37.9	12.92	-192	-574	335	909
1969	97.6	10.99	-549	-992	658	1,650
1971	178.7	13.16	-848	-1,046	1,132	2,178
1972	221.1	15.02	-371	-575	1,676	2,250
1973	305.1	18.59	-309	-567	3,271	3,837
1974	1,104.8	61.67	-2,023	-1,937	4,515	6,452
1975	1,328.1	70.92	-1,887	-1,671	5,003	6,674

1) US\$ million, 2) US\$/kl, 3) US\$ million

Source: Economic Planning Board, Handbook of Economic Indicators (Seoul: EPB, 1978) p.37 and p.245

as a whole signaled an imminent increase in protectionist measures for other export items. This tightening of export markets by the major trading partners further aggravated the slow recovery, which in turn reduced demands for Korean goods (Mitra 1979).

The final but equally troubling constraint was the stiffening of inter-South horizontal competition and the declining international competitiveness of Korean exports. Korean growth had been built around a fairly narrow range of products. In 1970 textiles, apparel, plywood, and wigs accounted for almost 60% of exports. This mix was vulnerable for a number of reasons. Real wages in the other Asian NICs had risen much more slowly than those in Korea over the late 1960s. New low-wage entrants including China and India were seeking to replicate Korean successes in the export of light manufactures again on the far-ranging tide of the product cycle. On top of all this, the collapse of the Vietnam boom drastically reduced²⁸ foreign exchange income in the early 1970s. The combined result of these external constraints was immediately translated into acute balance of payment crisis, recession, and unemployment, which in turn caused the outstanding debt to jump from about \$300 million to \$3.3 billion, a ten-fold increase within a period of ten years (Moon 1984).

The internal, external constraints in Saudi Arabia were different from Korea in a number of ways. The direction of the Saudi development strategy was neither outward-looking

nor geared toward industrial deepening. Its developmental emphasis was mainly on the transformation of a primitive dualistic economy into a viable modern, diversified economy through infrastructure creation, human resource development and a fuller exploitation of oil-based comparative advantage. Unlike Korea where external or systemic constraints were dominant factors in the shaping of the rate and direction of economic development, Saudi Arabia's external constraints included typical systemic vulnerability and dyadic dependence arising from an one crop economic structure, while internal constraints consisted of structural rigidity, backwardness, and a shortage of manpower.

Systemic vulnerability in the Kingdom came from two major factors; one was a heavy dependence on oil, and the other was an influx of world-wide inflation into Saudi Arabia. The Saudi oil revenue is chiefly a function of world oil demand and supply. Although a sharp rise in oil price had entailed huge revenues and surplus capital, the formulation and consistent implementation of development strategies were greatly affected by the stability or predictability of oil prices in the international market. For example, huge development spending habits formed during the heyday of the mid-1970s and the resultant pattern of budgeting became immediately irrelevant when oil prices plunged and domestic inflation took off in 1978. In that year, Saudi Arabia recorded the first deficit in its balance of payments after the oil crisis. In the following

year, the rate of development had slowed because of budgetary stringency. The assumption was that oil prices might continue to fall with the decline in oil demand because of conservation, alternative energy resource development by consumer countries, and the entry into the market of new independent oil producers such as Mexico, the United Kingdom, and China. However, when the second oil shock came, the trend was reversed. The same can be said of the period of 1982-1984 during which Saudi Arabia suffered from a cyclical pattern of oil price formation and the uncertainty involved in the linkage between oil revenue and spending commitments (Stevens 1981:214-234; Erb 1979:21-30; MEED June 1 1979:3).²⁹

The visible effect of world-wide inflation also imposed a serious constraint on the Saudi development process. The oil crisis had been accompanied by a world-wide cost push inflation which in turn brought about a boomerang effect on the Saudi economy. In the Kingdom imports made up a significant share of total goods and services. The heavy dependence on imports had made it unavoidable for Saudi Arabia to confront the world-wide inflation which was multiplied in the circulation process (Keran and al-Malik 1982: 113-149; Erb 1979: 24; Mallakh 1982). As can be seen in table 4-5, about 4-5% global inflation during 1974-1975 was responsible for an almost 20% increase in the import price index in the Kingdom from a 4.6% level the previous year. When the Saudi inflation is calculated in

US dollars , the only international oil payment instrument, the situation appears even worsened. Its diminishing purchasing power caused by consecutive devaluations in the mid-1970s elevated the import price index measured in US dollars from 9.9% in 1972 to 61.4% in 1975, more than a ten fold increase during a three year period. The result was an unprecedented domestic inflation. The cost of living index went up from a 4% level in the pre-oil crisis period to 34.6% in 1975. Over the 1974-1977 period cumulative inflation raised the cost of living index by 150%, which in turn necessiated a sharp reduction in government spending and a readjustment of the development process as a whole.

Table 4-5

The sudden influx of petro-dollars had allowed the Saudi government to pursue ambitious but import dependent development plans. The Kingdom had to import everything from economic planning, commodity, and technology to services. This import intensive development pattern began initially with a high level of partner concentration. Planning and consulting were virtually monopolized by US government agencies and private firms in the 1st and 2nd plan formulation. ³⁰ The US, Japan, and EEC countries accounted for more than two thirds of the Kingdom's imports

Table 4-5: Money Supply and Inflation in Saudi Arabia

Year	money supply(M3) (1)	supply of goods & services (2)	inflation gap (1)-(2)	non-oil sector GDP deflator	import price index in US\$	import price index	cost of living index
1970-71	12.1	1.0	11.1	2.6	3.3	3.3	4.9
1972-73	38.8	21.3	17.5	9.9	13.0	4.6	16.2
1973-74	40.4	21.8	18.6	17.6	33.2	19.9	21.4
1974-75	61.0	18.7	42.3	61.4	20.9	19.7	34.6
1975-76	73.9	47.7	26.2	40.4	0.6	0.7	31.7
1977-78	43.6	23.4	20.2	14.6	8.2	8.0	11.2
1979-80	18.4	15.4	3.0	9.6	13.8	13.8	5.0

Unit: average annual growth rate

Source: Saudi Arabia Monetary Agency, Annual Report 1980

of goods and services. This excessive partner concentration brought about a typical dilemma of dyadic sensitivity to Saudi Arabia. The dilemma was revealed in the monopolistic and/or oligopolistic business practices of the advanced industrial countries' firms. The following statement made to the Western firms by the Saudi government (Council of Ministers) succinctly characterizes some of those practices:

1. Some consulting firms recommend sizes and specifications for projects greater than the original goals.
2. Pre-arrangement of tenders among themselves to show illegal profits.
3. Seeking business opportunities through personal influence regardless of cost and size.
4. The fixing for their exports to Saudi Arabia higher than to other countries for the same goods at the same time of year.
5. Raising costs of project to illegal levels on the condition of accelerating the completion of the projects. (Saudi Business March 2, 1977; MEED March 4, 1977:3)32

The outcome of this dyadic sensitivity was waste and inefficiency of government expenditure, which in turn fueled inflationary pressures by inducing a higher level of money supply than planned. At the same time, the persistence of these business practices created spill-over effects to other new entrants in the Saudi market.³³ As a matter of fact, faced with this constraint, the Saudi government had taken drastic measures. In Feb. 1977, the Saudi government announced the cancellation of tenders by foreign firms for electrification and sewerage projects and threatened to blacklist certain Western firms for price

rigging on the grounds that the prices asked were alarmingly high (Shirreff 1977:3). Three months later, another major project, a \$ 7 billion contract for a nationwide telecommunication installation to the Dutch Philips, was canceled for the same reason, which involved the loss of \$ 100 million commission fee by a Saudi sponsor (MEED Dec. 31 1977; Lackner 1978:170).

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External constraints, systemic vulnerabilities and dyadic sensitivities, brought about less devastating effects on the Saudi economic development than the endogenous problems. As the development process deepened, the lack of infrastructure, manpower shortage, and socio-political rigidities posed more serious constraints and directly affected the developmental potentials of the Kingdom. The first most serious problem was the acute shortage of physical and social infrastructure. A Western observer dramatically described this infrastructural dilemma as follows:

The chief battlefield where the struggle to industrialize Saudi Arabia will be won or lost is Jeddah port. Congestion persists, with between 100 and 130 ships clouding the horizon, waiting anything between a fortnight and six months or more to unload at the 13 overworked berths (MEED Dec. 31 1976: 5).
(my emphasis)

Port congestion and supply bottlenecks slowed down the overall rate of development. Major industrial projects such as desalinization and power plants and a petrochemical complex construction etc. had to be postponed or reduced in capacity and size due to this poor transportation

infrastructure. When port congestion was eased with the new construction and the expansion of Jeddah, Jubail, and Yanbu commercial ports, another problem arose--inland congestion. Port entrances, cargo compounds, streets of major cities, and highways were not adequate to meet the exponentially growing cargo transportation needs, although about 1,800 km of new roads had been built during the 1st plan. An equal, if not more devastating, constraint was the severe housing shortage. The massive influx of expatriate labor and the expansion of major urban centers following the development boom was accompanied by excessive demands for housing, pushing up the annual rent for a three bedroom villa to about SR 100,000 (\$28,000) during 1975-1976, an 500% increase over the pre-oil crisis period (various special issues on Saudi Arabia, MEED 1975, 1976; Saudi Business 1975, 1976).

Certainly infrastructural problems were not insurmountable. They merely took time. However, there was a more fundamental domestic constraint substantially reducing the chances for "big spurt" of development. That was and remains the shortage of indigenous labor. This dilemma was described by a Saudi businessman:

How can a nation determined to preserve Islam and its own security at the same time throw open its doors to foreign technology, manpower and all other kinds of influence? Who is going to run all these industries and services when they are finished? Look at it this way, there are a maximum of 4 million Saudis in this country. Discount half of them because they are women, another 25% are children, which leaves a potential workforce of 1.5 million. After manning the armed forces, the National Guard and the police,

how many Saudis are there left to run the government and private sector? (MEED Dec. 31 1977: 32)

The manpower shortage was not a new issue. Even before the oil crisis, the Kingdom heavily relied on expatriate labor. Yemenis and Omanis accounted for the bulk of unskilled labor, while the Levantines performed skilled labor for ARAMCO and the Egyptians worked in skilled and white collar jobs often serving as medical doctors and educators (Sinclair and Birks 1982: 161-171). As of 1975, the total native work force was less than 550,000, a number insufficient to manage and initiate the \$143 billion 2nd plan. The 2nd plan therefore projected a need for 810,000 additional foreign laborers, which number in fact doubled at the end of the 2nd plan (McHale 1981:632-633). This acute manpower shortage allowed domestic and imported labor costs to rise by 200 % as government expenditures increased the demand for labor (Erb 1979: 24).

The consequences of these external and internal constraints were manifold: Among them, inflation presented the most pressing issue. Inflation in the cost of living, in industrial materials and in the cost of labor made it necessary for the Saudi government to brake its overly ambitious development plans. Since too much cash was chasing too few items, the government had to ease supply bottlenecks as well as to trim the money supply simultaneously. While the Saudi development plans suffered from the nightmare of inflation, other major socio-political problems were emerging. The acceleration

of the development process accompanied by rapid urbanization was eroding traditional social framework and system of allegiances (Johns 1981; Abir 1983; Salomeh 1979).³⁵ At the same time, the concentration of wealth and business opportunities in a handful of royal families, nouveaux riches and traditional merchants, the inevitable by-product of a ruthless drive for development, began to produce political and social problems, inducing oligarchic rulers of the Kingdom to re-think the rate and direction of its modernization drive (MERIP May 1980; Winder 1979:14-15 ; Halliday 1981). The deepening regional and sectoral imbalances began to attract the attention of policy makers³⁶ responsible for the their allocation of resources.

State Strategies and Bilateral Choice: the Rise of the Saudi Arabian-Korean Connection

Thus far, we have discussed the development strategies of Korea and Saudi Arabia as well as the patterns of opportunities and constraints arising therefrom in general terms. Implicit in this discussion is the view that the patterns of development strategies (i.e., pure economic variables) and the types of opportunities and constraints (i.e., ecological variables) per se do reveal a set of complementarity which might necessitate the bilateral tie between Korea and Saudi Arabia. Saudi Arabia's first two development plans and related demand pattern of goods and services matched nicely with the stages of development

taking place in Korea, particularly those related to its mastery of infrastructural and light industrial sectors. By the mid-1970s, owing to its development sequencing, Korea was in a position to provide goods and services on a competitive basis which the Kingdom badly needed. In the same vein, the constraints and opportunities affecting Korea and Saudi Arabia were complementary rather than competitive because of the difference in the labor-capital ratio and the necessity to diversify its economic partners.

However, the existence of these mutually complementary factors which derived from the pattern and stage of development alone does not fully account for the dramatic growth of the Saudi Arabian-Korean connection. As was discussed in Chapter Two, there were a number of countries which satisfied such complementary factors. Southern European countries, Israel, Turkey, Eastern European countries such as Yugoslavia and Rumania, and even Egypt and Lebanon maintained a similar stage of development facing a similar set of constraints and opportunities as in the case of Korea at that time. In fact, they had a more apparent advantage over Korea in terms of geographic proximity. Thus, the pattern and stage of economic development and associated environmental factors may offer necessary, but not sufficient, conditions for this phenomenon. A fuller explanation of the Saudi-Korean connection depends on the examination of more dynamic

elements, that is, the level of complementarity in specific foreign economic strategies pursued and in the decision and authority structure responsible for such strategies.

Korea: Faced systemic vulnerabilities, dyadic dependence, inter-South competition and the resulting domestic economic difficulties, Korea was obliged to adopt a variety of strategies to cope with them. To reduce vulnerability, Korea attempted to attract foreign capital in a diversified manner as well as to secure a stable supply of strategic raw materials, including oil, through multiple channels. Efforts to diversify export items and partners were actively pursued with a view to avoiding dyadic sensitivities. And as a way of improving international competitiveness and of coming to terms with growing horizontal competition, the government initiated in the mid-1970s massive industrial restructuring and deepening (Haggard and Moon 1983). As shall be discussed below, the choice of Saudi Arabia as a bilateral partner was a conscious strategic decision which grew out of Korean foreign economic policies at the time.

Immediately following the oil crisis, Korea suffered from severe balance of payments deficits as discussed in the previous section. Most of these deficits in 1974-1975 resulted from trade imbalances with Saudi Arabia. In 1970, Korea's bilateral trade deficit with the Kingdom was a modest \$38 million. But in 1974, it jumped to \$639 million, accounting for almost half of current account deficit.

Though reduced through a sharp cut in oil imports, the same problem persisted in 1975 (\$494.1 million). Following the principle of reciprocity, the Korean government attempted to correct this trade imbalance by aggressive market penetration in the Kingdom.³⁷ Another major reason for actively pursuing bilateral ties with Saudi Arabia was the growing necessity to secure a stable oil supply. As indicated in table 4-6, in the pre-oil crisis period, Korea's major oil supplier was Kuwait which provided 50.4% of Korea's imported oil was originated in 1972. The portion of Saudi Arabian oil was 42% that year.³⁸ Ironically, this import composition changed after the oil crisis. Since 1974, more than half of Korean imported oil came from Saudi Arabia.

Table 4-6

Besides these balance of payments and oil issues, there were a number of other factors pressing Korean policy-makers to strengthen the Saudi Arabian connection. One of these was the surplus petro-dollars held by the Kingdom. By 1974, Korean overseas' debt approached to \$3 billion, yet it needed more foreign borrowing to finance its heavy industrialization initiated just before the onset of the oil crisis. Immediately after the oil crisis, the period in which surplus petro-dollars had not yet reached Korea via the Eurodollar market, international financial

Table 4-6: Korean Oil Imports by Country

Country	1972	1975	1977	1978
Saudi Arabia	38,867 ¹⁾ (42.0) ²⁾	51,861(44.0)	83,895(57.6)	95,841(57.6)
Kuwait	46,628(50.4)	53,637(45.5)	49,658(32.1)	50,789(30.5)
Iran	2,824(3.1)	882(0.7)	16,361(10.9)	12,912(7.8)
Neutral Zone	5,542(6.0)	10,194(8.6)	912(0.5)	3,854(2.3)
Other countries ³⁾	720(0.8)	1,221(1.2)	4,222(2.3)	3,136(1.8)

1) in thousand barrels, 2) in percentage, 3) Indonesia and other sources.

Source: Korean Oil Development Corporation, Petroleum Related Research Materials (Seoul: KODC, 1979)

markets were swamped with many bidders for scarce capital to pay oil bills, and consequently interest rates were high. This growing domestic need for additional capital and the tight international capital market drove Korea to opt for bilateral inducements of capital from OPEC countries. In this regard, Saudi Arabia was the perfect candidate to approach since its absorptive capacity was low and the level of surplus capital was high (22.9 billion in 1974 and 14.1 billion in 1975).

Apart from this inducement, there was an urgent domestic need to pursue aggressive market penetration in the Saudi market. With the end of the Vietnam boom and the loss of this lucrative market, once burgeoning Korean overseas construction firms were placed in a panic. Since the domestic construction market boom ended with the completion of the 1st and 2nd plans which emphasized physical and social infrastructure, there was no room to accomodate these firms and the about-to-be unemployed workers returning from Vietnam. At this juncture, the Middle East construction boom was conceived as a new opportunity marking the post-Vietnam era.

The conception of the Middle East market as a post-Vietnam opportunity coincided with a new positive assessment of capabilities by both the government and the private sector. By 1975, some Korean industries reached a stage of maturity in the product cycle. Cement, plywood, copper-plate, transportation equipment, aluminum, and other

building materials had been substantially standardized during the massive import-substituting period of the 1960s. And it was these items that were in great demand from Saudi Arabia in particular and the Middle East in general. Thus, Koreans began to have optimistic expectations in the sense that they could compete with western firms by utilizing the changing comparative advantage (i.e., labor). Moreover, Korean construction firms had other advantages in the Middle East market. Their previous participation in the gigantic physical and social infrastructure projects during the 1st and 2nd plans such as the Seoul-Pusan Highway, had allowed them to accumulate management skills and technological expertise and to improve manpower and equipment mobilization, both of which were essential to their success in the Saudi and the Middle East markets. In addition, overseas market experiences in Southeast Asia and the availability of cheap and qualified manpower gave a sense of confidence to Korean firms in uncertain and high risk market.

Despite this optimistic perception, however, the overall formulation of policies conducive to market penetration in the Middle East and Saudi Arabia did not immediately follow. The optimistic projection of private firms and their patrons in government was countered by skepticism and reservation on the part of other economic circles. Duck-jin Chang, then vice minister for the Economic Planning Board, summarized the government's position at the time as follows:

The oil crisis created a great panic for us especially because we were in the throes of a severe recession, current account deficits, and unemployment even before the onset of oil crisis. In this context, we saw the Middle East economic boom as a valuable chance. However, we did not have any grand design to exploit this opportunity nor was there any consensus among our policy-makers. Our firms were backward in management and technological capability, poor in financial resources, and inexperienced in overseas markets. Given this, it was quite difficult for the government to commit itself fully to a set of policies aimed at the Middle East market. (Interview 1/20/83)40

In fact, the government's initial response to the Middle East boom was mixed. Representing the interests of private firms, the Ministries of Construction and of Commerce and Industry strongly advocated an immediate formulation of a comprehensive and preferential policy package composed of administrative, financial, tax, and diplomatic supports. Since a number of Korean firms had already begun operating in the Saudi market, the Construction Ministry argued that the government should back the bank guarantees involving various bonds.⁴¹ However, the response from other economic agencies was negative. The Ministry of Finance concerned with the interests of commercial banks took the position that the government should not be implicated in any bank guarantee issues requested by constructions firms because of the high risks involved.⁴² The Office of National Taxation also opposed the idea of granting tax holidays to Korean firms involved in the Middle East markets, claiming that such a policy violated the principle of fairness, which might

cause political opposition from other business sectors.
 The Office of Labor raised the question of wage disparity between domestic labor and labor employed in the Middle East market and the difficulty of adjustments in the domestic arena.⁴⁴

This bureaucratic battle continued until President Park personally intervened in late 1975. When the Economic Ministers Council failed to produce a consensus, the stalemate paved once again for Park's personal involvement. Park took the side of the Construction Minister and resolved the conflict in such a manner that the government produced a comprehensive policy package to promote economic advance in the Middle East in general and in Saudi Arabia in particular.⁴⁵ It is said that Park's decision was motivated by three major factors: his personal relationship with the Construction Minister, his usual emphasis on export promotion(i.e., foreign exchange earnings) and oil security, and finally his positive assessment of the private sector's capability.⁴⁶

Once the decision was made, the government took immediate steps. In December 1975, it announced three major policy guidelines on the economic relations with the Middle East: 1) the maximum foreign exchange earning from the Middle East market by promoting construction, services, and manpower exports with the assumption that the Middle East boom would last at least five years; 2) strengthening administrative supports by establishing an integral body of

policy networks encompassing all the ministries; 3) in the recognition of various internal as well as external risks, barriers, and potential negative effects, the government would pursue its supportive policies with a low profile (IMES 1976: 2). These guidelines signalled the direct involvement of the Korean government in enhancing economic cooperation with the Middle Eastern countries, and it provided for its coordinative, regulative, and facilitative functions of the government vis-a-vis the private sector.

To implement these policy guidelines, a comprehensive organizational structure was formed. On the administrative side, the Committee for Economic Cooperation with the Middle East whose chairman was the prime minister was set up in Jan. 1976 as the supreme policy organ to coordinate and supervise all public and private activities related to the Middle East. This supreme council was aided by a working committee composed of vice ministers from each ministry and by a Middle East task force team newly formed at each ministry. At the same time, information and infrastructural support mechanisms had been institutionalized. The Institute for Middle East Economics was established by the government for the purpose of providing information and other necessary services for the private sector in Sept. 1976. An institute for Arabic language training exclusively for the business sector was established by joint cooperation between the government and private firms in the following year (KIEI 1982: 32-38).

In addition, the Korea Overseas Trade Promotion Agency(KOTRA) expanded its branches in the Middle East countries, and the number of economic, commercial, and construction attaches to Korean embassies in the region increased more than 10 fold.

In sum, the Korean approach to Saudi Arabia in particular and the Middle East in general was chiefly motivated by the acute perception of new market opportunities on the part of the political leadership and the private sector as it related to state objectives: the diversification of export markets, the inducement of petrodollars, a stable supply of oil, and the enhancement of export earnings. Despite bureaucratic struggles, its decision was prompt and the follow-ups were orchestrated immediately and comprehensively. Korea's strategic choice of Saudi Arabia and the effective and timely provision of policy tools provided for the strengthening of the Saudi-Korean connection.

Saudi Arabia: While the Korean choice of the Saudi Arabia was mainly motivated by a set of external constraints, the Saudi approach to Korea stemmed from internal necessities. As discussed in the previous section, Saudi Arabia's immediate dilemmas were how to curb spiraling inflation, to secure stable manpower, and to accelerate infrastructure creation with low costs. Since a large portion of inflationary pressures originated from excessive dyadic dependence on western firms, the Saudi

policy-makers were obliged to diversify their import sources. Securing the optimal level of manpower was quite a difficult task because of the latent political risks deriving from heavy reliance on other Arab manpower. Hence, the choice was to diversify the sources of the expatriate labor force. Accelerating infrastructure creation without risks of inflationary fall-out demanded more conscious selection of foreign contractors.

To the Saudi elites, Korean firms were ideal candidates to satisfy their needs. First, Korean firms were cheap and competitive. Atef Sultan, a keen observer of the Saudi market, described South Korea as being "almost the only country able to provide both advanced technology and a (cheap) skilled labor force." He further added " While Western and Japanese firms can provide the technology, their labor costs are prohibitive..... South Korean firms have now established a reputation for producing high quality work on time, giving them an even finer competitive edge." (MEED 1976:3) His observation was shared by many technocrats and policy-makers in the Kingdom. When the Hyundai won the contract for the Jubail commercial port in 1976, the price difference between the Hyundai and a Dutch company, the second lowest bidder, was more than \$300 million.⁴⁷ The Korean bid was conceived to be the only alternative to Western firms who had been widely accused of price-rigging. In fact, in the midst of price-rigging scandals by western firms, Al-Qusaibi, then Minister of Industry and Electricity set off on a tour of

Korea and other Asian countries, announcing that he would favor placing contracts with competitive and friendly nations rather than the now-discredited western industrial nations (MEED March 4 1977: 4).

Price was not the only factor that the Saudi elites considered in choosing Korean firms. Efficiency, hard-work, and the discipline of the Korean labor force constituted important elements. To explain this point more vividly, we cite one episode. Early in 1975 while returning from Medina to Jeddah at night, King Faisal noticed a sea of torches in the desert. The curious King went to investigate and found a group of Korean workers building a highway under the light of the torches. The King was very pleased, it was said, and from that moment, wrote personal memos instructing that Korean firms be awarded⁴⁸ contracts with special preference. Dr. Derhaly, a high ranking official in Planning Ministry, echoed the same sentiment: "In the beginning of our 2nd plan, Korea was a unknown partner. We were suspicious of Korean firms' capabilities. But later we found that Korea is the most reliable partner. Their prices are less than others, yet they are more expeditious and deliver high quality products. Furthermore, Koreans never make complaints and work like soldiers." (Interview: 3/11/83)

Apart from the Saudi elites' favorable image of Koreans in terms of prices and labor, there was a more compelling internal reason for choosing Korea as an economic partner.

This was the political calculation related to internal and external security conditions. Externally Saudi Arabia shared a vast border with hostile neighbors. The Ba'athist regime in Iraq, Marxist South Yemen(PDRY), Iranian hegemonic expansion and insecurity in the Gulf under the reign of Shah, and the presence of Israelis on the Northern border were in one way or another perceived as acute threats to the security of the Kingdom. It was particularly so given the fact that the Kingdom maintained less than 50,000 men as security forces which were composed of the regular army, the National Guard, regular and secret polices. Furthermore, security measures to protect the huge oil facilities were not fully operational. It was not easy to oversee 14 oil fields, 775 wells, 3 refineries, 11 loading facilities and 2800 miles of pipeline, all spread over an area of 70,000 miles (Dawisha 1978; Tahtinen 1978; McLaurin 1981; Quandt 1981; Bloomfield 1981; Mansur 1980 ; Schuler 1982; Kuniholm).

In addition to this external vulnerability, various domestic threats to regime stability emerging as the development process took shape. Opposition from such traditional actors as the Islamic fundamentalists and newly western educated elites, rapid urbanization and the erosion of royalty system, and the widening gap between the rich and the poor posed new threats to the Saud regime. However, a more pressing dilemma was the problem of expatriate labor. Since the days of King Abdul Aziz, Levantines, Egyptians, Yemenis and Omanis had immigrated

into the Kingdom and filled the gap left by the shortage of the endogenous manpower. The massive influx of Arab manpower encouraged under the laissez-faire migration policy before the oil crisis increased the number of Arab workers in the Kingdom to 1.5 million in 1975, almost double their number in the 1960s. The dominance and the permanence, as opposed to temporary immigrant workers, of Arab male manpower, the inevitable outcome of the Saudi's need for modernization, caused considerable anxiety to Saudi rulers because of the potential politicization of this labor force (Abir 1983; Shaw and Long 1982; Birks and Sinclair 1981).

Political opposition movements in Saudi Arabia have long been characterized by the persistent participation of expatriate workers, mostly from other Arab countries. Levantine workers organized the ARAMCO strikes in 1953 and 1956, and created the first politically motivated labor movement since the Ikwhan revolt in the Kingdom (Lackner 1978:89-109). The spread of Nasserism fueled political opposition movements founded by Egyptian and Yemeni workers employed in the Kingdom. In some cases, even Saudi natives joined the Nasserist Arab nationalist movement as demonstrated by the attempted coup by Royal Air Force officers in 1969 (Dessouki 1982: 57; Shaw and Long 1982: 98-100; Dawisha 1979: 32). More importantly, these Arab expatriate workers were linked to their home governments or to politically active regional organizations as the

Ba'athist parties in Iraq and Syria, mainstream Nasserist movements, and other radical and Islamic fundamentalist groups.

Saudi security has always been dominated by two major concerns; protecting national border, the oil and other industrial and public facilities simultaneously in case of major conflicts with a limited defense forces and reducing the potential for internal political instability emanating from expatriate Arab manpower or insulating the workers from political and ideological influences exercised from their home countries or pan-Arab regional political organizations.⁵⁰ There was no easy way out of this security dilemma. But one of the solutions was to seek manpower from less meddlesome non-Arab countries. In this context, Korea was the perfect source. In describing the Saudi preference for Korean firms and workers, an official at the Saudi Ministry of Interior Affairs made the following statement:

I believe that the Saudi government looked favorably upon Korean labor and construction firms because Korean satisfied then many of our needs: Korea is far away from Saudi Arabia, so there is no question of political influence peddling; it is anti-communist and therefore satisfied our ideological needs. The Korean labor force is disciplined and efficient or at least it is under the firm control of the Korean government. Thus, it is not like other expatriate labor forces, -- unorganized less disciplined, and politically volatile. The only quality absent is that they are not Muslims. (Interview Jan. 18 1982) 51

Viewed from Saudi economic and security objectives, Korea was therefore an ideal partner to choose. Koreans

were competitive, efficient, and hard-working, which helped the Kingdom to reduce waste, inefficiency, and price-rigging practices, (partly responsible for inflation), and to expedite infrastructure creation. The non-political Korean labor force also eased security concerns of Saudi Arabia.⁵² This increasing utility of Koreans in the Kingdom in both the political and economic context and the gradual emergence of a favorable perception of the Koreans on the part of the Saudi ruling elite have in fact produced a number of pro-Korean elites. Western educated officials of the Ministries of Planning, Commerce, and Industry and Electricity etc. began to show a strong preference for Korean firms. In particular, Hisham Nazer, the Planning Minister, known to be the most strong supporter of Koreans, even remarked to a Western journalist, "If we had known Koreans a little bit earlier, our development experience would have been far better-off." (Washington Post March 5 1980). At the same time, members of royal family following the lead of King Faisal also recognized the actual and potential contributions by the Koreans. By mid-1976, it could be safely argued, major decision-makers in the Kingdom were greatly in favor of the Korean entry into the Kingdom and were already using Korean firms as a bargaining leverage with western firms.

Although the King is the final decision-maker and while members and intimates of the royal family and upper-level technocrats are influential agents in the making of final

decisions, the overall decision-making structure in the Kingdom is not as autocratic as in other monarchical regimes. It is rather a widely based oligarchical structure, operating on the principle of consultation (shura) and consensus(ijma) (Koury 1978; McLaurin 1982; Shaw and Long 1982; Stevens 1981, 1982; Quandt 1981; Moran 1981; Dwaisha 1979).⁵³ Thus, no matter what priority the foreign economic policy toward Korea is, it is quite misleading to reason that the perceptions of ruling elites are translated easily and automatically into final decisions(i.e., pro-Korean policies or attitudes). Other societal actors such as the merchant class, the ulama, and the military elites are also in a position to affect such decisions or policy outcomes through the Kingdom's unique political network called the halaga'at(clan) mechanism⁵⁴ (Niblock 1981:75-105; Koury 1978: 85-92).

However, the Koreans were well received by these second-tier political actors as well. The merchants welcomed the Korean entry more for political than economic reasons. By the mid-1970s, there was growing discontent from a large segment of the newly emerging middle class merchants. Their grievances were legitimate and politically important since they accused the big merchants, both traditional and new, of monopolizing the oil wealths. In fact, traditional Hejaz and Nejd merchant families such as Alirza's, Sulaiman's, Alrajih's, and Jamjum's did control the major sales dealerships in the Kingdom. At the same time, new young tycoons such as

Khashoggi, Pharaon, and OjjeH swept away contract agentship. It was quite a natural phenomenon because they were politically well connected, thereby attracting western firms' attention on the basis of their influence and experience. These firms were well aware of the fact that having a business tie with middle class merchants would produce nothing. But the entry of Korean firms eased this problem drastically. Although big Korean firms made contacts with these influential merchants, middle-sized Korean firms, desperate to find local sponsors, allied themselves with these somewhat alienated middle class merchants. Thus, Korean firms in a sense satisfied both groups of Saudi merchants by being competitive partners for big business groups and by providing new opportunities to Saudi middle level merchants (Salomeh 1980: 18; Thompson 1982:12).⁵⁵

Meanwhile, Saudi religious leaders also favored the Koreans despite the xenophobic attitude of the Saudi fundamentalist ulama who dichotomize the world into two opposing forces, Dar al Islam (the world of Islam) and Dar al Harb (the world of war).⁵⁶ To the ulama, Koreans are not the children of Holy Books, and thus belong to Dar al Harb. This being the case, Koreans theoretically cannot be allowed on Saudi soil. However, this author's interview with two leading Saudi religious leaders revealed very interesting reasons why they made an exception for the Koreans. Sheikh Hassan Kutbi, former Minister of Haji and Awgaf(Religious

Affairs), who visited Korea as a special envoy of King Faisal in the early 1970s and who was instrumental in promoting political ties between two countries, noted two major reasons why he recommended pro-Korean policy to King Faisal. The first was ideological. Korea's anti-communist ideology persuaded him to believe that there is a high degree of ideological homogeneity between the two countries.⁵⁷ The second reason was cultural. "The rapid rate of development in the Kingdom," he argued, "has been accompanied by cultural evils from the West." But "by having the Koreans, we do not have to worry about cultural contamination. Koreans are disciplined and their culture is not yet corrupt as that of the West," he added (Interview Feb. 20 1982). Sheikh Abdul Aziz Bin Baz, the supreme leader of ulama as well as minsiter of Darul Iftah⁵⁸ (Islamic Research and Propagation), made a different point in approving the influx of Koreans. His view was that: "I know Koreans are Kafir (non-believers) and live in the age of Jaihiliyah (ignorance). But for that fact alone we cannot reject them. We should not forget that it is our divine duty to convert ignorant Kafir into truely good Muslims. Having more Koreans here, we are given a great chance to preach Islam." (Interview May 8 1978) Various other religious leaders in the Kingdom interviewed⁵⁹ by this author echoed these sentiments.

While the merchant class and ulama have shown a moderate to strong preference for the Koreans, other major social actors such as military and univerity students, also

interviewed by the writer, revealed a feeling of
indifference towards the Koreans. ⁶⁰ On balance, therefore,
it can be asserted that the overall domestic political
structure was favorable to Koreans. The Saudi leadership's
perception about and consequent choice of Korea as a
reliable partner attracted no significant socio-political
opposition. Although Saudi Arabia, unlike Korea, did not
pursue a comprehensive policy to promote bilateral ties
with Korea, certain pro-Korean gestures had their intended
effect. During 1974-1978, the immigration law was
liberalized to allow non-Arab expatriate workers with the
Kingdom and the Saudi authorities showed a specially
lenient attitude toward the Koreans in issuing entry visas.
Various administrative barriers such as counter-guarantee
provisions on placing bonds by Korean firms were lifted.
The frequency and relative weight of Saudis' visits to
Korea increased substantially from 1974 to 1979. In
particular, economic ministers, businessmen, and other
government officials in the economic and planning agencies
rushed to Korea to promote economic cooperation. Most
importantly, Saudi receptivity of Koreans was revealed in
their agreement to set up a joint committee on economic and
technical cooperation. This committee was set up before
with the US and other Western European countries. ⁶¹

In sum, two major conclusions can be drawn from the
above discussion in relation to the hypothesis asserted
earlier in this chapter. The first is that the high level

of complementarity in development strategies and in the nature of constraints and opportunities was responsible for the rise of inter-South bilateral ties as in the case of the Saudi-Korean connection. Nonetheless, such complementarity can provide only a partial explanation for the phenomenon. In order for the explanation to be complete, it is essential to examine the nature of foreign economic policy as a whole and its domestic determinants such as, state objectives, leadership perceptions, domestic political structures, and the pattern of dynamic interactions among them. In the case of the Saudi-Korean connection, what might be called strategic complementarity between two countries, was a decisive factor in initiating and promoting their bilateral ties.

So far in this chapter, our discussion has focused chiefly on the initial pre-conditions responsible for the birth of the Saudi-Korean connection. As argued earlier, the existence of such preconditions does not explain why such bilateral ties endure as well as expand. The sustainability and expansion of bilateralism is largely a function of how two major agents, private entrepreneurs and the state, mutually manipulate transactions. Chapters Five and Six will examine the nature of these private and state entrepreneurial activities which are crucial to the understanding of the process-level dynamics of the Saudi-Korean connection.

Footnote

1. There is a vast literature on the economic development in Korea. For a general overview, consult Hassan and Rao (1978), Mason (1980), Westphal (1979) and Adelman (1977). On foreign trade and exchange regime, refer to Frank, Kim, and Westphal (1975), Krueger (1978), and Balassa (1981). For a brief overview of industrial policy, Westphal (1982) is a good source to look into.
2. "Big spurt" thesis is derived from Gershenkron's hypothesis that "the more delayed the industrial development of a country, the more explosive was the great spurt of its industrialization, if and when it came" (1962:44). For a related literature, refer to Hirschman (1968:2-32), Gourvitch (1977), and Cummings (1984).
3. "Growth first and distribution later" was a political slogan of late president Park in his 1971 election campaign.
4. For this topic, refer to KTA (1980; 1981).
5. On the Haji economy, consult Long (1979) and King (1972).
6. However, this linkage was limited to al Hassa region. Other regions such as Hejaz, Nejd, and Asir did not benefit from the ARAMCO.
7. In the late 1950s and 1960s, there were three major events affecting international oil price structure: 1) the entry of the independent consumer owned petroleum company (Ente Nazionali Idrocarburi of Italy); 2) the entry of new independent oil producers such as Phillips, Sun, and Atlantic Richfields; 3) the emergence of Soviet Union as a new oil exporter. For this topic, refer to Tanzer (1969: 70-77).
8. The suggestions made by the World Bank included: 1) financial reform such as cutting the allowances of royal family; 2) institutional reform with specific focus on planning and statistical agencies (Adam 1965; MEERI 1978; Mallakh 1982: 141; Lackner 1978).
9. The most salient example was the birth of the free princes movement led by prince Talal, then finance minister. This free princes movement was influenced by progressive Nasserite Arab nationalist sentiment and advocated for constitutional monarch (Lackner 1978: 90-93;

Lacey 1981: 340-342).

10. For Ten Point programs, refer to Gauvy (1966: 147-151).

11. The Ford Foundation was instrumental in drafting this first five year plan.

12. For a good discussion on political dilemma of the Kingdom emerging from clashes between the modernization drive and the conservative Wahabbi ideology, Lenczowski (1967: 98-104), Edens (1974: 50-64), Koury (1978), Lackner (1978), and Shaw and Long (1982).

13. The slower pace of growth in the oil sector was motivated by the Saudi government's efforts to reduce dependence on the oil sector and thereby to avoid vulnerabilities stemming from roller-coast effects of international oil price.

14. For the overview of the 3rd plan, consult Wells (1976), Cleron (1978), Erb (1980), Looney (1982), Farsy (1982), Mallakh (1982), and Mallakh and Mallakh (1982).

15. For a brief overview of the Jubail and Yanbu projects, refer to Shaw and Long (1982: 13-22).

16. The importance of the private sector was revealed in a conference organized by the Saudi Chamber of Commerce on the role of the private sector in the economic development in the Kingdom. For details of the conference, consult Saudi Gazette (March 12, 1983) and Saudi Business (March 19-25, 1983).

17. A flat 3% import tariff was imposed. The most noticeable non-tariff barrier was a boycott against Israel.

18. It may be difficult to conceive that Saudi Arabia had pursued import substituting industrialization in its authentic sense. Though protective, the Saudi government did not manipulate foreign exchange regime, for example.

19. In principle, foreign firms are allowed to have up to 50% of equity share. But in reality, that is seldom the case.

20. For this, refer to Haggard and Moon (1983) and Moon (1984).

21. The Vietnam boom generated a huge foreign exchange through increased commodity and service exports and workers and soldiers' remittance.

22. For the Saudi's negotiation with the ARAMCO, consult Lenczowski (1960) and Mosley (1973).

23. This was particular so because of declining US dollar value, which was the means of oil payment.
24. Systemic vulnerability is defined as " costs or constraints imposed by the transmission of external shocks or turbulence originating in the international economic system." For this, refer to chapter two.
25. The same phenomenon could be found in Japan.
26. Dyadic sensitivity is defined as " the costs or constraints imposed by a pattern of external reliance in terms of specific actors and issue areas." For this refer to chapter two.
27. Trade imbalances with Japan have been the most persistent foreign policy issue between Japan and Korea. Korea has never enjoyed trade surplus vis-a-vis Japan.
28. The troop withdrawal by Korea as well as US led to such a collapse.
29. Due to this reason, the Saudi government actively pursues economic diversification by reducing dependence on the oil sector.
30. There have been at least four major US organizations which monopolized planning and consulting works: the COE, ARAMCO, the Saudi Arabian-US Joint Economic Commission, and the private industries.
31. Refer to table 3-3 for this figure.
32. The pervasiveness of these practices led to the revision of the Tender Law in the same year. For a nature of 1977 Tender Law, consult Chapter Six.
33. The rationale behind this practice was attributed to the following factors: 1) bureaucratic delays; 2) delayed payments of project costs; 3) unrelenting attitudes governing penalties; 4) high overhead costs; 5) overall perception that unless you make a fat profit, don't get into the Saudi market (MEED March 4, 1977: 4).
34. Prince Muhammad ibn Fahd, a son of King Fahd (then Crown Prince), lost a \$100 million commission when his father personally cancelled the contract (MEED Dec. 31, 1977; Lackner 1978: 170).
35. This is particularly true given the fact that a large influx of bedouin population into urban areas entailed a blurred focus of their loyalty and allegiance, thus undermining a system of "hukma" based on tribal structure.
36. Especially al-Hassa area where a large Shi'ite

population reside was the case in point. After a series of revolts in the late 1979 and the early 1980, a substantial concession was made to this region (Salomeh 1981).

37. Since these trade imbalances were largely derived from oil imports, the Korean government had very limited leverage in taking reciprocal measures.

38. This was largely due to the fact that the Korea's major channel of oil imports was Gulf, the joint-venture firm with the National Oil Corporation, whose primary source of oil was Kuwait.

39. By then, a large of number of Korean workers previously employed with American firms such as Vinnel and Bechtel had penetrated in the Middle East market through these American connections.

40. Duck-jin Chang was the key architech of Korea's Middle East policy by serving as chairman of the Steering Committee on the Economic Cooperation with the Middle East.

41. For a detailed discussion on this issue, refer to Chapter Six.

42. This was mainly due to conservative attitude of Korean banking community whose assessment of Korean firms was negative at that time.

43. For the National Tax Agency which was desperate to raise additional revenues, a 50% reduction in corporate and income tax from major firms was not acceptable.

44. What the Office of Labor was concerned about was potential negative repercussions such as a growing wage gap between domestic wage and overseas wage. In addition, senior officials in the Office raised the question on the competence of Korean firms in the labor management on a large scale in abroad.

45. Decision-making style during the Park regime can be characterized by a high concentration of decision authority in the executive branch, especially in president. When informal economic ministers' meeting could not come up with consensus on certain economic policies, president was the final authority to resolve such conflicts. For economic decision-making under the Park regime, refer to Jones and Sakong (1980).

46. Among them, Construction Minister Kim's personal proximity to president was the crucial factor. Kim was one of the most trusted proteges of Park until the former assassinated the latter in 1979.

47. For price competitiveness, refer to table 5-3 in

Chapter Five.

48. For this episode, refer to Ilgan Naewae Gyungje Dec. 8, 1977.
49. Of course, this security environment has drastically changed in the 1980s. Chapter Six deals with Saudi elites' perception of changing security environment.
50. Opposition movements in Saudi Arabia can be characterized by three major trends: Islamic fundamentalist such as the Ikwhan revolt, Arab nationalist such as Free Princes Movement and 1969 Royal Air Force coup, secular leftist such as the 1953 ARAMCO strike. For this topic, consult Lackner (1978: 89-108), Helms (1981: 226-275), Buchan (1982: 106-124), and Bligh (1984:69-74).
51. This quotation is from an interview with a high ranking official of the Ministry of Interior, who wished to remain anonymous.
52. According to a reliable source, at one time in 1977, the Saudi government seriously considered requesting the dispatch of Korean workers who can perform as paramilitary forces in the case of national emergence. But the idea was leaked and the Pakistani force replaced Koreans.
53. Recently there has emerged a handful number of literature dealing with various aspects of the Saudi decision-making mechanism. For oil policy, Moran (1981) and Stevens (1981); for industrial policy, Stevens (1982); for security and foreign policy, Quandt (1981), Dwaisha(1979), and McLaurin (1982); for manpower policy, Birks and Sinclair (1981) and Abir (1983); and for general overview, Koury (1978).
54. For a detailed discussion of halaga'at politics, refer to Chapter Five.
55. For this aspect, refer to figures provided in table 5-7 in Chapter Five.
56. Long (1979) is a good source to understand this worldview in the context of the Saudi Arabian foreign policy. For a more general and theoretical overview, consult Abu Sulayman (1972).
57. A similar view was echoed by Ambassador Zein Dabbagh, the Saudi envoy to Japan and Korea, at an interview conducted in Tokyo (Jan. 22, 1983).
58. Interview with Sheikh Bin Baz took place before this research was initiated.
59. The leaders interviewed are those associated with the

World Muslim League, the World Assembly of Muslim Youth, and some other ulama and Saudi merchants who were active in Islamic propagation to Korean workers in the Kingdom.

60. Students interviewed are mainly from the King Abdulaziz University in Jeddah. The author could have very limited access to Saudi military personnels. Some opinions were obtained from members of the Saudi military delegation to Korea.

61. Chapter Six will discuss this topic in detail.