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The Role of Institutions in the Economic Development of East Asian Countries

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Abstract.
This paper discusses the role of institutions in East Asian economic development. In the economic development of East Asia, institutional factors have a significant role and are different from economic development models in other countries. The concept of new institutional economics (NIE) provides a theoretical basis for understanding the success of economic development in the region. Several authors such as Ranis, Chang, and Haggard have examined the role of institutions in East Asia's economic development. In addition, East Asia's economic development experience has historically also had relevance in formulating development strategies in developing countries. This paper aims to identify the institutional factors that determine the success of economic development in East Asia and provide strategic inputs for economic development policies in developing countries.

Keywords: institutions, economic development, East Asia

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1. Introduction

The experience of economic development of Asian countries, especially East Asia, has attracted the attention of many researchers. The success of economic development in a number of countries in the region is considered to be the fruit of an Asian-style development model that is different in many ways from the economic development model applied in other countries. The uniqueness of East Asian development emphasizes the importance of institutional factors in economic development. Many initially believed that the East Asian development model was unique and could not be replicated in different regions at all (as for example for Latin America). Such pessimistic claims close the possibility of thinking that there are lessons that can actually be used as inspiration by developing countries to emulate the success of East Asia. On the other hand, the relatively optimistic view the East Asian experience as an alternative development model that can be used outside of the neo-classical development model that has been believed to be the only ideal development model.

The emergence of a new branch in the realm of development economics, namely New Institutional Economics (NIE), provides a theoretical foundation that explains the success of several East Asian countries. If the mainstream strongly believes that the success of some countries in the region is due to following a purely free-market-oriented neo-classical formula, thinkers from the institutional or institutional camp have succeeded in identifying various factors relevant to East Asia's success. These factors can be extracted into a composite of main thoughts, namely institutional or institutional factors.

Departing from the above thoughts, this paper will specifically discuss several studies that discuss the role of institutions in the economic development of East Asia. Some of the articles in question are the writings of Ranis [1], Chang [2] [3] and Haggard [4]. Ranis's paper is an initial study of the development of East Asia before the financial crisis that hit the region. Ranis' review is the main reference that explicitly explains institutional elements as a key factor in the success of economic development in the region, while at the same time refuting the claims of laisez faire supporters and interventionists who previously both considered that the East Asian development model supported one of the approaches of the two competing camps. Meanwhile, the writings based on the 1997 financial crisis were carried out by Chang who explored the experience of South Korea and continued by Chang who examined the role of institutions in the development of Asian countries more comprehensively. Meanwhile, Haggard conducted a review of the study of the role of institutions ranging from developmental state issues to policies related to the micro institution industry.

East Asia's historical economic development experience is also very relevant in relation to the formulation of development strategies in developing countries. First, over the past few decades countries in the region have recorded impressive economic growth records without sacrificing the important aspect of equity. Second, in addition to growing convincingly, the economy in the region is relatively resilient. Evidently, the relatively severe financial crisis in 1997 could be overcome in a relatively short time. The effects of the crisis did not cause countries in the region to fall into a deep crisis abyss as experienced by some countries in other adjacent regions, such as the Southeast Asian region.

Based on some of the reference articles mentioned above and the facts of the economic growth of countries in the East Asian region over the past few decades, this paper basically aims to: (1) comprehensively identify the institutional factors that determine the success of economic development in East Asian countries, (2) identify development strategies that can be used as input for the benefit of economic development policy advice in developing countries.

2. Role of Institutions

The role of institutions in social science disciplines has basically been the concern of many experts for a long time. Institutional issues have emerged as one of the central themes in the post-world development economics branch. Development economics has become an independent field of study as there is a growing awareness that the rules or institutions that regulate the behavior of economic agents in developing countries are fundamentally different from those that apply in developed countries.

The development of development economics was drowned out by the rise of neo-classical growth theory in the late 1970s to early 1980s. The neoclassical approach emphasizes the assumption of human rational universality as well as the application of economic theory (with little modification) to explain economic phenomena in developing countries. However, the trend that has occurred since the 1990s shows that attention to the role of institutions in development is beginning to grow, as can be seen from the increasing number of literature that specifically discusses the subject of study on institutions.

Conclusively, Chang (1998) asserts that the debate over the role of institutions in development boils down to the agreement that institutional contributions can no longer be seen as complementary explanations to conventional market theories. More than that, institutions must be understood to be able to understand the workings of the market economy. In other words, a well-functioning market involves nothing but a number of institutional rules that can be illustrated as follows:

1. What goods can be traded (many countries prohibit the transaction of human organs)

2. Who trades (many countries prohibit children from working and only people with special qualifications can engage in legal medical services)

3. What are the restrictions on fair trade (rules that prohibit fraud)

4. How prices can vary (many commodities and stock markets are stopped trading if prices fall very sharply in a short period of time)

The functioning of the market is thus influenced by the nature of the effectiveness of a number of non-market institutions which include it;

1. State institutions that guarantee community coordination

2. Non-market property rights (rules governing the use of public goods may affect the use of rural resources and marketed products)

3. General code of conduct (the level of honesty in society can affect the effectiveness of fraud regulations in a particular market)

4. The business world (which works according to market logic) with related institutions (which coordinates the interests of company members through non-market measures)

5. Rules that govern the relationship between the government and private sectors.

An important thing that observers often forget is that institutions are not available instantly in the short term. Institutions must be built, although not always with very detailed planning, given the nature of institutional development that relatively passes through certain stages of evolution. However, the evolution process of institutions does not occur randomly, so planning and the learning process have a very important position. Institutional evolution can be traced through historical perspectives and comparative studies between cases (countries).

Reforms carried out in many developing countries through the free market prescription which includes elements of privatization, deregulation and openness often only underestimate the importance of institutional development in the economic development process. Without adequate non-market institutional support, development in many developing countries often fails. The experience of several developing countries in the Latin American region and several regions in the African continent deserves to be used as an example of the failure of a massively applied market approach. The free-market recipe by the IMF has also been applied in Indonesia in overcoming the impact of the 1997 economic crisis. A number of policy packages are implemented as a consequence of the loan package. In fact, Indonesia's economic recovery is relatively slow compared to other countries in the same region.

A different thing will be seen in the economic performance of four Asian tigers outside of Japan: South Korea, Taiwan, Hong Kong and Singapore. Whatever parameters are used, it is undeniable that these East Asian countries have relatively succeeded in getting out of the group of poor countries and continue to enjoy the dynamics of amazing economic development. The experience of several East Asian countries shows that the gradual introduction of market institutions and the support of various non-market institutions before achieving a contemporary Asian-style form of liberalization is relatively more promising than the hasty approach to market liberalization.

3. Conclusion

The basic question posed by Chang (1997) and also deserves appreciation is that after studying institutions in East Asia, can the existing institutional structure be replicated in other countries, especially in developing countries? Mainstream adherents who see the South Korean phenomenon as a model of a free-market economy will say yes, but those who are observant to see the unique features of existing policies and institutions (which are in many ways different from market economics textbooks) will answer "probably not". Chang (1997) insinuates that the changing views of supporters of market economics are motivated by the belief that markets are relatively easy to create and transplant in any part of the world, whereas institutions cannot. In the mainstream perspective, markets are seen as natural and can be created spontaneously while institutions must be built in order to respond to market failures.

However, the dichotomy of market versus institution is incorrect. First, the market itself is actually one of the institutions and the second, the market like the other institutions will not be created spontaneously and must be built evolutively as the British experience during the industrial revolution and even the United States itself. If the market model is considered natural, why are so few countries successful with this model while many successful countries are applying a different approach (deviant model).

There is no one-size-fits-all institutional structure for every country and transplanting foreign institutions to work in an instant is impossible. However, this does not mean that every country must develop a development model from scratch. Experience shows that the import substitution strategy is one of the prominent features in the construction of the modern economy. East Asian countries have shown that a well-functioning institutional structure can be created in a relatively short time if there is a desire to adapt foreign institutions to suit local conditions and then form innovative institutions.

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