

COMPLETION REPORT

Avoiding the Middle-Income Trap: The Role of Foreign Aid in Japan and South Korea's Transition to Upper-Income Status

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This study explored the role of foreign aid in Japan and Korea's successful transition to advanced-country status and thus in overcoming the so-called middle-income trap. Before achieving high-income status, both countries had received financial assistance particularly from the United States and the World Bank. The study's objectives were twofold: One, to understand how foreign aid was used in Japan and South Korea at the time of their transition and two, to examine the conditions which allowed aid to contribute effectively to their development. To attain the two objectives desk review, secondary data analysis, and interview of selected key informants were conducted. A framework of analysis where aid is viewed as a fungible resource that performs catalytic instead of leading role in development has been employed. It was argued that the principles of ownership and alignment as well as the concepts of 'internalization' and 'scaling up' were clearly present in the way Japanese and Korean governments had managed aid projects long before these principles were introduced in high-level forums on aid effectiveness. For aid to assist in avoiding the trap it must contribute directly or indirectly to industrial innovation and competitiveness. Direct contribution covers projects that benefited the industrial and infrastructure sectors while indirect contribution is a result of either internalizing a knowledge/ know-how acquired from an aid project and getting them to scale or taking advantage of aid fungibility by allotting more resources for improvement of social capital such as quality of education and research and development (R&D). As the case of South Korea and Japan had shown, the study found that:

Foreign aid to these countries was highly sequential. During the early post-war period foreign aid was in the form of grant and was used mainly for emergency relief, food and budget support. Aid was later used for improvement of the quality of education and institutional capacity which were necessary in internalizing and scaling up skills and technology from FDI and aid. As these countries began their way to upper middle-income status assistance was changed gradually to concessional loans and private financing. By 1990s in Korea the main source of funding gradually shifted to the private sector. Around 1960, the World Bank began to tighten its lending terms to Japan when Japan had begun to show its ability to borrow in international financial markets. Foreign aid uses were aligned with their national development plans and were earmarked for infrastructure development and industrial upgrading at the time of transition. In Japan a total of thirty World Bank loan projects worth USD 862.9 million were implemented between 1953 and 1966. Meanwhile, U.S. and UN assistance to South Korea between 1945 and 1975 was USD 4.424 billion. Almost all of the World Bank loans in both countries were used to finance infrastructure and industrial investments through two-step loans. Japan and South Korea succeeded in internalizing skills and technology acquired from aid-funded projects. In Korea iron and steel producer POSCO learned basic technology from Japanese technical cooperation under reparations payments. Finally, Japan and Korea adopted 'exit plans' from aid.

Publication of the Results of Research Project:

Verbal Presentation (Date, Venue, Name of Conference, Title of Presentation, Presenter, etc.)

- (1) To be presented at the International Conference of Japan Studies Association (JSA)-ASEAN in December 2016 in Cebu City, Philippines. Title: "Role of Foreign Aid in Overcoming Middle-Income Trap: Lessons from Japan and South Korea"
- (2) An expanded version will be submitted for presentation at the International Convention of Asia Scholars [ICAS 10] which will be held in Chiang Mai, Thailand on 20-23 July 2017.

Thesis (Name of Journal and its Date, Title and Author of Thesis, etc.)

The final draft of this study will be submitted to an academic journal for possible publication. I am thinking of three potential journals: (1) Third World Quarterly; (2) Asian Politics and Policy and (3) Asian Perspective.

Book (Publisher and Date of the Book, Title and Author of the Book, etc.)

This study would be part of the manuscript (book) that I am completing on East Asian Donors