KOREA'S SUCCESSFUL EXPORT PROMOTION STRATEGY: A LESSON TO ERITREA?

By

Eyob Kahsai Michael

THESIS

Submitted to
KDI School of Public Policy and Management,
in partial fulfillment of the requirements
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ABSTRACT

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The second half of the last century was difficult for many developing countries. Wide fluctuations in commodity price, the rapid accumulation of external debt, and changes in world trade and macroeconomic conditions have been among the many problems they have had to face. The Asian developing countries were able to adjust to these changing conditions and have been among the most rapidly growing countries in the world; and prospects for future growth remain bright. Developing countries in other regions, including African and Latin American countries, have been less successful; many are beset with problems, including huge debt burdens (where Brazil can be cited as an example), high inflation rates, and overall economic stagnation. Apart from these problems, African countries found themselves embroiled with civil war and famine.

To overcome these problems and achieve sustainable economic development Latin American countries resorted to Import Substitution Strategy (ISI) while Asian countries, particularly Korea, Singapore, Chinese Taipei and Chinese Hong Kong vigorously and aggressively pursued an outward looking and market oriented Export strategies. African states mostly attempted to adopt economic policies prescribed by their former colonizers. The result was diametrically opposed. Latin American countries virtually stagnated while Asian countries; particularly the four countries mentioned above – the Asian Tigers, scored a remarkable economic growth. Almost all African countries experienced negative growth.

The reasons why different regions scored different economic growth may be many but no one can deny that the economic policy pursued by each one is the main culprit. It is here where the picture of my country Eritrea comes. As a new nation that has recently joined the World community, it has ample opportunities to learn from the successes and failures of other countries.

The aim of the paper is, thus, to see whether Eritrea can learn from the success of Korea. This research paper attempts to draw compelling lessons from the remarkable success of Korea's export promotion strategy as an engine of growth. The paper starts by assessing Eritrea's economic and trade policies and performances and goes into analyzing Korea's export promotion strategies mainly of the 1960s – the era Korean miracle begun, and relating Korean economic, social and political situations to the Eritrean situation. After doing so, the paper identifies those lessons pertaining to Eritrea. The paper also critically reviews Eritrea's trade policy instruments and institutions. An attempt is also made to

give a bird's eye view of WTO protocols that need to be taken into consideration when and if Eritrea decides to join the Organization.

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I feel it is fitting to express my gratitude to KDI School for giving me the opportunity to pursue for my post-graduate studies.

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Introduction

ERITREA, a newly born African Nation, is located in the Horn of Africa, bordered on the north-east and east by the Red Sea, on the south-east by Djibouti, on the south by Ethiopia and on the west and north-west by the Sudan. The total area of Eritrea is about 124,000Km^2 and includes the Dahlak Archipelago, a group of around 365 islands lying off the coast of the port of Massawa. Its Red Sea coastline extends for about 670 miles (1,000Km). Eritrea became an independent state in May 1991 and the Eritrean population confirmed its support for independence in an internationally supervised referendum held in April 1993.[1]

The 30 years of war for liberation and years of recurrent drought left the economy virtually crippled and devastated. The cost of freedom in terms of loss of human life, displacement of population, economic and social disruption and environmental degradation was enormous.[2] The Government of the State of Eritrea inherited a country with virtually no physical and institutional infrastructure. To add insult to injury, when the Eritrean economy was about to take-off our neighbor to the south – Ethiopia opened war under the guise of border dispute. This war also aggravated the already dilapidated economy.

The Government of the state of Eritrea is now faced with immense challenges of reconstruction. It has to rehabilitate and transform the war ravaged socio-economic system while at the same time laying sound foundations for its further development. One of the prime objectives of the Government is to alleviate poverty of the people. To tackle this huge task different remedies and policy recommendations can be prescribed. One is

[1] Eritrea Investment Brochure, 1993.
[2] Macroeconomic Policy of the Government of the State of Eritrea, Nov. 1994.

to reform the trade policy in such a way as to boast export volume and to increase income of the poor so as to eventually achieve sustaining growth and development.

The Objective of the Paper

Eritrea has been less than successful in integrating into the world economy and benefiting from trade reform programs. The reasons are many. Chief among them are lack of viable trade policy, weak trade and financial institutions, low level of foreign direct investment, lack of effective complementary policies and institutions. In order to create an enabling environment that would stimulate the supply side of the economy that generates employment and economic growth, there must be a viable trade policy, along with those key ingredients that are lacking in Eritrea – investment climate, investment in human capital, infrastructure, good governance in public and private sector, efficient financial sector, etc.,

The objective of the paper, thus, is after assessing Eritrea’s trade policy and export performance, and critically analyzing trade policy and strategy pursued by successful country – Korea, and WTO rules and regulations, to come up with trade policy proposal, which I believe would help as a basis for policy makers of the country.

Structure of the paper

The structure of the paper will be as follows: After briefly introducing Eritrea’s economic and trade policy in chapter I, Eritrea’s export trade performance will be discussed in section II. In Chapter III, literature review regarding trade policy will be presented. The reason why Korea is chosen as a source of a lesson will be discussed in chapter IV. In Chapter V an attempt will be made to identify Korea's Export Promotion Strategy of 1950s and 1960s. Situational Analysis between Eritrea and Korea will be discussed and evaluated in section VI. In Chapter VII the most important lessons from Korea will be discussed and evaluated. The principal trade policy instruments and institutions are discussed and evaluated in Chapter VIII. The most important complementary policies are discussed in Chapter IX.

Given the importance of agriculture and business services for a poverty reduction strategy that employs trade, these sectors are accorded special section - Chapter X. At last, Concluding remarks and Policy recommendations are forwarded in Chapter XI. In the appendix section Eritrea's economic indicators, trade statistics and other relevant statistical date are presented.

Chapter I

Eritrea's Economic Policy

After Eritrea won its independence in 1993 and the dust of war settled, it downed on the liberation army turned Government of Eritrea the severity of the damage inflicted on the economy by the defunct government of Ethiopia. Once a vibrant economy, the country was destroyed beyond comprehension. Therefore, to kick-start and to spur the wheel of the economy, the Government of Eritrea needed to create a policy to guide the long-term economic development of the country. As such, the Government is currently engaged in creating a modern, technologically competitive economy where the private enterprise is the driving economic force. To achieve this goal, the Government has adopted a broad based growth strategy that has aspects of rehabilitation, reconstruction and development covering all sectors of the economy (Macroeconomic Policy the Government of the State of Eritrea, Nov. 1994). The strategy's main components are to: -

- Improve agricultural production and productivity through the development of irrigated agriculture and assist peasants, pastoralists and agropastoralists to enhance their productivity by providing new farming and grazing methods;
- Develop capital and knowledge intensive, export oriented industries and services;
- Develop tourism sector;
- Create an internationally competitive financial sector;

- Develop and systematize a public health care system;
- Provide a broad based education system and improve access to it;
- Provide effective social welfare and safety net system; and
- Safe guard and upgrade the environment from undue pollution.

The centerpiece of this strategy is the establishment of an efficient, outward looking, private sector-led market economy with the Government playing a pro-active role to stimulate private economic activities. While the public sector would normally be restricted to those areas that the private may tend to avoid, public investment programs in strategic sub-sectors can be initiated to stimulate economic growth and supplement the efforts of the private sector. In such cases, all strategic public investments will be operated on commercial bases, and eventual divestiture would not be excluded.[3]

In keeping with these development objectives and strategies, the Government designed a macro-policy framework to stimulate private investment and engender economic revival and growth. The thrust of the policy is the swift transition to a market economy, a liberal trade policy, a central role for the private sector and export – led growth.

As part of the macro-policy the investment proclamation is designed to mobilize investment capital from internal and external sources for export industries, by having external trade taxes and exchange rate regimes that favor exports. It also aims at creating and expanding employment opportunity, encourage the introduction of new technologies to enhance productivity, and foster the growth of small and medium scale enterprises. The proclamation provides incentives such as a nominal 2% tax on capital goods,

[3] Macroeconomic Policy of the Government of the State of Eritrea, Nov. 1994.

industrial spare parts and raw materials, and exemption from export duties and sales taxes for exports.[4]

Income taxes have been re-evaluated to range from 2 – 30% on corporate profit, 2-20% on commercial agricultural profit, 2 - 30% on rent income. On top of these, any corporate profit that is set aside for re-investment shall be taxed at the rate of 20%. There shall be no taxes on declared dividends. The proclamation also allows loss incurred during the first two years of operation by an investor to be carried forward for three consecutive years. Foreign exchange may be remitted out of Eritrea for, among others, net profits and dividends accrued from investment capital, debt-service payments for foreign loans incurred pursuant to the proclamation, and payments received from the sale or transfer of shares. Investors may retain up to 100% of their export earnings in foreign currency in Eritrea in accordance with Bank regulation.[5]

Closely tied to the success of any investment is the allocation of land. The land proclamation eradicates the antiquated practices of land allocation and creates a new system where ownership of all land is vested in the Government. This proclamation will spur growth by making land for business and residential purposes easily accessible to all who would put it to use.

Trade Policy

The Government of the state of Eritrea has also made it clear in its trade policy that it would:[6]

- Foster liberal internal and external trade regimes with limited intervention that would not contradict the tenets of free trade. This will mean, among other things,

[4] Gazette of Eritrean Laws, Vol. 10/2001 No. 4, Septmber 24, 2001.
[5] Ibid.,
[6] Macroeconomic Policy of the Government of the State of Eritrea, Nov. 1994.

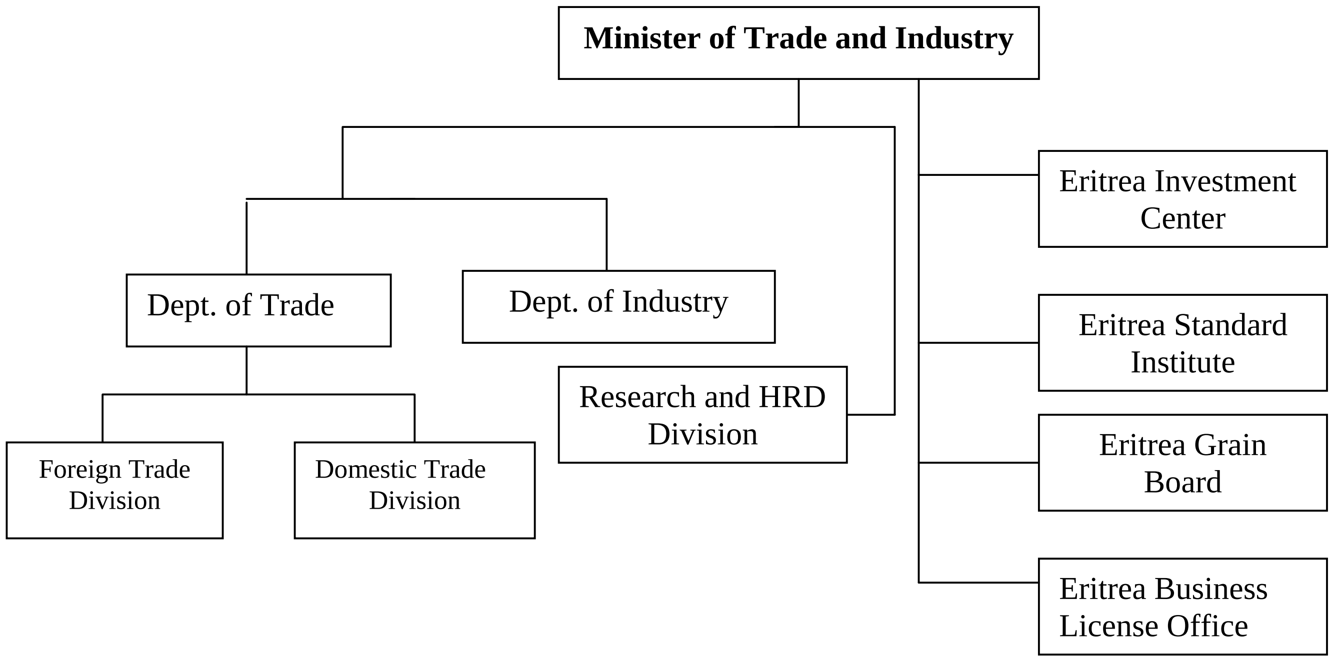
liberalizing and simplifying the licensing regime and reducing and eliminating tariff and non-tariff barriers;

- Foster export and export based industries and services by providing preferential financing, assistance in international market penetration and strong promotional support to aid exports, and support mechanisms for quality and standards control;
- Encourage participation in regional bilateral and multilateral trade and economic cooperation;
- Assist and encourage the private sector to play a leading role in both domestic and external markets;
- The role of the public sector will be limited to regulatory functions and the import and export of critical commodities and supplies required in several sectors.
- Help build the institutional capacity that would make Eritrea a trading country;
- Encourage and support participation of Eritreans living abroad in trading activities.

Despite these policy aim, the country lacks policy such as anti-dumping, countervailing measures, subsidy, and safeguard measures. The country is not a member of WTO, too. The country’s current tariff and other trade related issues are discussed at great length in chapter VIII.

Trade Institution

Ministry of Trade and Industry



Chapter II

Eritrea's Trade Performance

Eritrea's major exports consist of primary products such as live animals, fish, sesame seed, natural gum (gum Arabic) salt and manufactured products such as leather and leather products, textiles and garments, and intra-ocular lenses. Imports consist mainly machinery, motor vehicles, pharmaceuticals, electronic appliances, wheat, sugar etc.,[7]

Historically, Eritrea has been a trading nation, given its strategic location and easy access to the markets of the Middle East and Africa. In the 1940s its export base was relatively diversified earning – by 1970s – approximately USD 100 million worth of foreign exchange per year. During that period a variety of its industrial products used to be exported to Djibouti, Cyprus, Egypt, Ethiopia, Iran, Sudan, Yemen and other neighboring countries.[8]

At present there are over 40,000 licensed traders in the country. Added to those who carry trading activities in the informal sector, it can be fairly concluded that next to agriculture trade is the economic activity that accounts the highest for the livelihood of the Eritrean population.

As mentioned above Eritrea's economy, at the time of liberation, was virtually destroyed. To revive such a devastated economy needs a huge investment and a tremendous effort.

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[7] Trade report, Ministry of Trade and Industry, Government of the State of Eritrea, 1998.

[8] Ogbazghi, Bereket-AB, A collection of Country Report, Courses on Trade Promotion Strategies for African Countries, KDI & KOICA, 2000.

During the first five years of independence, where Eritrea breathed peace for the first time in its history, the country in general and the economy in particular managed to score a very commendable achievements – unprecedented in post-colonial Africa. The economy was growing at 8% per annum.

During those glorious years Eritrea's main trading partner was Ethiopia. Over 60% of its product was destined to Ethiopia. However, once again war broke between these two neighboring countries and Eritrea's trade and economic growth started to trickle. As the trade statistics below indicate Eritrea's export was increasing steadily. Import also was growing in a much higher rate. This is because in those first five years machineries, equipments and other vital inputs for growth had to be imported.

In millions of Dollars

Year	**1993**	**1994**	**1995**	**1996**
Imports (CIF)	**275**	**396**	**401**	**514**
Exports (FOB)	**36**	**65**	**81**	**95**

Source: US State Department.

The table above shows import surpasses export by manifold, indicating that there is a huge trade imbalance. Trade statistics from 1995 - 2001 depicted in tables 1, 2, and 3 (appendices) also confirm this trend.

Currently, Eritrea's main sources of hard currency are "remittances from Eritreans in Diaspora and loans from the World Bank, African Development Bank, Arab Development Bank, European Union and aid from donor agencies and governments". It is quite apparent that the Government of Eritrea cannot and should not rely heavily on these sources. It is high time to device ways and means to boast its export. And to do so, one of the prime objectives of the Government should be "to assess its trade policy and instrumental mechanisms" and find remedial solutions to all the stumbling blocks to the growth of export trade. This is what the paper aims to accomplish – to assess the country's trade practices and suggest remedial solutions.

Now that the war with Ethiopia is over the Government of Eritrea has shifted its focus towards reconstruction and rehabilitation. As recently as eight months ago, i.e., last May 2002 the Government proclaimed "Eritrea's Marshal Plan – titled Warsay – Yekaalo" in memory for those gallant Eritreans who gave their lives for the liberation and defense of the country. This plan is Eritrea's own version of the Marshal Plan. Issayas Tesfamariam, an Eritrea described it as "...It is a comprehensive, revolutionary, and an all-out, all-round economic rehabilitation and recovery program that is designed not to be only a "mere palliative" but rather to be a "crucial lubricant in the engine of comprehensive economic recovery".[9] One of the prime objectives of the plan is to alleviate poverty. And one way to alleviate poverty is through a comprehensive trade reform. Definitely Eritrea's trade policy and mechanism has to undergo reform so as to ensure a speedy recovery of the economy.

[9] Wefri Warsay-Yekaalo – Eritrea's own marshall Plan, June 16, 2002, www.biddho.com

Chapter III

Trade and Development:
Export Promotion VS. Import Substitution

As indicated in chapter II above trade policy of Eritrea aims at boasting free trade. Aim alone would not bring the desired result. It has to be augmented with effective trade mechanisms and policies. Evidence is that the economy remained stagnant. The reason is multi-faceted. One reason could be failure to revive and develop the domestic industries. The other and main factor is failure to institute the right strategies and effective institutional settings. The evolution of Eritrea's domestic industries dates back to the 1930s when the country was under the Italian colony. Eritrea was the most industrialized country in the Horn of Africa. However, thirty years of armed struggle and deliberate policy of neglect and mismanagement by the last two oppressive regimes of Ethiopia brought the industrial activity of the country almost to a standstill. Agriculture, too, is very traditional and underdeveloped. The same is true with the other economic sectors. The question one may ask would then be what trade strategy should Eritrea follow so as to revive its economy and be able to achieve sustainable development: Import substitution or export promotion?

Import – Substitution Industrialization Strategy

One of the problems that developing countries face in trying to improve their development growth rate is failure to identify ways to integrate their economies with the world economy. The basic question is whether they should encourage international trade with other countries or focus more on producing goods that substitute for international trade. There are two approaches. One approach is called the Import substitution.

The strategy of Import Substitution Industrialization (ISI) entails replacement of commodities previously imported (usually manufactured goods) with domestic production. It includes a number of industrialization policies based on a very little degree of international openness.

It was initiated in many Latin American Countries (LACs) as a reaction to the disruptions caused by WWI and WWII, the economic depression of the 1930s.[10] After 1955, ISI was pursued as a deliberately industrialization strategy. It was stimulated mainly by the thoughts of Prebisch and Singer in the 1950s.[11]

Developing countries have virtually no power in international competition and therefore cannot develop domestic market for export. So they may choose an import substitution policy naturally. Countries can develop their market when they choose import substitution policy primarily, because this policy makes a barrier of import from their countries so that domestic market can improve. According to this protection, domestic

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[10] Sato, Akihiro, IS and EP policy for trading, College of Policy and Planning Sciences, University of Tsukuba, June 25, 2002.
[11] Krueger, Anne O., The Effects of Trade Strategies on Growth, Finance and Development, June 1983.

market can develop with balanced and stabilized[12]. Akihiro Sato argues, "…Historically, many Asian countries have developed with an import substitution policy at first step of developing process. Similarly, developing countries can improve their market with an import substitution policy. The advantages in this policy make their market grow because of some restrictions for trading particularly import from other…" [13] However, the experience of Latin American Countries particularly that of Brazil indicate that at first the policy seems to work well but later on it tends to be less and less successful the longer it continues.

The table[14] below shows the difference in economic growth in countries that have tried the import substitution strategy compared to those that have tried the export-led growth strategy. The table compares four countries: Brazil, Colombia, South Korea and Tunisia over a 23-year period. Brazil switched from an import-substitution strategy to an export-led growth strategy and saw increased economic growth. By the 1970s, economic growth in Brazil was in double digits, much higher than in the 1950s and early 1960s. The change was also dramatic in Colombia.[15] The most dramatic change has been in South Korea. The Korean success story, which begun in the 1960s, seems related to the switch from an import-substitution strategy to one relying on trade and export growth.[16] The same basic phenomenon is apparent in Tunisia as well as many other countries.

[12] Liang, Hong, A thesis on the rationals of import substitution industrialization strategy, ISBN: 1-58112-007-9, University of Denver, USA.
[13] Sato, Akihiro, IS and EP policy for trading, College of Policy and Planning Sciences, University of Tsukuba, June 25, 2002.
[14] Urrutia, Miguel and Seiji Naya, "Lessons in Development: A comparative study of Asia and Latin America", International Center for Economic Growth, 1989.
[15] Ibid;
[16] Hyun Nam, Chong, Paper presented to the eleventh Pacific Trade and Development Conference, Sept. 1980, KDI, Seoul, Korea.

Country	**Period**	**Trade Strategy**	**Growth Rate**
Brazil	1955-0	Import substitution	6.9
Brazil	1960-5	Import substitution	4.2
Brazil	1965-0	Export-led	7.6
Brazil	1970-6	Export-led	10.6
Colombia	1955-0	Import substitution	4.6
Colombia	1960-5	Import substitution	1.9
Colombia	1970-6	Export-led	6.5
South Korea	1953-0	Import substitution	5.2
South Korea	1960-5	Export-led	6.5
South Korea	1970-6	Export-led	10.3
Tunisia	1960-0	Import substitution	4.6
Tunisia	1970-6	Export-led	9.4

I strongly believe that this experience indicates that a better strategy for increasing economic growth is to be outward looking rather than inward looking. A country's chance of catching up is greatly increased if it can adopt technology and use investment from abroad. By engaging in international trade, countries are able to learn more about technologies in other countries. For example, as South Korea's exports of electronic equipment grew, the Koreans learned more about technology for producing electric goods.

More countries appear to be changing their policies from inward looking to outward looking, based on this experience. Mexico, for example, lowered its restrictions on imports in the mid-1980s and joined the United States and Canada in a free trade area in the 1990s.[17] However, Akihiro Sato argues as "…For free trading, there is no protection barrier so foreign companies can enter into domestic market. And at last developing countries' markets can improve by efficient management of the foreign companies and low domestic labor cost. But this system has also disadvantages. When we talk about free trade, domestic market must be opened. So if domestic market has not improved enough, foreign companies may control their market. Export promotion policy has foreign companies in developing countries, instead of free trade's benefits".[18]

As a result, I can say import substitution policy is a prerequisite for export promotion development policy. This allows some degree of industrialization to take place, some development of an industrial labor force, and some expansion of modern infrastructure. All of these are necessary for export led development.

Export Promotion Strategy

As the facts presented in the table above indicate an alternative way to increase growth is the export-led strategy. Under this strategy, expanding exports encourages international trade. Hence, the strategy tends to be outward looking. Growth occurs through the manufacture and sale of products to other countries. The aim of export-led growth is to

[17] Javier Prieto, Francisco and Sherry M. Stephenson, "Regional Liberalization of Trade in Services", Development, Trade, and the WTO, A Hand Book, World Bank, 2002.

[18] Sato, Akihiro, IS and EP policy for trading, College of Policy and Planning Sciences, University of Tsukuba, June 25, 2002.

increase trade rather than reduce trade. Although many countries that have followed export led strategies have also had high tariffs on some commodities, such as agricultural goods, their strategies have been much more outward looking than those of the import substitution.[19]

The 1987 World Development Report (WDR87) of the World Bank uses the evidence provided by Greeaway and Nam (Kyklos, 1988) to suggest that the performance of outward looking economies has been superior to that of inward looking economies.

What, then, is the advantages of export led strategy?

Urrutia, Miguel and Seiji Naya enumerate them as follows:[20]

- Export promotion is a better policy because it involves incentives rather than controls, and because measures can be applied more generally across the board. Whereas import substitution policies discriminate against exports and create market distortion, many export promotion policies give similar incentives to production for domestic and export markets. Whereas import controls are usually highly selective, export incentives usually do not differentiate much between individual export commodities.
- It is easier to detect the effectiveness of export promotion policies because export performance can be observed easily and the policy mistakes of export promotion corrected more quickly.
- Export promotion gives industries the opportunity to enlarge their markets and achieve greater economies of scale.

[19] Krueger, Anne O., The Effects of Trade Strategies on Growth, Finance and Development, June 1983.
[20] Urrutia, Miguel and Seiji Naya, "Lessons in Development: A comparative study of Asia and Latin America", International Center for Economic Growth, 1989

- Export oriented development forces industries to compete in the international market and achieve greater efficiency.

Keesing[21] also argued that under an export promotion regime, international competition forces domestic entrepreneurs to pay close attention to the possibilities to innovations and speeding up the learning processes.

Then, which strategy should Eritrea use to achieve rapid economic growth? Import substitution or export promotion?

My view is the following:

The history of Latin American Countries show that import substitution could not bring the desired result, though the effectiveness of any policy depends on the prevailing domestic and external conditions. Development of an export-oriented economy will be crucial to Eritrea's rehabilitation and its long-term sustainability, too. There are several reasons why this strategy will be the most beneficial. Eritrea's past performance indicates that it can handle a much larger export base. Eritrea is but a small country with a very narrow domestic market. Once the needs of its small market have been met, export expansion will be the main engine of growth. Its proximity to the Arabian Peninsula gives it greater advantage to competitively export to the Arab countries. If Eritrea decides to follow export led strategy, then there are major lessons t be drawn from the Korean experience with trade policy. On the other hand, I believe there must be some sort of protection to the infant domestic industries until such time they become competitive in

[21] Keesing, Donald B., "Outward Looking Policies and Economic Development," Economic Journal, June 1967.

the world market and are financially strong. However, there must be time limit to the protection.

Chapter IV

Why Korea?

As indicated in the introductory remark, as a new member of the world community, Eritrea has the advantage to learn from the successes and failures of all the countries of the world. As failure is the mother of success, Africa's failed states teach Eritrea to avoid the path these countries pursued. On the other hand, Eritrea can amply learn from the successes of "The Asian Tigers", namely, Korea, Chinese Taipei, Chinese Hong Kong and Singapore. From these four countries it is Korea's economic and political situations in the 1950s and 1960s that strikingly resemble today's Eritrea. For this reason alone, it is tempting to take a lesson from Korea's export promotion strategy. Then, what are the similarities between Eritrea and Korea?

Political Similarities:

Both Eritrea and Korea share more or less the same turbulent histories. Both were victims of colonial aggression. Both countries fought bitter wars for their independences. Both countries had to fight for their survival after achieving independence. Korea had to go through the civil war of 1950 – 1953 and Eritrea had to fight for its existence and sovereignty against Ethiopia during 1998 – 2000 border war. Again, though they are geographically very far apart, both of them are located in areas that are militarily and economically very strategic, which makes them very prone to foreign influence and aggression. At the time of their independences from colonial rules, both countries did not have well functioning government settings.

The main difference between the two countries, however, is that the worldwide condition was favorable when Korea achieved its independence. The early years of the 60s were the time when the Cold War was at its height and was characterized by the Cuban missile crisis. Hence to deter the spread of communism in East Asian countries, the US government was heavily involved in the political and economic affairs of Korea. To stabilize its economy and allure its people, the US generously extended its aid packages, which undeniably played a decisive role in capital accumulation. The year Eritrea won its independence, however, international political situation was quite different. The former USSR - "evil empire" crumbled, German unification took place, the Gulf War was a fresh memory, etc., Therefore, the US and Western Europe were busy containing the aftermath of the Gulf War and totally absorbed by the unfolding situation of the fall of communism. On top of these, Eritrea's independence was not warmly welcomed by the US and EU, as they know little about the guerilla army turned government and wrongly suspected Eritrea's independence will lead to the destabilization of the entire Horn of Africa, particularly Ethiopia. Due to these reasons, Eritrea was refused the desperately needed aid to heal the wounds of war and to kick – start the process of building a viable state.

Economic and Social Similarities:

During the colonial era of 1910 to 1945, Seong Min Hong argues that the Korean economy experienced rapid structural transformation. He further argues that the structural pattern of this development was largely determined by the Japanese colonial regime. As a result, the Korean economy experienced what is known as colonial enclave industrialization.[22] Eritrea's history is practically the same. Eritrea also experienced a very rapid industrialization during the Italian colonial era, 1886 – 1942. For its war efforts during WWII, Fascist Italy erected industries so as to ensure a smooth supply for its war machine.

After they won their independences, both countries inherited a devastated economy. Both experienced chronic shortage of food and unemployment. Both countries are not blessed with natural endowments. However, both countries are blessed with a very dedicated and resilient people - People that are fiercely patriotic and with "we can do" attitude. Both peoples have the same social fabric – both enjoy extended family ties, friendship and communal life.

Their significant difference is "population size". Even though both have more or less the same land size, Eritrea's population size is quite small as compared to Korea's. Korea's population size, in 1945, is estimated to be 16 million[23] while that of Eritrea is only 4 million. Korea is, also, made up of one ethnic group – one language, one history and one

[22] Seong Min Hong, KIME Mideast Studies, 2001
[23] Ibid;

culture[24] while Eritrea is multiethnic country – nine different languages, nine different ethnic groups and cultures.

The other main difference is that Korea had a relatively literate labor force while Eritrea was and is devoid of this wealth.

Problem Statement:

The economic, political and social resemblance between these two countries, though are half of the globe apart from each other, is persuasive enough to make the hypothesis that "Korea's export promotion strategy led to higher per capita income; lessons for Eritrea". The export promotion strategy that Korea pursued in achieving higher per capita income is a good lesson for the Eritrean case.

[24] Ibid;

Chapter v

Korea’s Export Promotion Strategy: 1950 –1960s

In his paper, Seong Min Hong explains that Korea was totally in disarray after it won its independence from Japan in 1945. There was considerable disruption after 1945 because of plant exhaustion; loss of linkages with Japanese capital and loss of technical expertise, distribution systems and markets; and the subsequent obliteration of the industrial plant during the Korean War (1950 –1953)[25]. He further says that the Korean War destroyed almost two-third of the nation’s productive capacity, and almost 1 million civilians were killed. Jungho Yoo explains the decade that follows as: “…The rest of the decade was spent recouping from its destruction. The thrust of economic policy was import-substituting industrialization behind high protective barriers. The aid that the US extended to Korea was the main source of foreign exchange. However, when the US made it known that it would no longer extend its financial aid, the masses’ subsistence was put at risk, since US aid financed most imported goods such as grain and other food stuffs.”[26]

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[25] Seong Min Hong, KIME Mideast Studies, 2001

[26] Jungho yoo, Neoclassical versus Revisionist View of Korean Economic Growth, Discussion paper No. 588, Harvard University, June 1997.

Export Promotion Strategies in the 1960s

The decision the US made to stop aid forced the Korean government to look for alternative sources of foreign exchange. One possibility was to increase export, thus the slogan "nation-building through exportation"[27]. To promote export the government had to take a series of policy measures. One of many incentives introduced was unification of the exchange rate, and the currency, the won, was twice devalued to correct overvaluation – which was the cause of a large excess of import demand over export.[28]

Tax exemptions were also widely used. For example, Bon-Ho Koo explains that imported inputs destined for export production were exempted from tariffs.[29] A key incentive, however, was the introduction of preferential credit scheme for exporters. This scheme allowed exporters to enjoy automatic access to bank loans, usually at well below market interest rates. On top of these, other incentives such as wastage allowances for tax purposes, export-import link schemes and reduced public utility rates were offered at one time or another, and a cash subsidy for exports operated briefly in the early '60s.[30] To provide exporters with information on foreign markets, the Korea Trade Promotion Corporation (KOTRA) was established in 1964.[31] In addition, the 1960s saw the first steps toward import liberalization. Korea joined the GATT in 1967. This openness to international market allowed the world's technological frontier to be absorbed by Korea.[32]

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[27] Jong-Il, You, A reflection on the Korean Miracle: Toward a New Concept of Development, 1995.
[28] Seong Min Hong, KIME Mideast Studies, 2001
[29] Bon-Ho Koo, Korea's Experience of Economic Development, KDI, 2002.
[30] Seong Min Hong, KIME Mideast Studies, 2001
[31] Tae-Yong Yoon, Planning for export led growth and development in the Republic of Korea
[32] Seong Min Hong, KIME Mideast Studies, 2001

The success of Korean Industrialization

Korea's successful industrial growth began in the early 1960s, when the government instituted sweeping economic reforms emphasizing exports and labor-intensive light industries. The government led economic development in its early stages since the private sector was weak. Government intervention in economic areas such as resources allocation complemented the creativity and market principles of the private sector. As indicated in the preceded paragraph, during this period, the government strengthened administrative support for industries. Apart from replacing trade laws with new international trade law and the establishment of KOTRA, the government also held monthly trade promotion conferences to evaluate export promotion measures and to work out the difficulties related to exports.[33]

Introduction of Foreign Capital

For economic development, it was and is necessary to accumulate capital formation. Thus, for Korea, the mobilization of funds for capital formation was the most pressing economic problem.

Even though the government attempted to mobilize domestic funds for capital formation in the 1960s through various policy measures, it was impossible to provide sufficient funds for the voracious investment demand.[34] There was only one-way to fill this gap:

[33] Bon-Ho Koo, Korea's Experience of Economic Development, KDI, 2002
[34] Jungshik Son, Money and banking for economic development – Korea's early development decades.

foreign capital introduction. To this end, several laws promoting foreign capital inducement were rewritten into a single bill, the Foreign Capital Inducement Act.[35] This aimed to stimulate foreign loans, investment and technology transfers by providing tax shelters and extending tax exemptions, warranting free remittance and repayment guarantees by the government or government-owned commercial banks. Unlike foreign aid, these foreign loans had to be paid someday, therefore efficient and productive uses were imperative and the government set up various screening processes to weed out unimportant or unproductive projects.[36]

In the 1960s, the government welcomed foreign capital inflows without paying too much attention to the debt-servicing burden, terms of financing, linkage effects or the unfair competitive edge of large industries borrowing abroad at lower interest rates over the small and medium industry borrowing in the domestic market which had to borrow at higher rates.

The Role of the Government

In 1961 General Park Chung Hee overthrew the popularly elected regime of Prime Minister Chang Myon. Seong Min Hong argues that Park's prime objective, after his accession to power, was to transform the country from an agrarian economy into a modern industrial powerhouse.[37]

He decided, then, that his administration has to play a key role in the economic development of the country because no other Korean institution had the capacity or

[35] Seong Min Hong, KIME Mideast Studies, 2001
[36] Ibid.;
[37] Ibid;

resources to direct such drastic change in a short time. The resulting economic system incorporated elements of both state capitalism and free enterprise. However, the revisionists counter argues that there was extensive market intervention by the state.[38] Which I believe is the case because the Korean government provided the vision of future economic development around which the private firms' investments are organized. Therefore, investments were done not according to the laws of the market but were directly coordinated by the state. One of the key initiatives of the Park government was to create a powerful central economic policy coordination body, the Economic Planning Board. This agency took charge of designing and executing Five-Year Economic Development Plans, which contained both macroeconomic planning and industry-level indicative planning.[39] The economy was dominated by a group of Chaebol, large private conglomerates.

The government guided private industry through a series of export and production targets utilizing the control of credit, informal means of pressure and persuasion. In 1961 Park extended government control over business by nationalizing the banks and merging the agricultural cooperative movement with the agricultural bank.[40] The government's direct control over all institutional credit further extended Park's command over the business community. The government provided incentives through the allowance of subsidy loan to invest in the priority industries. The government also took a central role in "projecting

[38] Jungho yoo, Neoclassical versus Revisionist View of Korean Economic Growth, Discussion paper No. 588, Harvard University, June 1997.
[39] Ha-Won Jang, Jong-Il You, Changing Role of the State in South Korea: From Leading to Supporting the Market, 2001.
[40] Jungshik Son, Money and banking for economic development – Korea's early development decades

a vision and mobilizing and allocating financial resources, but left actual business activities mostly to the private sector”.[41]

To sum up, the most important factor of Korean economic growth was the government’s will to transfer the labor force from latent unemployment to employment in the process of economic development.[42] In 1960s, Korea had a high quality and plentiful low price labor force. Foreign capital played a great role to set on labor force, potential for development. Owing to the lack of capital accumulation in agricultural sector, influx of foreign capital was an indispensable factor to develop the country at the outset. In short, Korean economic growth can be characterized as a government-led, foreign capital-depended, industrialization-promotion and export-oriented.

Social Costs of the Korean Development Strategy

The development strategy pursued by Korea brought a huge material benefits to the Korean people. From 1950s up to 1980s Korea scored a remarkable transformation from a back-warded economy to an industrial powerhouse. Its GDP growth rate averaged 8.8% during 1963-1990. GDP per capita reached $6,250 in 1991 as compared to that of the early 1960s, which was only $87.[43] The change in the structure has also been impressive: the contribution of the agricultural sector in terms of employment and GDP declined from 63% and 43.4% in 1963 to 16% and 9% in 1990. While those of the manufacturing

[41] Ha-Won Jang, Jong-Il You, Changing Role of the State in South Korea: From Leading to Supporting the Market, 2001.
[42] Seong Min Hong, KIME Mideast Studies, 2001
[43] Professor Park, Hun Joo’s lecture, Democracy, Ethics and Public Policy, KDI, 2002.

sector rose from 8% and 15% in 1963 to 27% and 29% in 1990.[44] The tables below show how remarkably share of exports in GDP and industrial origin of GDP increased from 1961 up to 1990.

<u>Share of Exports in GDP</u>

Year	Share of Exports in GDP	Share of Manufacturing Goods in Total Exports
1961	3.2%	15.2%
1970	14.7%	77.4%
1980	32.0%	90.2%
1990	36.7%	93.8%

Source: Bon-Ho Koo, Korea's Experience of Economic Development, KDI, 2002

<u>Industrial Origin of GDP</u>

Year	Mining and Agriculture	Manufacturing Electricity and Construction	Services
1961	48.8%	12.3%	38.9%
1970	32.4%	27.1%	40.5%
1980	16.2%	40.1%	44.1%
1993	7.4%	43.0%	50.8%

Source: Bon-Ho Koo, Korea's Experience of Economic Development, KDI, 2002

However, this remarkable economic growth is not with out cost. Jong-Il You and Ha-Won Jang argue that these costs are:[45]

1. Political Freedom and Human Rights. General Park's government main concern was economic development at any cost. Therefore, he neglected the basic human rights and political freedom of the people. He employed an authoritarian style of

[44] Jong-Il, You, A reflection on the Korean Miracle: Toward a New Concept of Development, 1995.
[45] Ha-Won Jang, Jong-Il You, Changing Role of the State in South Korea: From Leading to Supporting the Market, 2001.

administration, which resulted in gross human rights violation and political persecution.

2. The other victim of this growth – maximization policy was the art of living together: Equity and community. The rapid industrialization led to a substantial disparity in income distribution. The enormous concentration of power and financial resources in the hands of Chaebol and their monopolized access to preferential loans and low-interest rate bank financing crowded out small and medium-sized business into the unorganized money markets. The other area where inequality loomed large is "regional inequalities".
3. The environment was practically neglected during the massive industrialization process. The damage inflicted on to the environment is very high.

Chapter VI

Situational Analysis

Policies alone would not guarantee success. Policies can only make miracle if and only if the necessary conducive conditions are laid down. African states have beautiful policies but because they lack the necessary and vital conditions that would enable them to effectively implement their policies, they miserably failed to achieve what they set off to accomplish. Park's government managed to boast Korea's export and thereby the country's economy simply because it could create and lay dawn the necessary conditions that would give rise to export promotion, albeit its undemocratic, ruthless and biased political system.

Here I will attempt to show that Eritrea fulfills those conditions and hence Korea's export promotion strategies are good lessons to Eritrea to promote and expand its export base. This does not, however, to mean that Eritrea has to resort to the type of government Korea had in the 1960s. I believe a democratic government committed to the cause of the people would be much more stronger in implementing its policies and rally the people behind its economic policies.

A. Political Situation

However the Park government, the driving force behind Korea's economic success, was an authoritarian, it was a strong, committed and consistent government. Jong-Il You describes the Park government as follows:

"…It was beyond dispute that the Korean state has had an unusual ability to impose its policies with little resistance from either the capitalist class or the working class. Not only was its hands free to pursue relentless growth-maximization policies, but it was able to discipline errant capitalists or trouble-making workers who deviated from the course of action set out by the economic development plans".[46]

Jong-Il You further argues that one of the reasons why the Park government committed itself to development was, through economic development, it wanted to erase the illegitimacy of the coup.[47] The strength of Park government emanates from weak social classes, the capitalists were dependent on the state, and landlords were stripped of their political and economic power through the land reform in the early 1950s. On top of these, Park's government ruthlessly crushed labor and popular movements.[48]

Eritrea has a guerrilla turned government that came to power after defeating Ethiopia's colonial army and got its legitimacy through the popularly elected general assembly. The government is very popular and strong that it faces little resistance to implement its policies. The source of its strength is its ability to effectively communicate with the people, by encouraging the people to participate in all the government's programs and by wholly embracing the peasantry. The selfless and simple way of life of the leadership has

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[46] Jong-Il, You, A reflection on the Korean Miracle: Toward a New Concept of Development, 1995
[47] Ibid;
[48] Ibid;

also deepened the love of the people for the government. However, unlike Park's government, Eritrea's government does not directly interfere in areas of investment nor does it try to control the rate of exchange. This does not necessarily mean that Eritrea has to continue the way it is now without instituting democracy. Once it put all the vital democratic and government institutions in place and instituted all the necessary laws, then it has to call for election. This way it can ensure the continuation of a strong government.

B. Land Reform

Type of ownership of land is one of the stumbling blocks to economic growth in all developing countries. Though Korea is not free from all the problems associated with land, it has at least managed to take a sweeping land reform policy, in the early 1950s. This land reform allowed the Park's government to have a free reign in its aggressive industrialization program.

One of the big policy measures that the government of Eritrea managed to implement is the land reform that was enacted in 1997. This land reform law transferred the ownership of the land to the government. However, it guarantees every Eritrean peasants will have enough land to farm. It, also, secures the right of women to own a land. Therefore, the government can now allocate land, on lease, for investors.

C. Human Resource

The people of Korea are obsessed by education. Every single family spends a fortune to educate their children. This helped Korea to acquire a highly qualified labor force. Korean success is nothing but the result of the sweat and dedication of its highly educated and disciplined work force.

Eritrea does not possess this blessing. However, it has been quite a while since the current Eritrean government realized that without educated work force nothing could be achieved. To this end, the government took a series of measures to enhance education. One is offering free education for all. The other is constructing schools in every town and village. To overcome shortage of teachers, it has hired teachers from India. The third and crucial measure it took was, with the 60 million USD it borrowed from the World Bank, it is sending all first degree holders to South Africa, Europe and the US for further studies.

D. Source of Foreign Fund.

As it is indicated in the preceding chapter, Korea's main source of foreign exchange was the US. The US not only extended its aid generously to Korea, but also opened its markets to Korean products and allowed it to borrow unlimited money from foreign banks.

Eritrea's relation with the US is strained due to various reasons. One is Eritrea feels betrayed and rightly so when the US took the lead in the mediation between Eritrea and Ethiopia during the 1998 - 200 border war. Also, the US usually attaches strings of conditions to its aid package, which forces countries to compromise their national interests. Eritrea's stand is to remain fiercely independent. However, there are some other European and Arab countries that have good relations with Eritrea. Besides, the World Bank, Arab Development Bank, African Development Bank and EU have good relations with the country. So, Eritrea does have a possibility to acquire seed funds to help her accumulate capital.

E. Adequate Communication and Transport Infrastructure

One of the most impressive achievements of the General Park's government is it connected the whole of Korea through well built roads. The whole Korea is intertwined by road. Telephone and other means of communications are part of the daily life of the people. Korea's stride in shipbuilding and car manufacturing further enhanced the sector. These help easy movements of people, resources and ideas.

Eritrea lags far behind most countries as far as communication and transport infrastructure is concerned. However, one of the priorities of the government of Eritrea is to make accessible, through roads, all of the country. To this end, the government has constructed, in the last six years, over five thousand km long roads and is constructing now over three thousand asphalted road, due to be finished mid next year. It is expanding and rehabilitating its two major ports, with the fund it secured from the World Bank. It has erected electricity-generating station worth 186 million USD, a fund secured from the

Arab Development Bank. It now entered into the program of electrification of the whole country.[49]

However, telecommunication, Internet services and other media outlets need massive investment. Before the 1997 financial crisis of Korea, joint venture agreement was reached between Eritrea and a Korea telecommunication company. The financial crisis of Korea killed the deal.

F. Location Advantage

Korea's geographical location is very strategic. To the north is China and to the east is Japan. Therefore, It can easily reach the big markets around it. Eritrea is, also, located in a very strategic area. It can reach markets of the Arabian Peninsula and Africa with ease.

G. Natural Endowment

Korea is not endowed with natural resources. It entirely depends on foreign supply for raw material and other inputs. Its food requirement is dependent on foreign supply, too.

Eritrea, on the other hand, though not yet fully assessed, is endowed with some precious metals, natural gas, abundant fish supply, and vast arable land. American, Canadian and Australian mining companies are exploring the potentiality of the resources. Also, the government is pushing, with every possible means, farmers and investors to enter into commercial agriculture so as to make Eritrea food self-sufficient. One may wonder why I

[49] www.shaebia.org

assert Eritrea has to strive to be food self-sufficient. The reason is that the people of Eritrea have been food aid dependent for the last thirty years due to war and recurrent draught. The people have to regain its confidence that it can feed itself! It is more of psychological than economic. Besides, agriculture could be a good source of foreign currency.

H. National Security

Jong-Il You argues that one of the reasons why the Park regime committed itself to development was,

"…The military leadership perceived that economic development was an imperative for national survival and dignity. For them, economic development was a national issue as North Korea was ahead of the South in economic strength in the early 1960s. The military leadership felt threatened by declining US aid and humiliated by their dependence on US support…"[50]

I believe national security of a country depends on its economic success or failure. The higher the economic success the more secure the country would be. All developed countries are free from the threat of war or other man made calamities. Some may counter argue by raising the issue of the 9/11 terrorist attack on US soil. But the US is so powerful it managed to contain it and cripple the AlQa'eda group. Korea's economic success, also, kept in check North Korean aggressive behavior. Therefore, the Korean

[50] Jong-Il, You, A reflection on the Korean Miracle: Toward a New Concept of Development, 1995

War, the of spread of communism in East Asian countries and the Viet Nam war were persuasive enough to motivate the Park's regime to push for speedy economic progress.

The grim reality of the Horn of Africa is that it is marred by war and famine. Eritrea's history is history of war. There is a constant threat to its national security and sovereignty from neighboring countries. To fend off its enemies, it is imperative that Eritrea has to be economically strong.

From the above discussion I conclude that I strongly believe Eritrea has all the necessary conditions that led Korea to kick start it export promotion. With proper and carefully tailored export promotion strategies, Eritrea is able to expand and boast its export base.

What, then, is Eritrea's lesson from Korea's export promotion strategies?

Chapter VII

Lessons From Korea

Industrialization Strategy

Unlike Korea, which totally focused on the development of its industrial base, Eritrea, on the other hand, with its vast arable land, can focus on both agriculture and industry. Now, the choice for Eritrea is which one first – agriculture or industry?

One strategy could be the one that Korea pursued in the 60s. Develop cotton plantation that can be used as a source of raw material in the textile industry. The soil texture and climate of western lowland of Eritrea is perfect for cotton plantation. Therefore, Eritrea can export textile products to European countries and the US, where it enjoys Generalized System of Preference. The other advantage of developing the textile industry is that it is labor intensive and does not require highly skilled labor, which Eritrea has in abundance. Another Eritrea's blessing is the Red Sea, which is rich in marine life. It is estimated that 70 to 80 thousand tons of fish can be harvested from the Red Sea per year. Therefore, developing the fishing industry would be advantageous.

Another strategy could be to continue to aggressively encourage farmers and investors to engage in commercial agriculture. Eritrea's proximity to the Arabian Peninsula could be an advantage. All the Oil rich Arab Sheikdoms import vegetables and fruits from as far as Latin American countries. If Eritrea could tap its agricultural resources, it can easily compete in these markets, as the transportation cost would be negligible.

The other possible source of growth is designating Eritrea's Red Sea Coast as free ports – rendering port and warehouse services. This is a very promising strategy as the Red Sea is one of the busiest sea routs for commercial vessels in the world. It connects the East Asian countries with Europe. And Eritrea's coast is only 4 miles away from the international waters. Therefore, cargo vessels can easily dock and get the required services.

The above line of argument indicate that the type of industries Eritrea should focus on, as an engine of growth, are the same in the textile industry but different in other industries from those Korea focused on.

What policy, then, should Eritrea follow to achieve rapid industrialization? Should Eritrea follow in Korea's footstep: import-substitution behind high protective barriers? Import-substitution works well when the domestic market is relatively big, of course, at the cost of domestic efficiency. D.W. Nam argued,

"It is difficult to draw a clear line between an import substitution industry and an export industry. The textile industry in Korea, for example, was initially intended mainly for import substitution but grew into a major export industry in later years. What matters is the prospect for international competitiveness. Protection is almost inevitable in the early stage of new industry because no investment can be expected to yield a profit in the first one or two years of operation, while the financial capability of private business is generally very weak in a developing country. What is crucial is whether or not the protected project will be internationally competitive in the expected time horizon without further protection. Seen from this perspective, the argument for protection of industry appears to have practical wisdom in its favor".[51]

As Eritrea's domestic market is very narrow, the country has to focus in industries where it has a comparative advantage, like the textile and leather industries. However, until such time the newly established industries acquire the required efficiency and experience so as to be able to compete in the world market, they need to be shielded from the cutthroat competition of the developed world. Therefore, the government needs to institute tariff barriers.

Export Promotion Strategy

Eritrea's export performance is not encouraging. Trade statistics of the country indicate that import is much higher than export. To boast export, Korea's strategy of currency devaluation, tax exemption and financial subsidy and other benefits such as preferential credit scheme are sensible and sound to Eritrea's case. Currency devaluation helps curb import and boast export and tax exemption helps exporters to be competitive in world market. Financial subsidy will help them not to lose confidence whenever they face setbacks in world market. Preferential credit scheme also helps exports to expand and diversify their industries. The other lessons that Eritrea learns from Korea's remarkable export promotion strategy are that, as amply explained by D.W. Nam, dynamism of entrepreneurship and business acumen.

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[51] D.W. Nam, Paper for Conference on South Africa's International Economic Relations in the 1990s, April 1993, Tranvaal, South Africa.

Introduction of Foreign Capital

Eritrea is one the poorest countries of the world. The income per capita is around $200. Over half of the people live below the world poverty line. Therefore, it is very difficult for the people to save, which could be used for capital accumulation. Thus, for Eritrea, the mobilization of funds for capital formation is the most pressing economic problem. One source could be to attract foreign direct investment. To do this, the country needs to come up with a law that is favorable to investors. In this regard, Eritrea has to learn a lot from Korea's experience.

The other possible source is borrowing from international lending institutions like the IMF and World Bank. If the fund obtained from these sources is effectively and efficiently utilized, Eritrea can emerge unscathed, unlike other African countries that are immersed in debt up to the neck. However, the problem with these lending institutions is that they attached conditions to their loan, which, if followed, can have a grave consequence. A case in point is Argentina. Argentina faithfully followed what the IMF prescribed her. Instead of making progress, the Argentine economy totally collapsed leading the country into chaos and anarchy.

The main and third possibility is to forge strong economic and political relationships with reliable and rich country.

The Role of the Government

The Korean government played a decisive role in stimulating and pushing the economy forward. Eritrea's government, following in Korean footstep, should do the same to the country's economy, too.

As Eritrea's private sector is very weak, the government has to play a key role in the economic development of the country. One area which warrants immediate attention is the formation of Trade Promotion Organization, like the one Korea established in the 1960 – KOTRA. To widen the possibility of foreign markets, the government has to also join regional and international trade organizations. The other area where the Korean government played a key role in the country's industrialization process is the advices it offered to the business community through monthly conferences. If applied in the Eritrean case, not only would enable to assess past performances but such forums would enable the government to make amendments in its policies and procedures. Eritrea has to also restructure its financial, customs and other government bodies in such a way, as they would be effective in boasting export.

However, to create an economic group like Chaebol would not be advisable as they are the main source of corruption and market distorting practices, even though the Korean Chaebols played a leading role in the Korean economic miracle. Besides, the more the government confines itself to policy formulation and guidance, the better the economy will perform. For one, Eritrea lacks the required skilled manpower that can run such a huge conglomerates and for another they require a huge amount of money to establish them – which Eritrea is short of. The other reason why Eritrea should avoid Chaebol style strategy is that these big conglomerates kill smaller but more efficient firms.

The other area where the government of Eritrea has the possibility of drawing lessons from Korea is the role the financial sector played in the development endeavor. Eritrean banks can play a role in extending credit to exporters at a reasonable interest rates and in encouraging saving that would be used for capital formation. However, nationalizing banks, as Korea did, would be harmful as they would not be efficient and would be a source of corruption. There is ample reason to believe that bank officials would favor someone they know in extending credits, a defect observed in the Korea case. On top of this, the preferential credit scheme of Korea was directed to specific industries without due analysis,[52] a move Eritrea has to avoid.

The love Koreans have to education and the Korean government effort to spread education, coupled with the Confucian emphasis on education and discipline in the psychic of the Korean people, created a very skilled and industrious working force – a vital input in the Korean economic miracle.[53] Eritrea, a country with virtually no skilled labor, has to follow the Korean path.

We have seen that Korea's experience in export promotion is a good lesson to Eritrea. This, however, would not suffice enough to promote Eritrea's export. Effective policy instruments and institutions should in place.

[52] Professor Park, Hun Joo's lecture, Democracy, Ethics and Public Policy, KDI, 2002.
[53] Seong Min Hong, KIME Mideast Studies, 2001

Chapter VIII

Trade Policy Instruments and Institutions

Bernard Hoekman and associates in the Development Research Group, World Bank, point out that “The first step in designing a strategy to use trade policy for growth and poverty alleviation is to understand how the trade regime works. This involves learning of the importance of non-tariff barriers, including who gets the licenses and permits. What is the structure of the tariff and including its dispersion, exemptions and rebates? How much revenue comes from tariffs? What policies are in place that may tax or subsidize exports? Are trade related institutions, such as standards organizations, export finance and marketing facilities adequate to support an expansion exports?”[54]

In this Chapter an attempt is made to address such questions pertaining to the Eritrean situation and policy recommendations are forwarded along the discussion.

The Tariff Regime of Eritrea

Customs duties on imported products vary widely. In an effort to direct the use of scarce foreign exchange for goods that will further development objectives, the Government has imposed tariffs ranging from 2% to 25% on essential goods such as capital equipment, industrial inputs, pharmaceuticals, school supplies, books, food, livestock, and seed. However, customs duties on imports of capital goods, intermediate industrial spare parts,

[54] Tarr David, Maurice Schiff, Constantine Michalopoulos, Bernard Hoekman, Development Research Group, International Trade Team, World Bank, 2001.

and raw materials are fixed at a nominal 2%. On luxury goods, liquor, tobacco, automobiles the tariff is between 50% and 200%. All goods are found in the Customs Import Tariff Schedule. Tariff exemptions are granted to diplomats. Articles and equipment specialized for use by the disabled or handicapped are exempted from import taxes.[55]

Even though Eritrea's tariff regime seem to be low the very fact that it has a differentiated structure with different tariff escalation it affords high "effective" protection to final goods producers thereby discouraging the development of intermediate industries.

Therefore, it is suggested that a uniform tariff regime be in place. A uniform tariff greatly simplifies customs operations, eliminates a number of ways used to avoid paying the tariff, and should help reduce corruption and save on scarce administrative resources. There will also be a direct saving of resources from reduced lobbying for higher protection. Many of these factors are pro-poor as they greatly reduce the scope for the exercise of power and rent seeking. However, those imports destined for exportable products should be exempted from tariff or nominal tariff be levied on.

Emergency Protection, Antidumping and Other Trade Remedies

Liberalization of trade will give rise to adjustment pressures as import competition intensifies. However, in some instances imports may expand so rapidly that governments may want to be able to intervene by raising trade barriers. In such cases trade intervention

[55] Gazette of Eritrean Laws, Vol. 10/2001 No. 4, Septmber 24, 2001.

may be the most effective instrument available to governments. If so, the appropriate action to take is a so-called safeguard measure – the imposition of a temporary duty against all imports of the product concerned.[56] So far, however, no such action has been taken in Eritrea. Actually, Eritrea is not yet a member of WTO. And the Government seems to be determined not to give protection whatsoever. This stand may hurt domestic producers. The most beneficiary from this action of not imposing anti-dumping measures is, however, the poor. This is because antidumping is a trade policy instrument that allows duties to be imposed on imports that are sold for less than what is charged in the exporting country. However, I believe that the government has to protect domestic producer until such time that they become competitive in the world market and financially viable.

Sooner or later Eritrea would be a member of the global village gathered under the umbrella of WTO. Though accession of Eritrea to WTO is beyond the scope of this paper, the following passing comments are in place. When Eritrea joins WTO it has to make the maximum out of WTO provisions relating to various elements of special and differential (S&D) treatment that constitute a set of rights and privileges that apply to developing and least-developed country members and from which industrial countries are excluded.

Oyejide, T. Amemola explains the provision of S&D as follows: "...The key S&D provisions that granted special trade policy discretion to the developing and least-developed countries were codified in GATT Article XVIII. Section A of this article permitted developing countries to modify previously negotiated tariff bindings in order to assist the establishment of a particular industry; section B allowed the use of quantitative

[56] Tarr David, Maurice Schiff, Constantine Michalopoulos, Bernard Hoekman, Development Research Group, International Trade Team, World Bank, 2001.

import restrictions by developing countries as an instrument for dealing with balance of payments problems; and section C permitted developing countries to use quantitative import restrictions for infant industry protection. Finally, GATT Article XXVIII bis (3) allowed developing countries not to offer full reciprocity for negotiating concessions made by industrial countries, in recognition of the developing countries' need to use import duties for general economic development and fiscal purposes. Similar exemptions from disciplines are to be found in the Agreement on Subsidies and Countervailing measures: the agreement permits countries with per capita income of less than $1000 and least developed countries to maintain certain kinds of export subsidies which are otherwise prohibited; while for other developing countries the period over which subsidies can be provided is longer.[57]

Special Customs Regimes for Exporters

In Eritrea there are programs like duty drawback and temporary admission, if properly administered, allow exporters duty-free access to imported intermediates. These programs are extended to those goods that enter the country to be processed and re-exported. However, the problem with this duty drawback scheme is that their administration is very costly, and led to cumbersome procedures and delays. There is also the risk of fraudulent claims. Even if the Customs Authority of Eritrea uses bonded warehouses to curb the problem, it persists. In short there is weak administrative capacity that leads to all the problems mentioned.

[57] Oyejide, T. Amemola, Development, Trade and the WTO, A Hand Book, The World Bank, 2002.

To overcome these problems the introduction of export processing zone (EPZ) is suggested. EPZ is discussed further below.

Export Subsidies

Export subsidies may be appropriate to offset market failures but at a huge cost to the budget. The Government of Eritrea has made it clear that it would not extended any subsidy – be it to commodities destined to export or other sectors of the economy. As discussed in Chapters V and VII Korea's success depended, apart from the other key ingredients, on effective export subsidy strategy, which was strictly implemented on export performance. Eritrea's export base is very weak and narrow. To expand the export base, the government has to introduce export subsidy scheme for the producers that are engaged in export.

Export Taxes

To promote the development of export industries, all export are exempted from duties and sales taxes. However, many items cannot be exported from Eritrea including national/cultural treasures and endangered wildlife. Certain commodities may require clearance from specific government bodies; i.e., livestock and cereals require the permission of the Ministry of Agriculture, marine products require the permission of the Ministry of Fisheries.

Through lobbying of tanneries and in an attempt to support local processing industries, the export of rawhide and skin is resisted by the Ministry of Trade and Industry. In this case the restriction is economically inefficient because it reduces the incentive to produce the primary product relative to the incentive to process it.

The Government's effort to exempt all commodities from export duties is commendable but it has to abolish the restriction such as the one imposed on the export of rawhide and skin.

Export Processing Zones (EPZs)

Eritrea possesses a very strategic position in one of the busiest sea routes of the world – The Red Sea. Following suit of U.A.E. Eritrea can capitalize this unique position by designating its coastal areas as free export processing zones. It can also designate its two ports as "free ports". The Port of Assab, the bigger of the two ports, is only 4 nautical miles from the international waters. If this port is designated as a free port then all shipments from Europe destined to the port of Dubai, U.A.E. and other ports in the Arabian Peninsula can cut their rout and cost considerably.

The Government of Eritrea is well known for its anti-terrorist stance, while its neighboring countries like the Sudan, Yemen and others back terrorist groups. Particularly after the Sept. 11 terrorist attacks in the US it became apparent that Eritrea's ports are safe haven and the Government should capitalize on this newfound opportunity.

The Government actually has already designated the port of Massawa as a free port and is putting the entire required infrastructure in place, including a modern airport and rehabilitating the port with the money secured from the World Bank.

However, the management of this free zone and those that would be designated in the future has to be given due and serious thought – least it may lead to corruption and other undesirable social problems.

Attracting investment into EPZs is a function of many factors, including some that are national – such as political stability and sound macroeconomic management. Eritrea is one of the rare African nations that enjoy a stable political situation and is one of the few countries of the world were crime is practically non-existent. The Government is renowned for its anti-corruption stance. However the Government may come with attractive macroeconomic policy unless there is a well-organized and efficient body with skilled personnel to implement it the result will be dismal.

It is, therefore, suggested that the Government has to pursue with its plan of designating more places for EPZs but at the same time has to install sound macroeconomic policy and see to its efficient implementation.

Other Trade Related Institutions

Customs Clearance

Efficient and transparency is an important determinant of the costs associated with trade. Burdensome and redundant procedures – red tape – can give rise to substantial uncertainty and are often associated with rent seeking and corruption.[58] Because of the cumbersome and lengthy procedures introduced by the government of Eritrea in the early

[58] Tarr David, Maurice Schiff, Constantine Michalopoulos, Bernard Hoekman, Development Research Group, International Trade Team, World Bank, 2001

years of independence corruption and rent seeking was widely practiced. This forced the Government to introduce a stringent law to combat corruption. However, the customs clearance procedures need to be stream lined.

The following are necessary for imported goods: commercial invoice, bill of lading/airway bill, certificate of origin, and health (where applicable), as well as an import license.

The following export documents are required: EUR1 certificate for export of goods to the European Union, PTA certificate of origin for export to the Common Market for Eastern and Southern Africa (COMESA).

Documentary requirements are stringent, and documents are sometimes delayed in bureaucratic channels. Although a somewhat cumbersome system can slow clearance of documents, minimal corruption and theft mitigate these problems.

In conclusion, however the Government's effort to make the customs clearance free of corruption is commendable it has to seek ways and means to shorten the procedure and make it transparent.

Export Finance

Export finance is one of the primary constraints inhibiting exports in many low-income developing countries. Inadequacies may result from the overall weakness of the financial sector, or it may reflect difficulties in assessing the creditworthiness of traders or the fact that traders do not have sufficient assets to be judged creditworthy.[59] Eritrea is not an exception. In Eritrea, exporters face special difficulties in obtaining access to the trade credit they need. This is partly the banks are owned by the Government. The bureaucratic delays and securing collateral led to corruption and rent seeking.

It is suggested that either the Government privatize the banking institutions or seek ways of remedying this malady. The Government can use a number of mechanisms to promote access to finance, especially for smaller firms.

According to De Wulf, Luc and Philip English the two mechanisms that are sometimes used are foreign currency revolving funds and preshipment export finance guarantee schemes.

Product Standards

Product standardization facilitates interconnection of goods and information exchange, and guarantee safety, health, quality or the environment. Cognizant of this fact the Government of Eritrea established a standard institute – The Eritrean Standards Institute (ESI). The Institution is mandated to ensure conformance to international classification of standards and Eritrean standards.

However, ESI suffers from technical and financial shortcomings. It is, therefore, suggested that the Government should ensure that ESI is technically well equipped and is staffed with qualified and highly motivated personnel. This can be achieved by seeking the cooperation and assistance of developed countries.

[59] De Wulf, Luc and Philip English, Export Development Policies and Institutions, Development, Trade and the WTO, A Hand Book, World Bank, 2002.

Marketing

One of the biggest problems of exporters is lack of information, product and country recognition, and concerns about quality. These is mainly due to the fact that there is high illiteracy among the business people and inefficiency of the Ministry of Trade and Industry, a Government body shouldered with the responsibility of promoting trade and industry, and the National Chamber of Commerce – a private organization. These two institutions lend no services to traders. Traders are left to struggle to achieve their goal on their own.

The Ministry of Trade and Industry is supposed to do the job but proved to be impotent. The best solution would be to create “Trade Commission”, like KOTRA, the one Korea established in the early days of its development, which would be solely responsible to the promotion of trade. This “Trade Commission” will have Trade Promotion Unit” and “Trade Policy Follow up Unit” under it that looks into securing foreign markets and vital trade information and assess the impact of the policy and propose remedial solutions, respectively. Exporters also have the responsibility of overhauling their Chamber of Commerce. As all producers and traders are members of this organization, they have to push for a better service.

International Cooperation: Regional Integration and the WTO

Eritrea is one of the 20 members of "Common Market for Eastern and Southern Africa" (COMESA), which offers preferential terms for trade among its members. Eritrea is also a signatory to the "Cotonuo Agreement", which allows goods to enter the European Union markets duty and quota free, as long as the goods qualify with the rules of origin criteria. Eritrea is also allowed to enjoy the "Generalized System of Preferences" for similar duty and quota free treatment of exports to the US.

So far Eritrea has failed to take advantage of these agreements partly because the exporting sector is underdeveloped and partly either due to the weakness of the organization (COMESA) or the conditions EU and the US attach to their preferential treatments. COMESA is marred with efficiency and regional politics, poor communication among member states, poor infrastructure and above all low level of purchasing power of their people make trading among them next to impossible.

The health, quality standards, political, human rights, etc., conditions that the EU and US attach to their offering of preferential treatments are simply unattainable. Under the pretext of preferential treatment they try to meddle in the internal affairs of developing countries and would want to dictate their terms. In addition, as the main export item of developing countries is agricultural products, it is difficult to compete in European markets as these products are highly subsidized by EU member states.

It is, therefore, recommended that Eritrea have to seek bilateral trade agreements with highly developed countries where there will be not only transfer of technology and know-how but foreign direct investment (FDI) and a secured market. It is also advisable to form bilateral trade agreements with neighboring countries.

Eritrea's Accession to WTO

Within the rules and disciplines of the WTO, each country has considerable scope as to how restrictive or liberal its trade regime will be.[60] Eritrea, when and if decided to accede to WTO, it has to pursue a strategy of liberalizing as little as is necessary to ensure accession. This will enable the country to have a broader chance and latitude in future negotiations. However, as Eritrea is a very small and underdeveloped country, it has little leverage in market access negotiations, and so the potential benefit it is supposed to realize may be small if the liberalization it makes during negotiations is very small. This is because the costs of protection are high and its small economic size poses fewer market access issues of major WTO members. The country has to, also, seek to obtain transition periods and other special and differential treatment the WTO agreements extend to developing countries.

The Protocols of GATT/WTO Relevant to Eritrea

Hibbert, Edgar P. explains the GATT/WTO protocols pertaining to developing countries as follows:

"…Government export promotion is regulated by the rules on subsidies contained in Articles XVI of the General Agreement and the Subsidiaries Code. The latter resulted from the Tokyo (1982) and Uruguay (1993) Rounds of multilateral trade negotiations and was intended to clarify the substantive procedures of Article XVI through 'transparency'

[60] Michalopoulos, Constantine, WTO accession, Development, Trade and the WTO, A Hand Book, World Bank, 2002.

and more efficient remedial measures, not only in subsidies, but in licensing, ‘countervailing’ and anti-dumping duties (Article VI), import licensing and Government procurement. The more recent Uruguay Round has extended these provisions, with some qualifications, to intellectual property services, textiles and agricultural produce.

In order to come within the GATT rules, a Government export promotion measure must first constitute a subsidy. There is no definition of this term I the General Agreement or the Subsidies Code, but both clearly indicate that a subsidy connotes some form of financial support. Article XVI:1 mentions specifically ‘any form of income or price support’; an authoritative definition describes a subsidy as ‘a measurable economic advantage afforded to an enterprise by or at the direction of a Government’. This perhaps is the best definition of a subsidy under the GATT rules. It is not, however, the subsidy per se that is subject to GATT regulation; there must also be an effect on exports that distorts normal trading patterns. Thus Article XVI:!, which deals with subsidies in general, singles out those that operate directly or indirectly to increase exports in a manner that causes or threatens to cause serious prejudice to the interests of other contracting parties.”[61]

GATT barriers to Government export promotion operate, therefore, only against those measures that confer a measurable economic advantage on domestic exporters that distorts trading patterns by increasing exports to a higher level than would otherwise be the case. Government export promotion measures, such as direct fiscal subsidies for exports, and “dumping” fall into this category.

Hibbert, Edgar P. further points out those GATT/WTO articles that can be used by developing countries, including Eritrea, without violating WTO rules. These are articles

[61] Hibbert, Edgar P., “Trade Promotion – The Uses of Trade Policy to Develop Exports.

VI and XVI of the WTO agreement. Article VI permits Governments to levy compensatory countervailing duties on imported goods that benefit from a subsidy in the exporting country. According to Article XVI export subsidies on non-primary products are excepted unless they produce ‘trade distorting effects’ which would make them actionable. And a crucial point with respect to ‘contingent protection’ is that under XVI and the Subsidies Code the subsidy causing distortion is defined as ‘displacing’ another signatory’s exports to a third country market or adversely affecting the domestic market of a signatory.

Under GATT short term tariff protection was permitted to Governments where new ‘infant’ industry needed protection against cheap imports or some established industry was suffering ‘material injury’ through unfair competition such as dumping, discriminatory tariffs and refusal to accord MFN status.[62]

Chapter IX

[62] Finger, J. Michael, “Safeguards: Making sense of GATT/WTO Provisions allowing for Import Restriction”, Development, Trade, and the WTO, A Hand Book, The World Bank, 2002.

Complementary Policy to Trade Reforms

Macroeconomic and Exchange Rate Policies

As a result of the border war with Ethiopia, Eritrea's macro-stability of the economy is shaky. It needs to be addressed urgently. The exchange rate mechanism is "floating system". Since May 1, 1998 float of the Nakfa (local currency) there are no foreign exchange controls. Banks are allowed to set up foreign currency accounts and make foreign currency loans. This liberalization of the exchange rate revealed that the currency was over-valued. After the introduction of this policy, however, the currency is devalued, which will make imports more expensive and exports more profitable in domestic currency.

Therefore, it is suggested that the Government introduce a series of policy measures to ensure macro-stability so that the devaluation be accomplished without further debilitating losses in reserves.

Labor and Other Factor Markets

In Eritrea, there is very low labor mobility in Government institutions. This is because of the Government's refusal to release anyone who wants to quite his/her job. The reason why people want to quite government job is that for one the salary is not competitive and for another the rigidity of the structure. In the private sector, however, there is no government regulation that prohibits the movement of employees.

Therefore, the Government has to reform its policy in such a way as to allow free mobility of the employees. Property rights to land and other factors are also important to boast export. In Eritrea, the government owns the land. The Government has made it clear that anyone who is interested to invest in the country can easily acquire land through reasonable lease. Often than not, however, investors are heard complaining for bureaucratic delays.

Competition Policies

As such there are no barriers to international competition and no barriers to entry against domestic firms in Eritrea. There are, however, parastatal marketing boards such as Eritrean Grain Board (EGB), Ali Gider Cotton Plantation and Allied Afro – Trading Company. The Eritrea Grain Board's objective is to stabilize the price of grain. During the harvest time the price of grain falls due to increased supply. To protect the interest of the farmers, then, EGB offers a minimum of 50% higher price than the grain traders. It is not engaged in export. Therefore, the existence of EGB, in the short – run, is good for the farmers but in the long – run it has to cease to exist for the simple reason that it will pave the way for corruption and inefficiencies. The help of the Government should be confined to extending financial assistance and introducing new technology and markets.

Ali Gider Cotton Plantation is a state owned company. Apart from being engaged in cotton plantation, it also encourages small farmers who are engaged in cotton plantation through the provision of cottonseeds and marketing. However, because these small farmers have severe financial problem they are forced to sell their output at the price set by this parastatal company. Whether this parastatal company buys them at a reasonable price or not is of less importance. What is important, however, is that it has to extend financial assistance and at the same time teach them how to secure a market. In short "teach them how to fish, not how to eat a fish".

Allied Afro-Trading Company is a state owned trading company whose primary objective is to export industrial products to the Great Lake Countries of Central Africa. Because it is poorly staffed and the decision making process is tedious it is dead on arrival case. It never scored any profit nor managed to successfully penetrate foreign markets.

It is suggested that the Government abolish or privatize these parastatal companies and divert its meager resources in assisting those private enterprises engaged in the same business.

Foreign Direct Investment (FDI) and Intellectual Property Protection

Eritrea's Investment Proclamation of 1994 established a framework of investment. It eliminates joint venture prerequisites, opens all sectors of the economy to foreign investment (except for domestic retail and wholesale trade, import and commission agency), reduces tax on profits, allows remittance of profits in foreign exchange, and minimizes customs duties on selected import items.[63] However, there is not, as yet, established a simple set of steps for registering a foreign investment in Eritrea. There is

[63] Eritrea Investment Proclamation 1993.

bureaucratic delay for approval. In addition, on paper, authorization power is vested with the Investment Center. In practice, large-scale projects are approved at the highest levels.

It is suggested, therefore, that the Government has to introduce a system whereby it greatly reduces the red tape of acquiring investment permission and has to effectively enforce the benefits the investment proclamation offers.

Regarding protection of Property right, Eritrea has a civil law, codified system where private property is protected by law. Even though land is not bought or sold buildings and other improvements are private property and protected by the civil code. National and international copyrights and patents are protected under the commercial code. Eritrea is also a member of World Intellectual Property Organization (WIPO).

However, Eritrea neither has an office that enforces intellectual property rights nor does have qualified personnel capable of enforcing these rights.

As enforcing property rights is one key issues potential foreign investors look at in deciding an investment, the Government has to create an independent patent office whose sole responsibility is to enforce this right.

Rights to “Private ownership and Establishment” are clearly stated in the investment proclamation. The investment proclamation specifically requires the investment center to issue certification within ten days from the completion by the investor of the required formalities. The investment proclamation eliminates the requirement for joint ventures or acquire Eritrean partners, thus projects can be wholly owned by private foreign companies. Projects will be examined to ensure that the plans include training Eritrean staff to replace expatriate workers and that the projects will not negatively affect the environment or local conditions.

Licensing System

The licensing system of Eritrea is a one-stop shop where any one can acquire license with in one hour. However, license for retailing and importation are not issued to foreigners. As the domestic market is very narrow and these type of business can be done by nationals thus the decision seem to be of sound judgment.

Transparency of the Regulatory System

Eritrea is gradually emerging from the centrally planned economy of the Ethiopian Derg government. The private sector is only slowly reawakening, and government policies permitting competitive, market-based adjustments through privatization, revenue reform, and other actions are fairly new.

Eritrea presents many bureaucratic barriers to investors, which are frequently cited by US and other business representatives as major problems. These include difficulties with customs clearance, obtaining telephone/fax service and public utility hookups, locating appropriate office space, leasing land, and obtaining work permits and various government offices.

Even though the Government of Eritrea is new and is still learning how to run the country, this cannot be used as an excuse not to institute an efficient government apparatus. It has to take a clear measure that technocrats occupy all the government posts, save the politically sensitive ones. It has to also ensure all the government regulations are clear and un-ambiguous.

Corruption

Corruption is not a significant barrier or hindrance to investment or trade in Eritrea. The Government and business investment is considered to be relatively free of corruption from the top down. The penal code provides punishment for giving or accepting bribes and embezzlement. A special court is set up to specifically deal with corruption, embezzlement and theft.

Chapter X

Sector Issues

The importance of Agriculture

Because the overwhelming majority of the poor in Eritrea are located in rural areas (80% of the population) and are employed in agriculture, how trade reform affects agriculture will critically affect its overall impact on poverty alleviation.

Admittedly, the Government of Eritrea is doing its best to boast agricultural production. It is extending its financial assistance to commercial farmers, trying its best to introduce new methods of farming and seeds, offering training opportunities to farmers in animal husbandry, supplying pesticide and fertilizers, building micro dams and terracing the landscape. However, it has to device ways and means to increase the ability of the farmers to shift to the production of new products (possibly exportable products whose price has risen) through necessary complementary reforms such as infusion of additional capital or increasing access to water. Given that poor farmers may be hurt in the short run as a result of shifting to the production of new products, compensation policies such as improving rural infrastructure, research and development and creating educational opportunities for children are important.

The Role of Services

The importance of an efficient service sector goes beyond the contribution of the services sector itself to the balance of payments, because the efficiency of many service sectors is a key determinant of the competitiveness of firms.[64] Key sectors that influence the ability of firms to participate in world trade are telecommunications, transportation, financial services and other business services such as accounting and legal services.

The Eritrean telecommunication Authority is the sole state owned provider of telecommunication services. As mentioned above, there is acute shortage of telecommunication services in the country. As it is a state owned with no competitor, the rate that it charges is exorbitant. The solution would be to privatize it and invite foreign telecom companies to invest in the country.

Eritrea does not have flag carrier airlines. It depends on the services of others such as German’s Lufthansa, Egypt Air, Yeminia, British Air and others. However, because of high freight rates the export of cut flowers to European markets is becoming a problem. Understandably, running an airline, in that a very competitive market requires a huge amount of resources in terms of finance and human expertise. This can be tackled through joint venture with some dependable airlines.

The marine transport sector is not well developed, too. The few cargo ships available are of limited capacity and are privately owned. Again, to speed up delivery of goods to and from there ought to be a well developed marine transport service. This can be achieved through joint venture or allowing foreign shipping companies to use Eritrean flag.

[64] Tarr David, Maurice Schiff, Constantine Michalopoulos, Bernard Hoekman, Development Research Group, International Trade Team, World Bank, 2001

The Eritrean banking system can be characterized as “strong but primitive”. All banks operate alongside the Central Bank of Eritrea. To make Eritrea a financial hub the Government has to allow foreign banks to come to the country and have to privatize the already existing ones and encourage new privately owned ones to sprung.

Road transport is no exception, either. This is due to high cost of fuel, unpaved roads, and high cost of spare parts and above all low market for transport services due to low economic development. This problem will phase out with the passage of time as the economy develops.

Chapter XI

Concluding Remarks

Eritrea's current situation, particularly after the devastating border war with Ethiopia, has a strong resemblance to the Korean situation of the 1950s and 1960s. From the discussion above, we can conclude that all the necessary and vital conditions that led to Korea's successful export promotion are also found in Eritrea. Hence, Korea's export promotion strategies are good lessons to Eritrea. We have said that even though policies have to be designed to suit ones' country situation, the export promotion strategies and policies pursued by Korea are an excellent source of lessons to Eritrea. Based on this conclusion, we tried to suggestion some policy recommendation. To wrap up the following are the conclusion we arrived at:

1. The type of industry that Eritrea should focus for its growth strategy differs from that of Korea except in the textile industry.
2. Korea's import-substitution strategy does not work for Eritrea.
3. The protective barriers employed by Korea can safely be applied to the enfant Eritrean industries.
4. Korea's export promotion policies are highly applicable to the Eritrean case.
5. The introduction of foreign capital policy of Korea can be emulated to the Eritrean case.

6. The role of the Korean government is undeniably vital. There is no doubt that a committed government like that of Korea, which lucky Eritrea got one of its own, can transform a back warded economy into a thriving one. However, for the reasons cited in chapter VII the formation of conglomerates like the Korean Chaebols would not be suitable for Eritrea's case.
7. Again the confiscation of Banks, which Korea did, is not advisable in the Eritrean case.
8. The effort exerted by Korea to create a highly skilled and yet cheap labor is commendable, which Eritrea needs to follow, if at all it wishes to win its own niche in the world market.

However the policies pursued by Korea may seem rosy to Eritrea's case, policies alone do not guarantee development. The concept of development is not only confined to industrialization but to the issue of income and political equality, freedom, environmental protection and others. Development goes beyond satisfying one's hunger: freedom and justice.

The Park government delivered rapid economic growth to the Korean people but the cost of freedom and human values was beyond measure. The dark sides of the Korean economic miracle, lack of democratic rights, social values and environmental degradation, cannot be simply dismissed as unimportant. The massive state intervention in the economy and top-down administrative practices eroded the confidence of the people to do things in their own way led the economy to be vulnerable to outside shock.[65]

[65] Professor Park, Hun Joo's lecture, Democracy, Ethics and Public Policy, KDI, 2002.

Therefore, Eritrea may emulate some of the economic policies of Korea but cannot afford to instill an authoritarian government like the one Korea had. Democracy and rule of law are much more valuable to the people of Eritrea than mere economic progress. Eritrea can achieve what Korea did in the last five decades without resorting to Korean style government. I believe economic development should be accompanied by democracy and rule of law. And the economic development should take into account income equality, environmental protection and social values and norms.

Appendix A

Table I

Value of Re- Exports by Commodity Descripition, 1995 - 2001

In '000 of Nakfa

Commodity Description	1995	1996	1997	1998	1999	2000	2001
Food and Live Animals, Chiefly for food	90,083	55,633	58,429	44,984	39,290	65,653	51,113
Beverages and Tobacco	1,473	463	424	121	66	3	22
Crude Materials, Except Fuel	2,296	3,106	1,724	81	39	497	1,077
Mineral Fuels, Lubricants and Related Materials	113	239	52	87	0	0	0
Animal and Vegetable Oil, Fat and Wax	1,556	2,514	1,311	20	1,548	185	80
Chemicals and Related Materials n.e.s.	2,487	2,393	1,194	619	184	403	142
Manufactured Goods Classified Chiefly by Material	39,554	24,262	6,106	3,911	3,908	4,329	4,536
Machinery and Transport Equipment	18,066	26,000	9,487	1,987	28,936	3,343	1,028
Miscellaneous manufactured Aritcles	17,778	11,913	4,576	521	1,459	585	1,853
Total Re-Exports	**173,406**	**126,523**	**83,303**	**52,331**	**75,430**	**74,998**	**59,851**

Source: Trade Report: Ministry of Trade and Industry, 2002

N.B. 1USD = 10.4Nakfa

Table II

Value of Exports by Commodity Descripition, 1995 - 2001

In Millions Of Nakfa

Commodity Description	1995	1996	1997	1998	1999	2000	2001
Food and Live Animals, Chiefly for food	51,171	36,786	22,831	13,310	28,906	44,119	28,266
Beverages and Tobacco	18,272	25,732	8,482	144	384	470	1,284
Crude Materials, Except Fuel	153,821	119,898	127,775	89,079	24,173	37,205	29,672
Mineral Fuels, Lubricants and Related Materials	2	9	4	0	0	0	0
Animal and Vegetable Oil, Fat and Wax	608	93	54	5	14	34	0
Chemicals and Related Materials n.e.s.	9,541	10,954	6,997	3,442	3,935	5,921	6,951
Manufactured Goods Classified Chiefly by Material	60,770	64,027	58,340	22,220	20,330	21,760	50,773
Machinery and Transport Equipment	2,129	1,710	1,282	2,666	1,581	49	4
Miscellaneous manufactured Aritcles	59,107	134,696	66,299	13,309	8,844	4,097	3,234
Total Exports	**355,421**	**393,905**	**292,064**	**144,175**	**88,167**	**113,655**	**120,184**

Source: Trade Report: Ministry of Trade and Industry, 2002

N.B. 1USD = 10.4Nakfa

Table III

Value of Imports by Commodity Descripition, 1995 - 2001

In '000 of Nakfa

Commodity Description	1995	1996	1997	1998	1999	2000	2001
Food and Live Animals, Chiefly for food	426,733	542,857	599,880	460,027	747,718	1,125,659	1,130,913
Beverages and Tobacco	10,651	23,507	22,366	20,190	18,826	13,770	23,834
Crude Materials, Except Fuel	65,906	116,487	67,745	43,719	77,019	58,096	30,675
Mineral Fuels, Lubricants and Related Materials	48,223	39,505	52,504	41,315	31,405	51,043	37,114
Animal and Vegetable Oil, Fat and Wax	28,819	55,014	57,557	71,279	89,832	111,241	138,274
Chemicals and Related Materials n.e.s.	144,201	209,742	182,787	152,504	298,562	241,016	471,119
Manufactured Goods Classified Chiefly by Material	478,104	733,820	678,490	642,448	635,922	726,693	1,034,812
Machinery and Transport Equipment	1,165,952	1,091,139	1,158,209	1,039,570	996,191	771,236	1,095,677
Miscellaneous manufactured Aritcles	166,939	250,781	242,728	231,113	233,163	245,272	350,953
Commodities and Transactions n.e.s.	0	0	63	0	0	0	0
Total Imports	**2,535,528**	**3,062,852**	**3,062,329**	**2,702,165**	**3,128,638**	**3,344,026**	**4,313,371**

Source: Trade Report: Ministry of Trade and Industry, 2002

N.B. 1USD = 10.4Nakfa

Appendix B

People	1996	1999	2000
Population, Total	3.7 million	4.0 million	4.1 million
Population Growth (annual %)	2.7	2.8	2.6
National Poverty Rate (% of population)	-	-	-
Life expectancy at birth (years)	-	-	52
Fertility rate, total (births per woman)	-	-	5.4
Mortality rate, infant (per 1,000 live births)	-	-	59.6
Mortality rate, under – 5 (per 1,000 live births)	-	-	102.9
Births attended by skilled health staff (% of total)	-	-	-
Malnutrition prevalence (% of children under 5)	-	-	-
Urban population (% of total)	17.4	18.4	18.7
Prevalence of HIV (female, % ages 15 –24)	-	-	-
Illiteracy rate, adult male (% of males 15+)	36.2	33.5	32.7
Illiteracy rate, adult female (% of females 15+)	59.5	56.5	55.5
Net primary enrollment (% of relevant age group)	30.4	-	-
Girls in primary school (% of total enrollment)	45.1	-	-
Net secondary enrollment (% of relevant age group)	15.7	-	-
Girls in secondary school (% of total enrollment)	41.8	-	-
Environment			
Surface area (sq. km)	117,6000	117,6000	117,6000
Forest area (sq. km)	-	-	15,850
Annual deforestation (% of change)	-	-	0.3
Freshwater resources per capita (cubic meters)	-	-	2,147.9
CO_2 emissions (metric tons per capita)	-	-	-
Improved water source (% of total population with access)	-	-	46.0

Improved sanitation facilities, urban (% of urban population with access)	-	-	66.0
Energy use per capita (kg of oil equivalent)	-	-	-
Electricity use per capita (kwh)	-	-	-
Economy			
GNI, Atlas method (current US$)	747.6 million	791.8 million	696.2 million
GNI per capita, Atlas method (current US$)	200.0	200.0	170.0
GDP (current $)	631.1 million	648.5 million	607.6 million
GDP growth (annual %)	6.8	0.8	-8.2
Inflation, GDP deflator (annual %)	2.9	8.2	18.4
Agriculture value added (% of GDP)	9.8	17.1	-
Industry, value added (% of GDP)	27.4	29.2	-
Services, etc., value added (% of GDP)	62.8	53.7	-
Exports of goods and services (% of GDP)	31.7	10.1	15.7
Imports of goods and services (% of GDP)	92.0	92.1	86.1
Gross capital formation (% of GDP)	29.3	39.1	38.0
Current revenue, excluding grants (% of GDP)	-	-	-
Overall budget balance, including grants (% of GDP)	-	-	-
Technology and infrastructure			
Fixed lines and mobile telephones (per 1,000 people)	5.1	7.3	7.9
Telephone average cost of local call (US $ per three minutes)	0.0	0.0	0.0
Personal computers (per 1,000 people)		1.5	1.6
Internet users	0.0	900.0	5000.0
Paved roads (% of total)	21.8	21.8	-
Aircraft departures	-	-	-

Trade and finance			
Trade I goods as a share of GDP (%)	-	-	-
Trade in goods as a share of goods GDP (%)	-	-	-
High-technology exports (% of manufactured exports)	-	-	-
Net barter terms of trade (1995 = 100)	-	-	-
Foreign direct investment, net inflows in reporting country (current US$)	36.7 million	36.0 million	35.0 million
Present value of debt (current US$)	-	-	187.9 million
Total debt service (% of exports of goods and services)	0.0	1.6	1.1
Short-term debt outstanding (current US$)	0.0	200.0 thousand	13.1 million
Aid per capita (current US$)	43.4	37.3	43.0

Source: World Development Indicators database, April 2002

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