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SPEED

PUBLIC ADMINISTRATION AND POLICY
An Asia-Pacific Journal

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PUBLIC ADMINISTRATION AND POLICY

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(2011, 2013); *Public Administration Singapore-Style* (2010); *Taiwan's Anti-Corruption Strategy: Suggestions for Reform* (2010); *Combating Corruption Singapore-Style: Lessons for other Asian Countries* (2007); and *Curbing Corruption in Asia: A Comparative Study of Six Countries* (2003).

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EDITORIAL

This Journal has developed steadily in the last five years. During this period, we have published ten issues on various aspects of public administration and management as well as one special issue on "Health Policies" and two on "Tertiary Education". We plan to publish two more special issues next year, one on the 20th anniversary of the establishment of the Hong Kong Special Administrative Region of China and the other on healthcare delivery and financing reform. Academics and practitioners are welcome to contribute papers to these special issues. Please refer to the notes to contributors at the end of this issue for more information.

In this issue, we have five articles on various topics on public administration and policy in the region namely, India, Vietnam, Japan, South Korea, and Hong Kong. The first article is a speech by the Acting Chief Executive and Financial Secretary of the Hong Kong Special Administrative Region Government (HKSARG) of China, John C. Tsang, on Managing Financial Resources in Achieving Policy Objectives of the HKSARG, delivered at the AGM and Luncheon of the Hong Kong Public Administration Association on 17 June 2016 at The Hong Kong Polytechnic University. It is followed by Jon S.T. Quah's article on India's Anti-Corruption Agencies: Policy Reforms for Improving their Effectiveness. Thi Thuy Nguyen then examines the Fiscal Decentralization Trends in Vietnam: Developments and Reforms. Seyed Kamal Vaezi from Iran studies the Entrepreneurship and Innovation Policy in Training Systems: A case of South Korea. Finally, Franky K.H. Choi discusses The Role of the State in Economic Development: Expansion of the Government's Role in Japan from 1945 to 2000.

We thank all the article authors for their contributions to this issue as well as the reviewers for their constructive comments and suggestions in helping the authors to improve their articles. I also wish to express my sincere appreciation of the efforts by our editorial team for making the journal publication on time.

Peter K.W. Fong
Editor-in-Chief
PAAP
President
Hong Kong Public Administration Association

Managing Financial Resources in Achieving Policy Objectives of the Hong Kong Special Administrative Region Government

John C. Tsang
Acting Chief Executive & Financial Secretary
The Hong Kong SAR Government

(The following is a speech by the Acting Chief Executive & Financial Secretary, Mr. John C. Tsang, delivered at the AGM and Luncheon of the Hong Kong Public Administration Association, held in the Hong Kong Polytechnic University on 17 June, 2016.)

Peter (President of the Hong Kong Public Administration Association, Prof. Peter Fong), distinguished guests, ladies and gentlemen,

It is my great pleasure to be here with you all today. I was told a while ago that I could speak on any topic that I thought appropriate and Peter, let me remind you, that kind of invitation in the wrong hands could be a very big mistake. But relax, I shall not overstep my boundaries on this occasion. I do not intend to spring any surprises today. So I'd like the friends from the media to know that. No surprises today.

About this time last month, LegCo (the Legislative Council) passed the Appropriation Bill 2016, putting an end to the long drawn-out but rather eccentric discussion on the Bill. As with the case of my previous Budgets that were also punctuated heavily with filibusters, this year the interests of the public and the media focused mainly on the relief measures, and not the politically laden proclamations and proposed amendments. Thus spoke pragmatic Hong Kong.

Since matters on the current state of our public finance and how we are managing our financial resources in achieving our policy objectives have not been extensively articulated, I thought it would be a good opportunity for me to do so today.

I fully understand that this topic is not exactly the most interesting thing for listeners, especially after a gratifying meal. So I promise that I shall keep my talk as short as I can, to about 10, 15 minutes, and hopefully, you can stay awake during the talk. Meanwhile, maybe you can order some coffee.

Let me first set the scene with some upbeat news. You will be happy to know that the state of our public finance remains healthy. We have experienced 12 successive years of budget surpluses, and yours truly has been Financial Secretary for nine of those 12 years.

We are, by and large, government with a small "g". Public expenditure constitutes

about 20 per cent of our GDP. Government revenue generally matches that, roughly equivalent to about 20 per cent of GDP as well. Our fiscal reserves exceed HK\$800 billion - about 35 per cent of our GDP.

That should be good news, particularly for, say, ministers from Europe, they would love to hear something like that. But there is always the flip side of the coin. And that relates to matters that are of serious concern to us. The biggest concern of all is that our labour force is set to decline from around 2018, resulting in the reduction of our tax income as well as constraints on our economic growth.

In the event, how should we manage the contraction of our tax income? Would raising taxes help compensate for the reduction in our working population? Would the younger generation be able to afford higher taxes? Would government have the resources to expand services for the growing number of our older generation? These are all good public administration questions and I'm sure an esteemed body like yourselves would be in a very good position to deal with some of them.

In the next few minutes, I would like to share with you our thinking in striking the right balance in response to some of these pertinent questions.

Some have said that we could have spent a great deal more on services for the people in Hong Kong, if not for the underestimation of Government revenue. I can assure you that it is not intentional on our part to underestimate our income, but as an open and small economy, we are often subject to the whims of the volatile external sector.

I can also assure you that we have not constrained our expenditure because of the underestimation of our income. In fact, for the decade between 2006-07 and 2016-17, our GDP grew by 65 per cent, Government revenue grew by 73 per cent and Government expenditure by 115 per cent, all on a cumulative basis. In short, Government expenditure has grown a lot faster than revenue growth, while the economy lagged behind both.

We need to focus on the discrepancy of the speed of growth of our revenue and expenditure as well as the economy. Occasional revenue windfalls cannot justify more rapid expenditure growth, especially expenditure on a recurrent basis. We need to find a delicate, but most importantly, a sustainable, balance among these three factors.

So while we are here — and, I trust, most of you are still somewhat conscious — let me touch on our fiscal reserves. Given that they exceed HK\$800 billion, are we being overly prudent with Government expenditure? Are we insensitive to the needs of the community? Should we not dip into our reserves, or as some have suggested, our Exchange Fund?

Perhaps I should, first of all, make clear that we cannot just take money from the fiscal reserves to cover spending in the implementation of policies without recourse to

LegCo. As a matter of fact, much of the fiscal reserves are actually locked up in funds with designated uses, such as funds for supporting public works projects, funds for paying pensions to public officers, as well as funds for financing innovation and technology projects, etc.

It is true that, in absolute dollar terms, our fiscal reserves have more than doubled from HK\$369 billion to HK\$854 billion over the past decade. But so did Government expenditure. In terms of months of Government expenditure that our reserves can cover, the number has remained quite constant, about 20 or so.

I should add that the fiscal reserves are all that we have to meet our day-to-day operational needs, to meet our outstanding commitments for capital works as well as our liabilities, such as pensions for public officers. Just to give you some perspective. Outstanding commitments for capital works projects underway amount to over HK\$300 billion. These are bills we have to pay. The value of pensions as of March 2015 has reached a substantial level of \$816 billion. This is the total amount, and we only need to pay out about HK\$30 billion each year. But it is still a large commitment.

The fiscal reserves can be quickly depleted, as the deficit years between 1998-99 and 2003-04 demonstrated all too well. During that period, Hong Kong faced severe economic downturns and 40 per cent of our fiscal reserves were depleted in one go. The reserves provide us with a shock-absorbing cushion during these economic bad times.

The primary objective of the Exchange Fund, as laid down in the Exchange Fund Ordinance, is to affect the exchange value of the currency of Hong Kong for the purpose of maintaining the monetary and financial stability of Hong Kong. It is essential that we maintain a sizable Exchange Fund that is commensurate with the scale of Hong Kong's financial system in order to deal with potential risks and to stabilise the financial system, and preserve market and public confidence during unforeseen circumstances.

And coming back to our topic today, the management of public finance is really an art — the art of allowing expenditure to grow, while containing the growth to align with GDP and revenue growth; the art of acceding to some expenditure demands but declining others, when all seem well justified in isolation; the art of balancing short-term needs and long-term fiscal sustainability. The art, too, of relaying the inconvenient truth - that resources are limited - without being chased out of town, hopefully.

Allow me now to explain how we have allocated Hong Kong's money.

You should be interested to know that in the past 10 years, recurrent expenditure for social welfare has increased by 104 per cent; for health, it's up 92 per cent; and for education, it has climbed 70 per cent from a very high base. Despite these significant increases, we still have been able to add to our reserves, gathering resources that would protect us from the rainy days ahead.

Major recurrent funding initiatives in these past few years include the 3-3-4 new senior education structure reform, the Old Age Living Allowance, the HK\$2,000 Elderly Healthcare Voucher Scheme, the Low Income Family Allowance and the HK\$2 public transport subsidy scheme for those who are 65 and above and for the disabled.

These are all big-ticket items. In the past six years, for example, annual spending on the healthcare voucher scheme has risen from HK\$100 million to HK\$1.3 billion — up 13 times. As for the HK\$2 public transport subsidy scheme, it has risen from HK\$200 million per year to HK\$1.1 billion — a five and a half-fold increase.

From 2017-18 on, Government will spend about HK\$6.7 billion per year to implement our new free kindergarten education policy. This will more than double our existing recurrent funding on pre-primary education. This is money well spent, I agree, but it is still a large sum. Not exactly chicken feed.

We have also been investing heavily in capital works projects, from healthcare and education, to sports, recreation and district facilities. Capital works expenditure last year was HK\$76 billion, and it will remain at this high level and more for the next few years.

These expenditures, I should add, have yet to reflect the fiscal pressure emanating from our aging population. If we were to continue at this level of spending, we run the risk of a structural deficit, as clearly articulated in the study by our Working Group on Long-Term Fiscal Planning.

Which is why we are making strenuous efforts to contain expenditure growth. Among other things, we have initiated a three-year programme to achieve efficiency savings of 2 per cent, just 2 per cent, from operating expenditure, beginning in 2015-16.

We are encouraging departments to re-engineer and re-prioritize — we call that R&R — in order to free up savings for new or enhanced services. This is also a good opportunity for our controlling officers to have a good look at their baselines and the services that they have been rendering.

To stabilise revenue, we are reviewing fees and charges in accordance with cost-recovery and user-pays principles. Income, as an example, from fees and charges, amounts to around HK\$15 billion per year.

As to new taxes and ways to broaden our tax base, we keep an open mind, because I fully recognise the difficulty in forging any form of consensus on this most contentious political issue of all. In formulating options for expanding tax revenue, we should insist, and we would insist, that any such measures should be fair and ably reflect the capacity-to-pay principle. They should also be in line with Hong Kong's simple and low tax system.

We have also been formulating strategic investment and savings plans to better

cope with known fiscal challenges. In January this year, we established the Future Fund, created to secure higher overall returns for Hong Kong. Rather than investing all of our fiscal reserves in highly liquid, conservative investment options, we have allocated a portion for investment in longer term, higher-risk assets.

The Future Fund is the part we have set aside for longer-term investments. Other than the initial endowment of HK\$220 billion, we shall be injecting about one-third of the HK\$14.4 billion actual surplus for 2015-16 into the Future Fund as a top-up, come July 1. That amounts to about HK\$4.8 billion.

We have also established a Housing Reserve, using the investment returns in 2014-15 and 2015-16, in order to assist the Housing Authority to fulfil its 10-year housing objective despite its depleting financial situation. Our Housing Reserve balance, by the way, now stands at HK\$74 billion.

Securing Hong Kong's future, of course, demands more than containing expenditure, more than stabilising revenue, and more than clever saving and clever investing. We need, as well, to ensure that our economic growth engine continues in high gear.

But that's another bedtime story, one that I'll save for another day when I am invited back again.

So for you ladies and gentlemen who are still awake, that is my story for today. I originally allotted time for some questions but I do need to run off to attend to some urgent issues, so I do apologise, and I look forward to speaking with you again soon. So now back to you, Peter.

India's Anti-Corruption Agencies: Policy Reforms for Improving their Effectiveness

Jon S.T. Quah

Anti-Corruption Consultant, Singapore

Abstract

This article explains why corruption remains a serious problem in India in spite of the various anti-corruption measures implemented during the past 75 years. After identifying the major causes of corruption and evaluating the effectiveness of India's two major anti-corruption agencies, the article recommends five policy reforms for improving their effectiveness.

Keywords: Central Bureau of Investigation, Central Vigilance Commission, causes of corruption, India

Introduction

Corruption remains a "wicked problem"¹ in India in spite of the many anti-corruption measures implemented after the creation of the Delhi Special Police Establishment (DSPE) in 1941 to "investigate cases of bribery and corruption in transactions" involving the War and Supply Departments (Palmier, 1985, p. 30). Corruption was made an offence in the Indian Penal Code in 1860 and in March 1947, the Prevention of Corruption Act incorporated relevant sections of the Indian Penal Code and became law (Quah, 2008, p. 245). Gurnek Bains (2015, pp. 82, 108), a psychologist who is originally from India but lives in London now, observes that Westerners would "be jolted by the crass materialism, dishonesty, corruption" when they visit India, and businessmen would discover that "Indian officials have taken corruption to the level of a fine art." Vijay Anand, an Indian activist, complained that: "From birth to death, an Indian citizen has to go through the corruption cycle" (quoted in Gentile, 2010). Similarly, Varun Mishra, a software engineer, described the daily routine of petty corruption faced by many citizens in India in their interactions with corrupt civil servants and public agencies responsible for delivering essential services thus: "You pay for a birth certificate, a death certificate. All your life you pay. And for what? For things that should be free" (quoted in Burke, 2011). According to S.S. Gill (1998, pp. 125, 127), a retired senior civil servant, there is no sphere of public administration in India which is "not infested with corruption" because corruption "infects the whole system" with every level devising "its own methods of extortion."

Many Indian scholars have analysed the problem of corruption in India and proposed various solutions. For example, the late Samuel Paul (1997, pp. 286-304)

recommended "a strategic agenda for action" to minimise corruption in India. Sixteen years later, he presented "a set of actionable ideas on the way forward to fight corruption" in India (Paul, 2013, p. 271). N. Vittal (2012, pp. 37, 225), the Civil Service Commissioner from 1998-2002, contended that the "persistent disease" of corruption "led to a multiple organ failure in governance" and suggested a combination of the engineering and medical approaches to end corruption in India. However, he admits that there are "umpteen studies offering solutions to our challenges but these have never been translated into action" (Vittal, 2012, p. 225).

The Right to Information (RTI) Act No. 22 of 2005 was enacted on 15 June and implemented on 12 October 2005 to provide citizens in India with the right to access information from all "public authorities" which are required to provide the requested information within 30 days.² Madhav Godbole (2013, p. 113), a former Home Secretary and Secretary of Justice in India, described the RTI Act as "a ray of hope" and "an important tool in the fight against corruption" because "a great deal of corruption has come to light through the efforts of RTI activists." In 1968, the lower House of Parliament or *Lok Sabha* introduced a bill to establish the *Lokpal* or Ombudsman. Different versions of the bill were considered during the next 43 years until the ninth version of the *Lokpal* and *Lokayukta* Bill was passed in December 2011 and became an Act in 2013 after the demand to create a *Lokpal* at the central level by the activist Anna Harare in 2010 (Godbole, 2013, p. 105; Tummala, 2016, pp. 9-10). However, to date, the *Lokpal* has not been established yet.

The RTI Act of 2005 and the *Lokpal* when it is established will be important tools in India's battle against corruption. However, this article focuses instead on the two anti-corruption agencies (ACAs) the Central Bureau of Investigation (CBI) and the Central Vigilance Commission (CVC) instead because of their important and direct role in combating corruption in India.

Why is corruption still a serious problem in India today after the implementation of various anti-corruption initiatives during the past 75 years? What can be done to minimise corruption in India? This article addresses these questions by identifying the causes of corruption, evaluating the performance of the CBI and CVC, and recommending five policy reforms to improve their effectiveness.

Causes of Corruption in India

There are five major causes of corruption in India namely, the low salaries of civil servants, red tape, the low probability of detecting and punishing corrupt offenders, cultural values and practices, and the difficult governance environment.

Low salaries

Low salaries contribute to corruption because poorly paid civil servants rely on their positions to accept bribes to make ends meet, especially "when the expected cost of being caught is low" (Mauro, 1997, p. 5). It is impossible to combat corruption "on

an empty stomach" and "when salaries are below real living standards" (Passas, 2015). A survey of civil service compensation in Bangladesh, India, Nepal, Pakistan and Sri Lanka from 1977-1987 found that "despite salary revisions and dearness allowances, [the] starting basic salaries" of their civil servants were very low by international standards. Consequently, corruption became "an unsavoury response" to the "falling or low real salary scales" in these countries and was widespread and viewed as "inevitable and incurable by the public" (Chew, 1992, pp. 2, 78, 101). In other words, corruption is "a coping strategy to compensate for economic hardship" for poorly paid civil servants in many countries, including India (Lindner, 2013, p. 2).

The Third Pay Commission (1970-1973) in India "confidently stated that the payment of a salary which does not satisfy the minimum reasonable needs of a government servant is a direct invitation to corruption" (Das, 2001, p. 105). In the same vein, Chief Justice K.G. Balakrishnan (2009) contends that a major cause of corruption in India is the wide disparity in salaries offered in the public and private sectors. Since then, public sector salaries in India are increased periodically, with the most recent increase announced by the Seventh Pay Commission on 26 July 2016. Table 1 provides details of the new salary structure of the Indian Administrative Service (IAS). Even though civil service salaries in India have improved in recent years, they are still relatively low compared with the salaries of civil servants in Singapore, Hong Kong SAR, Japan, Taiwan and South Korea (Quah, 2011, p. 465).

Table 1: Salary Structure of the Indian Administrative Service, July 2016

| Grade | Position in state governments or central government | Monthly pay scale ^a | Year of service |
|-----------------------------|--|--------------------------------|-------------------------------------|
| Cabinet Secretary Grade | Cabinet Secretary of India | Rs 255,000 (US\$3,800) | 35 th year (only 1 post) |
| Apex Scale | Chief Secretary of States, Secretary (Union Secretaries in charge) of ministries of Government of India | Rs 255,000 (US\$3,800) | 31 st year |
| Above Super Time Scale | Principal Secretary in the State Government or Additional Secretary to Government of India | Rs 200,000 (US\$2,980) | 24 th year |
| Super Time Scale | Divisional Commissioner in a division or Secretary in State government or Joint Secretary to Government of India | Rs 175,000 (US\$2,608) | 17 th year |
| Selection Grade | District Magistrate/Collector/Deputy Commissioner of a District or Special Secretary in the State government or Director in Government of India | Rs 118,000 (US\$1,758) | 11 th year |
| Junior Administrative Grade | District Manager/Collector/Deputy Commissioner of a District or Additional Secretary in the State government or Joint Director/Deputy Secretary, Government of India, Private Secretary, Government of India | Rs 78,800 (US\$1,174) | 6 th year |
| Senior Time Scale | Additional District Magistrate/ Additional Collector/Additional Deputy Commissioner of a District or Under Secretary in State Government or Deputy Secretary, Government of India | Rs 65,000 (US\$969) | 4 th year |
| Junior Time Scale | Sub-Divisional Magistrate in a sub-division of a district/Section Officer in state secretariat (Entry)/Assistant Director, Government of India | Rs 56,000 (US\$835) | Initial year |

^aRs 1 = US\$0.015 (on 24 August 2016).
Source: Wikipedia (2016).

Red tape

Red tape is the pejorative description of "bureaucratic procedures characterised by mechanical adherence to regulations, excessive formality and attention to routine, and the compilation of large amounts of extraneous information resulting in prolonged delay or inaction" (Chandler and Plano, 1988, p. 233). Civil servants are tempted "by opportunities to sell their official discretion and information" and "by the opportunities to extort payments" because "permits can be delayed, licences held up, deliberations protracted, proceedings prolonged, unless rewards are offered" (Kaufman, 1977, pp. 51-53).

The "penchant for ritualistic thinking and pedantic detail" among Indians has resulted in "the mind-numbingly high levels of procedural delay and bureaucracy anyone conducting business" faces in India. Bains (2015, p. 118) illustrates the serious problem of red tape in India with these examples:

Something as simple as buying a train ticket in an Indian train station can quickly become a Kafkaesque exercise, requiring the negotiation of various arcane layers of bureaucracy. Doing anything official in India typically involves dealing with frustratingly rigid and unerring unempathetic officials who pass you around from one desk to the other. Tasks like opening a bank account or retrieving a birth certificate can take months, often requiring several visits and endless reserves of patience.

Consequently, red tape gives poorly paid civil servants the excuse to extort bribes from those members of the public who are willing to pay "speed money" to cut red tape and reduce delay by expediting their applications for licences or permits (Quah, 2009, pp. 820-821).

Table 2: The Speed Money Phenomenon in Six Public Agencies in Bangalore, 1994

| Public Agency | Proportion of respondents who paid bribes | Average amount of bribe paid per transaction |
|---|---|--|
| Regional Transport Office | 33% | Rs 648 (US\$21.60) |
| Bangalore City Corporation | 21% | Rs 656 (US\$21.90) |
| Public hospitals | 17% | Rs 396 (US\$13.20) |
| Bangalore Water Supply and Sewerage Board | 12% | Rs 275 (US\$9.17) |
| Karnataka Electricity Board | 11% | Rs 206 (US\$6.87) |
| Bangalore Telecom | 4% | Rs 110 (US\$3.67) |

Source: Paul (2002, p. 45)

The late Samuel Paul pioneered the use of a report card to collect feedback from 1,130 citizens using public services on the extent of "retail" corruption in six public agencies in Bangalore, India in 1993-1994. He found that 33 per cent of the respondents paid "speed money" to the officials in the Regional Transport Office to expedite the

provision of services. However, Table 2 shows that the bribes paid to the Bangalore City Corporation officials were the highest, with an average amount of Rs 656 (US\$21.90) per transaction. The most surprising finding was that 32 per cent of the poorer respondents admitted that they had to pay bribes to solve their problems (Paul, 2002, pp. 33-35, 50). A more recent study by Subhash Bhatnagar (2013, pp. 225-226) has confirmed that corruption "hurts disproportionately" the poor Indian citizens who have to pay bribes ranging from Rs 100 to the police in Bangalore for a traffic violation to Rs 5,000 to the police in Noida City for a first incidence report on a stolen car.

Table 3: Ease of Doing Business Rank in India, 2007 and 2016

| Indicator | 2007 (N=175) | 2016 (N=189) | Difference |
|--|-----------------|-----------------|------------|
| Ease of doing business rank | 134 | 130 | +4 |
| Starting a business rank | 88 | 155 | -67 |
| No. of procedures | 11 | 12.9 | +1.9 |
| Time (days) | 35 | 29 | -6 |
| Dealing with construction permits rank | 155 | 183 | -28 |
| No. of procedures | 20 | 33.6 | +13.6 |
| Time (days) | 270 | 191.5 | -78.5 |
| Registering property rank | 110 | 138 | -28 |
| No. of procedures | 6 | 7 | +1 |
| Time (days) | 62 | 90.1 | +28.1 |

Sources: World Bank (2006, p. 118; 2016c, p. 208).

Since 2004, the World Bank has conducted an annual survey on the ease of doing business in many countries around the world. The ease of doing business in a country is a measure of the extent of red tape as it would be difficult to do business in those countries afflicted with this problem. Table 3 confirms that red tape remains a serious problem in India even though its ease of doing business rank has improved from 134th position among 175 countries in 2007 to 130th position among 189 countries in 2016. India's rank in starting a business deteriorated from 88th to 155th positions during the same period even though the number of days needed was reduced from 35 days to 29 days. Its rank in getting construction permits also declined from 155th to 183rd positions even though the time taken was cut from 270 days to 191.5 days. Finally, India's rank in registering property dropped from 110th to 138th positions as the time required was increased from 62 days to 90.1 days.

Bhatnagar (2013, pp. 240, 247) contends that e-governance is "a powerful tool, which if utilised forcefully, thoughtfully and imaginatively" can reduce bribery in the delivery of government services in India by introducing "efficiency-less trips, less waiting time and reduced elapsed time for delivering" these services. However, he laments that even though there is increased efficiency, bribes are extorted because "enough discretion still remains with the bureaucrats in e-Governance projects to delay or deny service."

Low probability of detecting and punishing corrupt offenders

In her analysis of corruption in post-Communist countries, Rasma Karklins (2005, p. 160) contends that for an anti-corruption strategy "to send a clear signal that corrupt practices will be curtailed" corrupt acts must be deterred by ensuring that "it is highly probable that people who engage in them will be called to account and will pay a significant price." Palmier (1985, p. 280) found that the insufficient policing devoted to curbing corruption was an important cause of corruption in India. As the probability of detecting and punishing corrupt offenders is low in India, the public perceives corruption as a "low risk, high reward activity" as they are unlikely to be detected and punished (Quah, 2011, p. 90).

According to P.C. Alexander (1995, p. 79), the major cause of corruption in the Indian Civil Service is "the ease with which corrupt officials are able to get away without punishment [that is] commensurate with their offence." He explains that the complicated procedures involved in the disciplinary enquiries provide not only protection for the honest official but also "a loophole for the corrupt to escape" because "when punishments are not prompt and deterrent, they cease to be disincentives for the dishonest" (Alexander, 1995, p. 80). In January 2008, Joginder Singh, a former CBI Director, lamented that those persons involved in the corruption scandal of five health care projects in India would not be prosecuted because "the legal system in this country is such that this is not going to happen and they will merrily keep the money" (quoted in Gentleman, 2008, p. 2).

In their comparative study of Bangladesh, India and Sri Lanka, Ahmad and Brookins observed that "official punitive action has seldom been taken against corrupt officials" in spite of the large number of corruption reports. They analysed the number of corruption reports in three major newspapers in Dhaka, Mumbai and Colombo from November to December 1996. In the case of India, they found that only 18 cases (15 per cent) of the 119 cases of corruption reported in the *Times of India* in Mumbai had resulted in official punitive action. They concluded that for genuine anti-corruption reform in the three countries to succeed, there must be "greater effort to make corrupt persons accountable for their actions" (Ahmad and Brookins, 2004, p. 29).

Table 4: Outcomes of Corruption Cases in Court in India, 2010-2014

| Outcome | 2010 | 2011 | 2012 | 2013 | 2014 |
|------------------------------|-------|------|-------|-------|-------|
| Conviction | 468 | 497 | 743 | 763 | 635 |
| Acquittal | 178 | 209 | 345 | 301 | 258 |
| Discharge | 15 | 35 | 20 | 48 | 27 |
| Disposal | 85 | 154 | 80 | 113 | 86 |
| Total no. of cases | 746 | 895 | 1,188 | 1,225 | 1,006 |
| Conviction rate ^a | 70.8% | 67% | 67% | 68.6% | 69% |

^aThis is calculated by excluding the number of cases disposed of for other reasons. Sources: CBI (2011, p. 23; 2012, p. 32; 2013, p. 38; 2014, p. 55; 2015, p. 40).

An analysis of corruption cases brought to court by the CBI from 2010-2014 in Table 4 shows that the conviction rate ranges from 67 per cent in 2011 and 2012 to 70.8 per cent in 2010, or an average of 68.5 per cent for this period. However, the combined effect of "poor evidence and judicial delays" makes corruption a low-risk activity in India. To illustrate, it would take the courts in Orissa decades to clear the backlog of cases because only 70 (or 35 per cent) of the 200 cases handled annually are disposed by them. Consequently, it is not surprising that 12 per cent of the defendants in Orissa "die before their case comes to trial; the evidence base collapses and memories blur, making prosecution an impossible task" (Menon, 2006, p. 345). In March 2010, Justice V.V. Rao, an Andhra Pradesh High Court judge, estimated that the judiciary would take 320 years to clear the backlog of 31.28 million cases pending in various courts in India (Times of India, 2010).

Cultural values and practices

Culture contributes to corruption when traditional practices like gift-giving and family ties influence individuals to give or receive bribes, and make them tolerate corrupt practices. Gift-giving is an important social tradition in India and is practised during festivals like Diwali and Holi, and such events as weddings, anniversaries, birthdays and funerals (Sharma *et al.*, 2015, p. 114). Gift-giving encourages reciprocity in social relations and as it is also difficult to distinguish between a gift and a bribe, there are regulations to prevent civil servants from accepting gifts and to prevent vote-buying during elections.

Section 11 of the All India Services (Conduct) Rules 1968 stipulates that all government employees may accept gifts from their relatives and personal friends with whom they have no official dealings on social and religious events like weddings and funerals but they must report those gifts whose value exceed Rs 25,000 (US\$375). A "gift" includes free transport, free boarding, free lodging or any other service or pecuniary advantage provided by a person who is not a relative or personal friend but excludes a casual meal, casual lift or other social hospitality. All civil servants are prohibited from accepting any gift without government approval if its value exceeds Rs 5,000 (US\$75). They are also not allowed to accept lavish or frequent hospitality from those persons with official dealings with them or from commercial or industrial organisations.³

To prevent vote-buying in elections, political parties in India are forbidden from providing gifts to voters during the campaign period. However, such regulations are not enforced as vote-buying is widespread as "be it laptops, TVs or even goats, party promises of gifts and special privileges are the norm in Indian politics." Three weeks after announcing the election dates in March 2014, the Election Department revealed that it had seized US\$36 million in cash, more than 10 million litres of liquor, and 100 kilogrammes of heroin that were used for buying votes (Paul, 2014). This is not surprising as Robert Wade (1985, p. 487) has observed that Indians "vote for whom they think can give them most favours in a particularist way."

Hinduism is the most important religion in India as, according to the 2011 census, 79.8 per cent of the total population are Hindus (Singh, 2015). Tummala (2002, pp. 45-46, 64) contends that Hinduism encourages tolerance and forgiveness as "the Hindu system of life, as being not only absorbing but also forgiving in itself appears to be a hurdle" in combating corruption because "a corrupt official can always count on the benevolence of a superior authority." Vittal (2003, p. 19) agrees with this view and attributes the "social roots of corruption" in India to Hinduism's "eternal message of tolerance, the sense of forgiveness, the hope held for sinners to come to the right path [which] probably have also led to the tolerance of a sin like corruption." Furthermore, the fatalism of Indians and their acceptance of corruption also hinder the fight against corruption because their fatalism "becomes a self-fulfilling prophecy" as they have become so fatalistic that they "no longer even seem to suffer a guilty conscience" when they give or accept bribes (Raghunathan, 2006, p. 46).

Difficult governance environment

Gill (1998, p. 251) has astutely observed that "God seems to have taken special care to make India ungovernable." More recently, the journalist Edward Luce (2013, p. 85) believes that "sixty-five years after independence, the task of governing India from the center gets more difficult by the year." Indeed, India's policy context is unfavourable for curbing corruption for five reasons. First, India is a sub-continent and the seventh largest country in the world with a land area of 3,287,263 sq. km (*Economist*, 2015, pp. 14, 156). Second, it has the second largest population of 1,311,051,000 in 2015, according to the World Bank (2016a, p. 1). Third, as India's gross domestic product (GDP) per capita in 2015 is US\$1,582 (World Bank, 2016b), this means that the central and state governments cannot afford to pay their civil servants adequate wages to prevent corruption. Furthermore, there is also a great deal of poverty, especially in the rural areas as the Planning Commission estimated in 2014 that 363 million Indians or 29.5 per cent of the total population were living below the poverty line of US\$2.40 per day in 2011-2012 (Katyal, 2015).

Table 5: Performance of India on World Bank's Governance Indicators, 1996 and 2014

| Indicator | 1996 | | 2014 | | Difference in Percentile rank |
|--------------------------|-------|-----------------|-------|-----------------|-------------------------------|
| | Score | Percentile rank | Score | Percentile rank | |
| Voice and accountability | 0.40 | 62.02 | 0.42 | 61.08 | - 0.94 |
| Political stability | -0.91 | 19.23 | -0.96 | 13.59 | - 5.64 |
| Government effectiveness | -0.08 | 53.66 | -0.20 | 45.19 | - 8.47 |
| Regulatory quality | -0.44 | 32.35 | -0.45 | 34.62 | + 2.27 |
| Rule of law | 0.26 | 59.33 | -0.09 | 54.33 | - 5.00 |
| Control of corruption | -0.40 | 40.00 | -0.46 | 38.94 | - 1.06 |
| Total | - | 266.59 | - | 247.75 | - 18.84 |

Source: Compiled from World Bank (2015).

The fourth and most important obstacle for combating corruption in India is its poor quality of governance as reflected in its performance on the World Bank's six governance indicators in 1996 and 2014. Table 5 shows that India's total percentile rank has decreased from 266.59 in 1996 to 247.75 in 2014. Except for the marginal improvement in percentile rank for regulatory quality, the percentile ranks for the other five indicators declined, with the most serious decrease in government effectiveness (8.47), followed by political stability (5.64), rule of law (5.00), control of corruption (1.06) and voice and accountability (0.94). Finally, India is ranked 68th among 178 countries with a "warning" score of 79.4 on a scale of "very sustainable" (0-20) to "very high alert" (110-120) on the Fragile States Index (FSI) 2015⁴ (Messner, 2015, p. 5). In sum, India's difficult governance environment for combating corruption is reflected in its high level of corruption, political instability, government ineffectiveness, low regulatory quality, and low level of the rule of law.

India's Anti-Corruption Agencies

Unlike Singapore and Hong Kong, which rely on a single independent ACA, India relies on many ACAs, including the CBI, CVC, anti-corruption bureaus (ACBs), and state vigilance commissions (SVCs) in the 28 states. However, this section focuses only on the CBI (the lead ACA) and the CVC.

Central Bureau of Investigation

Corruption was made an offence in the Indian Penal Code in 1860 and defined as "acceptance by public servants of any gratification, other than remuneration, in exchange for an official act" (Shunglu, 2000, p. 13). However, as mentioned above, India began her battle against corruption with the creation of the DSPE in 1941. The CBI was established by the Government of India (GOI) in April 1963 by incorporating the DSPE as the Investigation and Anti-Corruption Division, with these five divisions: Technical Division; Crime Records and Statistics Division; Research Division; Legal and General Division; and Administration Division.

In February 1964, the Economic Offences Wing was added to the CBI to deal with cases of violation of fiscal laws. Seven months later, the Food Offences Wing was formed to collect data on hoarding, black marketing, smuggling, and profiteering in food grains. These two wings were merged in 1968 to form the Economic Offences Wing. The CBI's increased workload resulted in the establishment of the Anti-Corruption Division and the Special Crimes Division to deal with conventional crimes and economic offences. As the liberalization of India's economy led to the vast increase in securities scam cases and economic offences, the Economic Crimes Division was created in 1994 to deal with these cases and offences. The Special Crimes Division was responsible for handling terrorism cases, bomb blasts, homicides, kidnapping, and organised crime (CBI, 2010, pp. 3-4).

The CBI performs these functions: (1) combating public sector corruption and

curbing economic and violent crimes through investigation and prosecution; (2) ensuring "effective systems and procedures for successful investigation and prosecution of cases in various law courts"; (3) fighting cyber and high technology crime; (4) supporting state police organisations and law enforcement agencies regarding enquiries and investigation of cases; and (5) playing the lead role in combating national and transnational organised crime (CBI, 2015, p. iii). Accordingly, the CBI is divided into seven divisions today: Anti-Corruption Division; Economic Offences Division; Special Crimes Division; Policy and International Police Cooperation Division; Administration Division; Directorate of Prosecution; and Central Forensic Science Laboratory. The CBI's Director, who is also the Inspector General of Police, DSPE, is responsible for administering the CBI (CBI, 2015, pp. 4-5)

The CBI has 16 investigative zones and 60 investigative branches under these zones. This means that each state has at least a branch or unit of the CBI at the state capital or at a major city (CBI, 2015, p. 6). The 28 states in India also have their own ACBs for dealing with anti-corruption work and these ACBs derive their investigation powers from the Police Act because they are regular police units (Quah, 2011, p. 97).

The CBI is a Type B ACA because it performs both anti-corruption and non-corruption-related functions as reflected in the workload of its first three divisions. The Anti-Corruption Division is responsible for investigating corruption and fraud cases committed by public servants working for the central government. The Economic Crimes Division investigates bank and financial frauds, import export and foreign exchange violations, large-scale smuggling of narcotics, antiques, cultural property, and smuggling of other contraband items. The Special Crimes Division deals with cases of terrorism, bomb blasts, sensational homicides, kidnapping for ransom and organised crime (CBI, 2015, p. 4).

Central Vigilance Commission

The Santhanam Committee was appointed in June 1962 to review the anti-corruption measures employed in India and to make recommendations for improving their effectiveness. The Santhanam Report recommended the establishment of the CVC to "investigate any complaint or suspicion of improper behaviour" against a civil servant and the appointment of a Chief Vigilance Officer (CVO) in each ministry or department to supervise its vigilance staff (Quah, 2011, p. 94).

The GOI accepted the Santhanam Report and created the CVC in February 1964 to perform these four functions: (1) investigating improper transactions by public servants; (2) examining complaints of corruption, misconduct, lack of integrity or other malpractices committed by public servants; (3) supervising the vigilance and anti-corruption work of ministries, departments, and public enterprises by requesting and checking their reports on these activities; and (4) requesting the CBI to investigate a case, or entrust the complaint, information or case for inquiry to the CBI, or to the ministry, department, or public enterprise concerned (Narasimhan, 1997, pp. 264-265).

The Hawala scandal of 1991 involved the payment of US\$18 million to several politicians by four hawala brokers, including the Jain brothers. A "hawala" is an illegal transaction in foreign currency and an economic offence punishable under the Foreign Exchange Regulation Act, 1973 (Singh, 1999, p. 164). According to N.K. Singh (1999, pp. 162-163), a former CBI Joint Director, the Hawala scandal discredited the CBI for what it "did and what it failed to do" and for "the flippant and reckless way in which it launched prosecutions, totally disregarding its age-old work culture." The Supreme Court of India found that the CBI did not follow the proper procedure in investigating the Hawala scandal because the alleged offenders were powerful persons. Consequently, it directed on 18 December 1997 that the CBI's supervision should be transferred from the central government to the CVC, which should be given a statutory status. The CVC Ordinance was enacted on 25 August 1998 to comply with the Supreme Court's directions. The central government promulgated another Ordinance on 8 January 1999, and the CVC functioned under the Resolution of 4 April 1999 until the CVC Act 2003 was passed in Parliament on 11 September 2003 and transformed the CVC into a statutory body to supervise the operations of the CBI (CVC, 2009, p. 1).

As a statutory body, the CVC supervises the CBI's operations by conducting monthly meetings with the CBI Director to review the progress and quality of the cases investigated. Furthermore, it advises the disciplinary and other agencies in disciplinary cases involving vigilance at the investigation and inquiry stages. It also supervises the vigilance and anti-corruption work in the ministries and departments of the central government. The CVOs in the ministries and departments provide advice on vigilance administration and the establishment of effective systems and procedures to remove systemic failures or loopholes. They submit monthly and annual reports to the CVC, which holds annual zonal meetings to review and monitor their performance (CVC, 2009, pp. 2, 6).

The SVCs in the 28 states focus on vigilance work and are patterned after the CVC. They are assisted by the special police establishments in conducting investigations. The SVCs play an advisory role and their jurisdiction includes matters within the executive power of the states but excludes cases of political corruption. The SVCs investigate those transactions where public servants are suspected or alleged to be involved in corrupt behaviour (Sharma and Sharma, 2009, pp. 437-438).

Evaluation of CBI and CVC

The high level of perceived extent of corruption in India is reflected in its poor performance on the eight indicators shown in Table 6. First, India has a score of -0.5 with a percentile rank of 38.9 for the control of corruption in 2014. Second it was ranked 76th among the 168 countries included in the CPI in 2015 with a score of 38. Third, the Political and Economic Risk Consultancy (PERC) annual survey in 2016 ranked India last among 16 countries with a score of 8.13. Fourth, India also scores poorly on the five indicators from the *Global Competitiveness Report 2015-2016*.

India's poor performance on these eight indicators is not surprising as the CBI and CVC are ineffective ACAs, as shown below.

Table 6: Perceived extent of corruption in India, 2014-2016

| Indicator | India's Performance |
|------------------------------------|-----------------------------|
| Control of corruption 2014 | -0.5 (38.9 percentile rank) |
| Corruption Perceptions Index 2015 | 76/168 (38/100) |
| PERC annual survey 2016 | 16/16 (8.13/10) |
| Diversion of public funds 2015 | 4.1/7 (40/140) |
| Irregular payments and bribes 2015 | 4.1/7 (63/140) |
| Organised crime 2015 | 3.9/7 (119/140) |
| Ethical behaviour of firms 2015 | 4.2/7 (44/140) |
| Public trust in politicians 2015 | 4.0/7 (31/140) |

Sources: World Bank (2015); Beddow (2016, p. 4); *Asian Intelligence* (2016, p. 1); and Schwab (2015, p. 201).

Transparency International's *Global Corruption Barometer 2013* has confirmed the high levels of perceived corruption in these institutions in India: political parties (4.4); police (4.1); parliament and civil servants (3.8); education system (3.7); medical and health (3.6); business sector (3.4); judiciary and religious bodies (3.3) and media (3.2). Table 7 also shows that the nongovernmental organisations (NGOs) (2.9) and the military (2.5) were perceived to be the least corrupt institutions in India.

Table 7: Perceptions of Corruption in India by Institution, 2013

| Institution | Score ^a | Institution | Score |
|--------------------|--------------------|------------------|-------|
| Political parties | 4.4 | Business sector | 3.4 |
| Police | 4.1 | Judiciary | 3.3 |
| Parliament | 3.8 | Religious bodies | 3.3 |
| Civil servants | 3.8 | Media | 3.2 |
| Education system | 3.7 | NGOs | 2.9 |
| Medical and health | 3.6 | Military | 2.5 |

^aScore ranges from 1 (not at all corrupt) to 5 (extremely corrupt).

Source: Transparency International (2013, p. 36).

Limitations of CBI

First, the CBI's Achilles' heel is that it is a police agency because it derives its investigating powers from the DSPE Act of 1946. This means that, unlike Singapore's Corrupt Practices Investigation Bureau (CPIB) or Hong Kong's Independent Commission Against Corruption (ICAC), the GOI has continued to employ the traditional British colonial government's method of relying on the police to curb corruption in India since 1963 even though this method is ineffective. The experiences of the CPIB and ICAC have confirmed the folly of relying on the police to curb corruption when they are corrupt. Indeed, the "golden rule" is that "the police cannot

and should not be responsible for investigating their own deviance and crimes" (Punch, 2009, p. 245).

Singapore's experience in curbing corruption has shown that during 1937-1951, the Anti-Corruption Branch of the Criminal Investigation Department (CID) of the Singapore Police Force was ineffective because of its limited resources and the prevalence of police corruption. The Opium Hijacking scandal of October 1951, which involved the robbery of S\$400,000 (US\$133,330) of opium by three police detectives and some senior police officers, made the British colonial government realise the necessity of removing the responsibility of corruption control from the police. Consequently, the CPIB was formed as an ACA independent of the police in October 1952 (Quah, 2007, pp. 14-16).

The British colonial government employed the same method of corruption control in Hong Kong with the creation of the Anti-Corruption Branch in 1948 as a special unit of the CID of the Royal Hong Kong Police Force (RHKPF) to deal with the investigation and prosecution of corruption cases (Kuan, 1981, p. 24). The enactment of the Prevention of Bribery Ordinance in May 1971 resulted in the establishment of the Anti-Corruption Office (ACO) but its lack of independence from the RHKPF remained a serious obstacle. However, the ACO's credibility was undermined on 8 June 1973, when a corruption suspect, Chief Superintendent Peter F. Godber, escaped to the United Kingdom while he was under investigation. Godber's escape angered the public in Hong Kong and the government appointed the Blair-Kerr Commission of Inquiry to investigate the circumstances leading to his escape. The Governor, Sir Murray MacLehose, was forced by public criticism to accept the Blair-Kerr Commission's recommendation to establish an independent agency, separate from the RHKPF, to fight corruption. In October 1973, MacLehose informed the Legislative Council of his decision and the ICAC was formed on 15 February 1974 (Quah, 2011, pp. 252-253).

In short, the success of Singapore and Hong Kong in combating corruption can be attributed to their rejection of the British colonial government's method of relying on the police to curb corruption and their reliance instead on the CPIB and ICAC, respectively. Singapore has taken 15 years (1937-1952) and Hong Kong has taken 26 years (1948-1974) to learn this important lesson: do not rely on the police to curb corruption, especially when police corruption is rampant as "this would be like giving candy to a child" and expecting him not to eat it (Quah, 2004, p. 2). Unfortunately, the GOI has not learnt this important lesson yet, as it still relies on the CBI, which is a police agency, to fight corruption in the midst of widespread police corruption in India.

Second, unlike the CPIB and ICAC, which are Type A ACAs performing only anti-corruption functions, the CBI is a Type B ACA that performs both anti-corruption and non-corruption-related functions. Indeed, the CBI is a police agency rather an ACA because apart from combating corruption it is also responsible for dealing with economic crimes and special crimes, including organised crime and terrorism. After the Mumbai terrorist attacks in November 2008 and the current international concern with

combating terrorism, it will be difficult for the CBI to focus exclusively on its anti-corruption functions because of the competing demands on its limited resources. In other words, combating corruption would be accorded much lower priority than combating terrorism by the CBI.

Table 8: Growth of CBI's Personnel, 2002-2014

| Year | Establishment | Actual Strength | Vacant Positions |
|------|---------------|-----------------|------------------|
| 2002 | 5,920 (100%) | 4,908 (82.9%) | 1,012 (17.1%) |
| 2003 | 5,886 (100%) | 4,938 (83.9%) | 948 (16.1%) |
| 2004 | 5,891 (100%) | 4,811 (81.7%) | 1,080 (18.3%) |
| 2005 | 5,891 (100%) | 4,711 (80.0%) | 1,180 (20.0%) |
| 2006 | 5,959 (100%) | 4,652 (78.1%) | 1,307 (21.9%) |
| 2007 | 5,959 (100%) | 4,623 (77.6%) | 1,336 (22.4%) |
| 2008 | 5,960 (100%) | 4,874 (81.8%) | 1086 (18.2%) |
| 2009 | 5,961 (100%) | 5,242 (87.9%) | 719 (12.1%) |
| 2010 | 6,526 (100%) | 5,147 (78.9%) | 1,379 (21.1%) |
| 2011 | 6,590 (100%) | 5,666 (86.0%) | 924 (14.0%) |
| 2012 | 6,586 (100%) | 5,755 (87.4%) | 831 (12.6%) |
| 2013 | 6,674 (100%) | 5,796 (86.8%) | 878 (13.2%) |
| 2014 | 6,676 (100%) | 5,676 (85.0%) | 1,000 (15.0%) |

Sources: CBI (2005, p. 29; 2006, p. 38; 2008, p. 45; 2010, p. 56; 2011, p. 41; 2012, p. 62; 2015, p. 84).

Third, the CBI is both under-staffed and poorly funded to perform its various functions. Table 8 shows that while the CBI's establishment has increased from 5,886 in 2003 to 6,676 in 2014, its actual strength varies from 4,623 in 2007 to 5,796 in 2013. This means that the number of vacant positions ranges from 719 (12.1 per cent) in 2009 to 1,379 (21.1 per cent) in 2010. The CBI's inability to fill its many vacant positions during 2002 to 2014 reflects its serious staff shortage. B.R. Lall (2007, pp. 230-231), a former CBI Joint Director, described the CBI as "a very small organisation as compared to the quantum of crimes" committed in India and recommended the expansion of its personnel by 20 per cent annually for the next decade.

Arising from its staff shortage, it is not surprising that the CBI's staff-population ratio is unfavourable and ranges from 1:234,217 in 2005 to 1:228,206 in 2014. Table 9 also shows that even though the CBI's budget has grown from US\$30.3 million in 2005 to US\$65.5 million in 2014, its per capita expenditure has increased marginally from US\$0.03 to US\$0.05 during the same period. The CBI's inadequate personnel and budget is a reflection of the GOI's weak political will in combating corruption in India. By contrast, the strong political will of Singapore's government in curbing corruption is reflected in the CPIB's favourable staff-population ratio of 1:24,638 and higher per capita expenditure of US\$5.68 in 2014.⁵

Table 9: CBI's staff-population ratio and per capita expenditure, 2005-2014

| CBI | 2005 | 2008 | 2014 |
|------------------------|------------------|------------------|------------------|
| Personnel | 4,711 | 4,874 | 5,676 |
| Budget | US\$30.3 million | US\$52.1 million | US\$65.5 million |
| India's population | 1,103.4 million | 1,186.2 million | 1,295.3 million |
| Staff-population ratio | 1:234,217 | 1:243,373 | 1:228,206 |
| Per capita expenditure | US\$0.03 | US\$0.04 | US\$0.05 |

Source: Compiled by the author from the CBI's budget and personnel provided in CBI (2006, pp. 38, 44; 2009, pp. 56, 65; 2015, pp. 84, 94).

The CBI's fourth limitation is that it cannot investigate corruption cases at the state level because the Constitution of India states that law and order come under the jurisdiction of the states. Section 5 of the DSPE Act of 1946 gives the CBI investigating powers and indicates that the central government can empower it to investigate the notified offences in any state with the consent of the government of that state (Narasimhan, 1997, p. 255). The CBI did not encounter any problem with this arrangement when the Congress Party was in power in the states and centre during the post-independent period. However, with the decline in power of the Congress Party, some state governments had withdrawn the consent given by their predecessors "whenever they felt that an investigation taken up by the CBI was politically embarrassing or uncomfortable for them." C.V. Narasimhan (1997, p. 256), a former CBI Director, contends that the CBI's "unstable" status as an investigating agency within a state depends on the latter's mercy and is "a serious handicap" in developing a national network of anti-corruption investigating units.

The fifth limitation is the CBI's lack of independence because it is "an administrative nightmare" to serve "multiple masters," including the Ministry of Home Affairs for the appointment of the Director; the Ministry of Personnel, Training and Public Grievances for its budget; the Union Public Service Commission for the appointment of CBI officers above the rank of Superintendent of Police; the CVC which supervises its investigation of corruption cases; and the Ministry of Law and Justice, which pays the salaries of those officers prosecuting corruption cases for the CBI (Tummala, 2016, p. 7).

Limitations of CVC

The CVC consists of three Commissioners, 238 personnel (with 58 vacant positions) and relies on 199 full-time CVOs and 438 part-time CVOs in 2014 (CVC, 2015, p. xi). However, the CVC and the internal vigilance machinery in the ministries and government departments are under-staffed to handle its heavy workload, as reflected in the complaints and vigilance cases received and disposed by the CVC from 2010-2014. Table 10 shows that the CVC has received 164,022 complaints and disposed 162,140 complaints during this period. Similarly, Table 11 confirms that the CVC has received 27,343 vigilance cases and disposed 27,251 of these cases during the same period.

Table 10: Complaints received and disposed by CVC, 2010-2014

| Year | Complaints received | Complaints disposed |
|-------|---------------------|---------------------|
| 2010 | 16,260 | 16,211 |
| 2011 | 16,929 | 17,238 |
| 2012 | 37,039 | 33,308 |
| 2013 | 31,432 | 33,284 |
| 2014 | 62,362 | 62,099 |
| Total | 164,022 | 162,140 |

Source: CVC (2015, pp. 23-24).

Table 11: Vigilance cases received and disposed by CVC, 2010-2014

| Year | Cases received | Cases disposed |
|-------|----------------|----------------|
| 2010 | 5,327 | 5,522 |
| 2011 | 5,573 | 5,341 |
| 2012 | 5,528 | 5,720 |
| 2013 | 5,423 | 4,801 |
| 2014 | 5,492 | 5,867 |
| Total | 27,343 | 27,251 |

Source: CVC (2015, p. 14).

In addition to its severe staff shortage, the CVC's Achilles' heel is that it is an advisory body that relies on other public agencies to investigate the complaints of misconduct by civil servants it receives. Consequently, given the CVC's limited budget and personnel, it has no alternative but "to continue to rely on vigilance divisions in government organisations and public sector units, which remain weak" (Menon, 2006, p. 339).

Policy Reforms

Like AIDS, corruption in India "continuously erodes all normal systems of immunity against malgovernance in the body politic" (Vittal, 2012, p. 231) as reflected not only in the further decline in the country's poor quality of governance from 1996 to 2014 (Table 5) but also in the prevalence of many corruption scams. Vittal (2012, p. 18) has identified 24 corruption scams in India from 1976 to 2010. As corruption is a "wicked problem" in India, the GOI must have the political will and capacity to address the five causes of corruption discussed in the second section. However, as the CBI and CVC are the most important ACAs in India, this concluding section recommends five policy reforms for the policy-makers to improve their effectiveness by rectifying their limitations identified in the fourth section.

1. Establish the Anti-Corruption Agency of India

As the CBI is a police agency and a Type B ACA that performs both anti-corruption and non-corruption-related functions, the GOI should establish a new ACA known as the Anti-Corruption Agency of India (ACAI) to replace the CBI as India's

lead ACA. Unlike the CBI, the proposed ACAI should be independent of the police to avoid the conflict of interest in dealing with police corruption cases. To address the CBI's inability to investigate corruption cases at the state level without the consent of the state government, the Constitution of India must be amended to empower the ACAI to investigate corruption cases at both the central government and state governments. Above all, the ACAI should not serve several masters like the CBI, but be accountable only to Parliament for its budget and appointment of its personnel.

In short, the GOI should abandon the ineffective traditional British colonial government's method of relying on the CBI to curb corruption when police corruption is rampant. It should emulate the success of Singapore and Hong Kong by establishing the ACAI as the lead ACA that is independent of the police and provide it with adequate budget and personnel to perform its anti-corruption functions effectively. Unlike the CBI, the ACAI would be a Type ACA concerned only with combating corruption and provided with the operational independence to investigate all corruption cases without fear or favour.

2. The CBI should focus only on its law enforcement functions

The CBI is an ineffective law enforcement agency not only because of its limited budget and personnel but also because it is over-burdened with many responsibilities. Fred Riggs (1970, pp. 129-130) explains that "administrative capacities can be enhanced by reducing the number of problems to be solved by government as well as by strengthening the capacity of government to solve problems." In other words, the CBI's effectiveness can be enhanced by improving its capacity or by reducing its workload. With the transfer of its anti-corruption functions to the ACAI, the CBI can concentrate instead on combating economic crimes, organised crime, terrorism, and its other non-corruption-related functions.

3. The ACAI should be provided with adequate budget and personnel

Learning from the CBI's inadequate budget and personnel in curbing corruption, the GOI should allocate the ACAI with sufficient financial and human resources to enable it to combat corruption more effectively. As shown above, the CBI had an unfavourable staff-population ratio of 1:288,206 and a low per capita expenditure of US\$0.05 in 2014. A comparison of the staff-population ratios and per capita expenditures of nine Asian ACAs in 2008 found that the CBI had the lowest per capita expenditure of US\$0.04 and the second most unfavourable staff-population ratio of 1:243,373 (Quah, 2011, pp. 455-456).

4. The CVC should be provided with more manpower to perform its functions

Tables 10 and 11 above confirm that the CVC has a heavy workload in terms of the complaints and vigilance cases received and disposed. However, the three Commissioners, 238 personnel, 199 CVOs and 438 part-time CVOs are inadequate to

enable the CVC to handle its heavy workload effectively. Given its heavy workload, the CVC and the internal vigilance machinery in the ministries and government departments should be provided with more personnel to perform their functions.

5. The GOI must address the causes of corruption in India

In the final analysis, to address the causes of corruption in India, the GOI must improve the salaries of civil servants to minimise petty corruption, increase the probability of detecting and punishing corrupt offenders by enforcing the anti-corruption laws impartially and reducing the delay in prosecuting offenders, and reducing the opportunities for corruption by cutting red tape and relying on e-governance to enhance accountability and transparency. By addressing these four causes, the GOI will also improve the difficult governance environment, which is the fifth cause of corruption in India.

Needless to say, the implementation of these five policy reforms will not be welcomed but will be strongly resisted by those stakeholders who will benefit from maintaining the status quo in India. As the GOI has relied on the ineffective DSPE and CBI to combat corruption since 1941, it must be rational and demonstrate its political will by establishing the ACAI and strengthening the CVC and providing both agencies with adequate budgets and personnel to enable these ACAs to perform their functions effectively. Failure to implement these policy reforms would mean "business as usual" as the GOI continues to rely on the same ineffective anti-corruption strategy it has employed for the past 75 years.

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Notes

1. Rittel and Webber (1973, p. 160) contend that societal problems are 'inherently wicked' and "ill-defined" and rely on "elusive political judgment for resolution."
2. Details of the RTI Act 2005 are provided on its website at: <http://www.rti.gov.in> (accessed 18 September 2016).
3. The complete text of the All India Services (Conduct) Rules 1968 is available at: http://ipr.ias.nic.in/Docs/AIS_ConductRules1968.pdf (accessed 22 August 2016).
4. The FSI is based on 12 indicators: four social indicators; two economic indicators; and six political and military indicators.
5. The CPIB's staff-population ratio and per capita expenditure in 2014 are calculated from its personnel and budget provided in Republic of Singapore (2014, p. 359).

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Fiscal Decentralization Trends in Vietnam: Developments and Reforms

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Abstract

Over the past few decades, Vietnam has been achieving a number of positive results in fiscal decentralization and improving the efficiency of using national financial resources. This article analyzes the current fiscal decentralization in Vietnam, focusing on four main pillars, namely: (i) expenditure assignments; (ii) revenue sharing; (iii) intergovernmental fiscal transfers; and (iv) local governmental borrowing. The study also presents a number of developments and reforms that may have a great impact on fiscal autonomy. It concludes that decentralization is a continuous process and some further reforms should be done to enhance fiscal decentralization in Vietnam in the future.

Keywords: Fiscal decentralization, fiscal autonomy, expenditure assignments, revenue sharing, intergovernmental fiscal transfers, local government borrowing, Vietnam.

Introduction

Fiscal decentralization is the process through which powers over expenditures and revenues are delegated from the central government to the local governments. The extent of fiscal decentralization depends on the ability of lower tiers of government to make independent revenue and expenditure decisions within their jurisdiction, without interference by the central government (Martinez-Vazquez and McNab, 1997). The main purpose of fiscal decentralization is to ensure the efficiency of spending and providing public services; harmonize the powers over budget management among levels and contribute for the socio-economic development.

Fiscal decentralization is a major concern for developing countries and has been receiving more attention of economists and policy-makers. Like other developing countries, Vietnam has attempted to improve fiscal decentralization in order to make the delivery of social services more efficiently, especially since the adoption of the State Budget Law (SBL) 2002 with effect from fiscal year 2004 towards improving local autonomy and the system of intergovernmental fiscal relations. The SBL 2002 sets key principles for spending assignments, revenue arrangements, intergovernmental fiscal transfers and local government borrowing. It also grants provincial authorities a fair degree of autonomy to determine fiscal relationships with districts and communes within their jurisdiction. The current system allows a reasonable level of differential

treatment across provinces to take account of their specific circumstances. Progress has been steady and considerable but some challenges remain in terms of fiscal autonomy, the clarity of spending assignments, the effectiveness of local revenue arrangements and potential for debt increasing for local authorities.

The revised SBL 2015, with effect from fiscal year 2017, is a turning point in state budget management, providing a more comprehensive legal framework in consistent with current economic context as well as the trend of international integration and contributes to the process of public finance reform. It ensures the uniformity of the state budget, increases fiscal decentralization and promotes the autonomy of the local government.

This paper aims to review current fiscal decentralization in Vietnam and provide fiscal decentralization trends through doing research on available data, current laws, regulations and policies on fiscal decentralization at central and local levels. The study focuses on four pillars of fiscal decentralization, namely: (i) expenditure assignments; (ii) revenue sharing; (iii) intergovernmental fiscal transfers; and (iv) local governmental borrowing.

The rest of the paper is organized as follows: The next section briefly covers macroeconomic developments in Vietnam in recent years. Then it describes Vietnam's recent central-local fiscal system. The following section analyses achievements and drawbacks of our current fiscal decentralization that focuses on four main pillars. Next, it mentions a variety of developments and reforms as a result of the issuance of the revised SBL 2015. And the final section concludes.

Macro-economic Developments

Vietnam exhibits a record of high and sustained growth in recent years. Real GDP growth picked up to 6.68 percent as of 2015, driven by strong domestic demand amidst external headwinds. On the production side, the manufacturing sector sustained relatively robust growth on the back of continued foreign direct investment (FDI) inflows, and construction industry also improved together with a recovering real estate market and strengthened investment activities (AMRO, 2016). Inflation, meanwhile, recorded its lowest level of 0.6 percent in 2015 but pace could jump in 2016. Table 1 below summarizes key economic indicators for 2011-2015 and the Government's target for 2016.

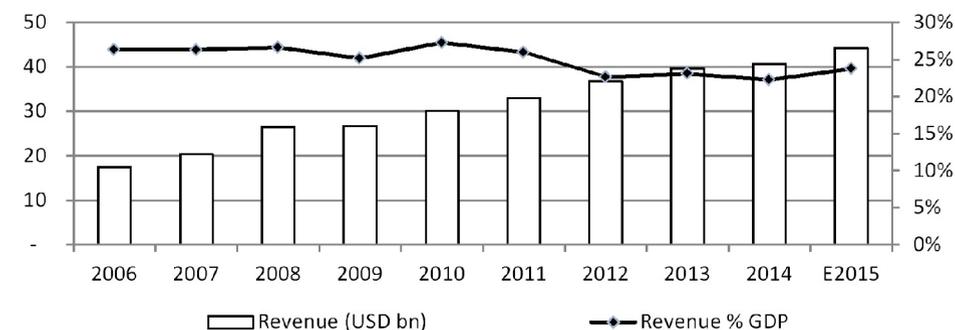
Table 1: Key indicators for 2011-2015 and the Government's target for 2016

| | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 (target) |
|--|-------|-------|-------|-------|-------|---------------|
| GDP growth (at constant 2010 prices - annual growth %) | 6.24 | 5.25 | 5.42 | 5.98 | 6.68 | 6.7 |
| GDP per capita (USD) | 1,532 | 1,753 | 1,902 | 2,049 | 2,088 | 2,164 |
| Inflation (Average CPI; previous year = 100%) | 18.13 | 6.81 | 6.04 | 1.81 | 0.6 | <5 |

Source: General Statistics Office of Vietnam and International Monetary Fund (2016)

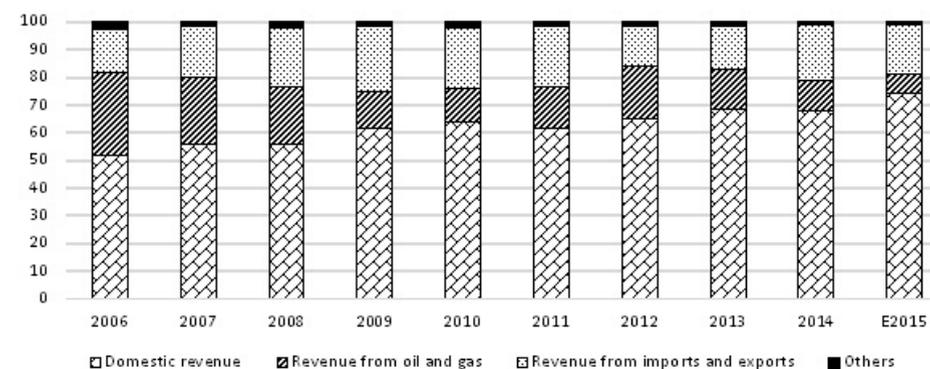
The Government's revenues continued to increase despite the after-effects of the global financial crisis and falling oil prices as a result of the Government's various tax reforms that have been designed to support the business and production sector by lowering the corporate income tax rate. Total State budget revenues for the period of 2011-2015 increased 2 times compared to the previous period of 2006-2010 (Figure 1). Share of domestic revenues increased from 59 percent for 2006-2010 to 68 percent for 2011-2015, meanwhile revenue from imports and exports reduced from 21 to 18 percent and revenue from oil and gas decreased from 18 to 13 percent (Figure 2).

Figure 1: Total revenue and revenue % GDP



Source: Calculated from Ministry of Finance of Vietnam data (2016)

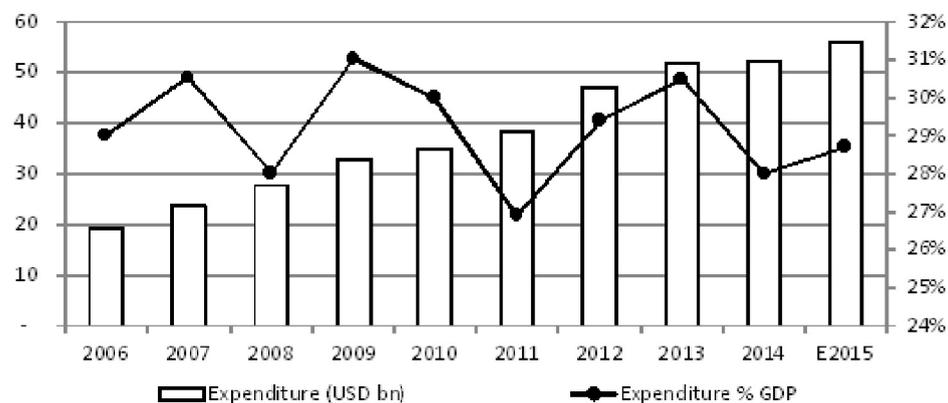
Figure 2: Revenue structure (% total)



Source: Calculated from Ministry of Finance of Vietnam data (2016)

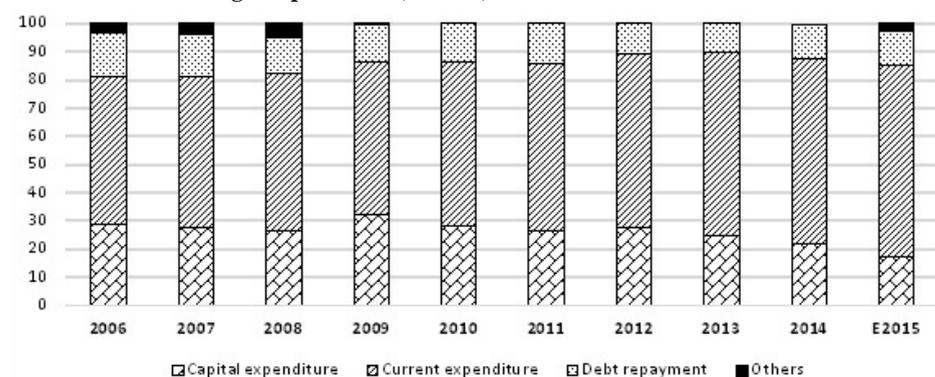
However, State budget expenditure also increased rapidly due to the expansion of current expenditure. Actual budget spending is estimated to increase marginally to 28.7 percent of GDP in 2015, relative high in compared with other countries in the regions¹ (Figure 3). In addition, the current expenditure took the largest share of the total expenditure meanwhile there was a fall in share of capital expenditure in total expenditure² (Figure 4).

Figure 3: Total expenditure and % GDP



Source: Calculated from Ministry of Finance of Vietnam data (2016)

Figure 4: Structure of budget expenditure (% total)



Source: Calculated from Ministry of Finance of Vietnam data (2016)

The budget deficit remained persistent as the expansion in budget expenditure outpaced the improvement in revenue collection. The overall budget deficit, which excludes principal repayments, was 4.7 percent of GDP in 2014 and estimated to be about 4.6 percent of GDP in 2015³. Public debt has been increasing rapidly. Latest data suggest that public debt, which includes central government debt, government guaranteed debt and local government debt, remained at high level of 62.2 percent of GDP in 2015 (Table 2). Persistently sizeable net government borrowings to finance the budget deficit and public investment have been the key factors contributing to such an increase in public debt.

Table 2: Budget deficit and debt indicators (% of GDP), 2011-2015

| | 2011 | 2012 | 2013 | 2014 | E2015 |
|---|------|------|------|------|-------|
| Budget deficit (excluding principal repayments) | 1.1 | 3.4 | 5.0 | 4.7 | 4.6 |
| Public debt | 50.0 | 50.8 | 54.5 | 58 | 62.2 |
| Central government debt | 39.3 | 39.4 | 42.6 | 46.4 | 50.3 |

Source: Ministry of Finance of Vietnam (2016)

Recent Central-local Fiscal System

The legislative framework for budget is firmly established. The SBL, first enacted in 1996, and revised in 1998, 2002 and 2015, is the key legislation underpinning budget management in Vietnam and covers all levels of government to ensure uniformity of the budget system. Vietnam has 4 tiers of government: central government; 63 provinces (cities); 713 districts (cities, towns) and 11,162 communes (wards). Vietnam's budget system consists of central budget and local budget, in which local budget includes provincial budget (including provincial and district budgets); district budget (including district and commune budgets) and commune budget.

Vietnam is one among a few countries that utilize a nested budget system ('Matrioska') that means lower level budgets are components of higher level budgets. Although it ensures the uniformity of the budget, it reduces fiscal autonomy of local governments and complicates budget preparation and monitoring through bottom-up budgeting and top-down decision-making. In addition, it does not facilitate fiscal accountability of the lower levels of government⁴.

Current Fiscal Decentralization in Vietnam

Expenditure assignments

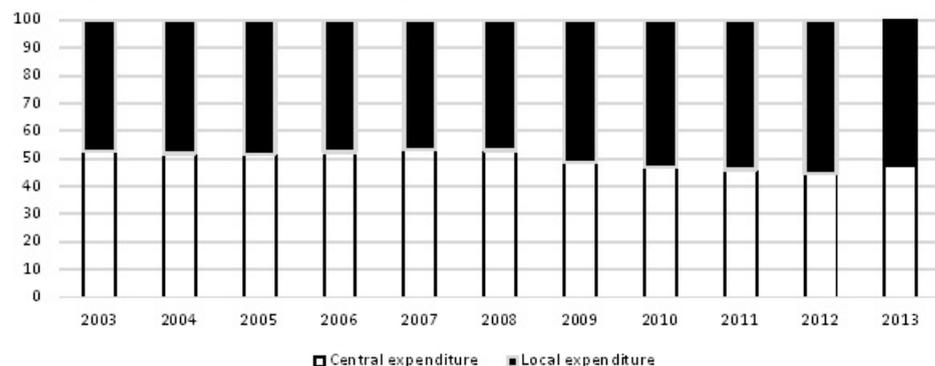
The SBL 2002 lays out the spending tasks that are assigned to the central or local budgets. Spending tasks of central budget comprise: (i) investment spending (investment in construction of socio-economic infrastructure projects managed by the central level; investment and capital support for State enterprises); (ii) current spending (spending on activities in the fields of education, training, health care, social affairs, culture, information, physical training and sports, science and technology managed by the central agencies; spending on national defense and security, excluding the portion allocated to the localities; price subsidies; national programs implemented by the central government); (iii) payment of principles of and interests on Government's borrowings; (iv) aids; (v) other expenditures as stipulated by laws; (vi) additions to the central financial reserve fund and (vii) supplementary revenue to the local budget.

The spending tasks of the local budgets include: (i) spending on development investment (investment in the construction of locally managed socio-economic infrastructure projects); (ii) current spending on locally-managed activities in the fields of economy, education and training, health care, culture, information, science and technology, tasks of national defense and security assigned to the provinces, social policies managed by the provinces; (iii) payment of principals and interest on funds mobilized for investments of provinces; (iv) spending on supplementing the financial reserve fund and (v) spending on supplementing lower-level budgets.

Local spending accounts for a half of total government spending (Figure 5). Both local capital and current expenditures take a large proportion in the total capital and

current expenditure respectively. In 2013, 69 percent of overall capital expenditure and 54 percent of current expenditure were devoted to local governments. Local governments play a particularly important role in public service delivery. In practice, more spending is given to local governments in social sectors such as education, health care, social assistance and economic services. During 2011-2015, local authorities account for the average of 80-90 percent of total current spending for education and around 75-80 percent for health care (World Bank, 2015).

Figure 5: Expenditure position (% total expenditure)



Source: Calculated from Ministry of Finance of Vietnam data (2016)

However, most spending assignments are shared or concurrent. The SBL 2002 currently assigns the same expenditure responsibilities to both central and provincial authorities. Sector legislation in health and education for example provides some clarity in terms of assigning exclusive responsibility for regulation to central government. In general, however, having so many shared functions between central and provinces causes ambiguity over spending assignments. In many cases, both province and district authorities are also assigned the same service delivery responsibility and may lead to overlap and complicates planning and budgeting.

Central fiscal rules and norms on minimum allocations impact adversely on local autonomy. Despite increased power over spending, central fiscal rules and norms affect local autonomy over budget decisions in selected areas and allocate financial resources inefficiently. For example, there are minimum allocations set for education and science and technology without due consideration of actual needs, the level of service provision and capacity to absorb that may lead to waste and the inefficient use of resources⁵.

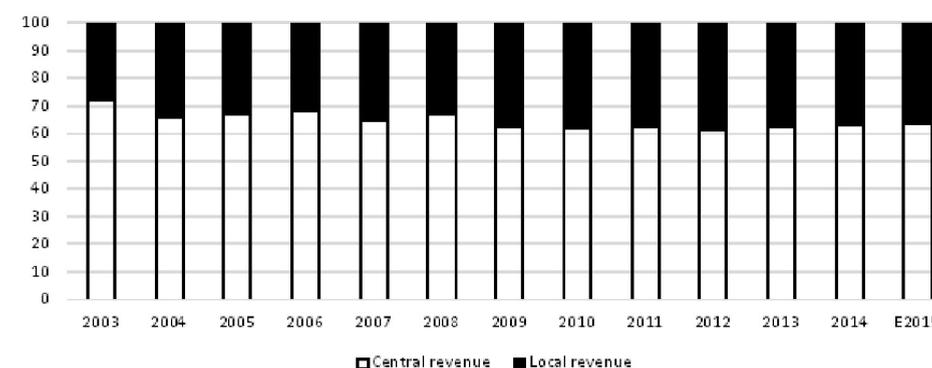
Revenue sharing

According to the SBL 2002, the revenue sources are divided into 3 categories: (i) central revenues includes value added tax (VAT) on imports; excise tax on imports, import and export taxes; corporate income tax (CIT) on enterprises with uniform accounting, taxes and other revenues from petroleum; (ii) revenue retained 100 percent by local authorities includes land tax; natural resource (except petroleum) tax;

registration fees, licensing fees, rental of land and water and sale of state property and (iii) revenue shared between central and local authorities includes VAT (except VAT on imports), excise tax (except excise tax on imports), CIT (except enterprises with uniform accounting), personal income tax, environmental protection tax.

Figure 6 below shows that share of local revenue in total government revenue increased from 28.1 percent in 2003 to 36.4 percent in 2015.

Figure 6: Budget revenue composition (% total revenue)



Source: Calculated from Ministry of Finance of Vietnam data (2016)

Vietnam adopts the "sharing rate" which is kept stable for 5 years (known as the Stability period). In principle, provinces with "sharing rate" less than 100 percent will transfer to the central budget. In the Stability period 2011-2015, among 63 provinces, there were only 13 provinces having revenue transferred to central budget and 50 provinces retaining 100 percent of shared taxes collected in their jurisdictions.

Local authorities have limited powers in setting fees and charges within the ceiling set by the central authority. Local authorities are not allowed to impose local taxes but allowed to impose some local fees and charges that present only 10 percent of total local budget. In practice, revenues retained 100 percent by local authorities are small and unstable taxes and fees with relatively low tax collection efficiency. Increasing revenue autonomy is one of the most significant issues with the current local revenue arrangements in Vietnam. It is important for the efficiency of spending and enables richer provinces to fill their infrastructure financing deficit.

Shared revenues in Vietnam are allocated based on where revenues are actually collected rather than where the tax is incurred, especially for the VAT and CIT. In this case, the major taxes are credited to the local governments where the headquarters of the enterprises are located or the place of business registration which are mainly large cities (e.g. Hanoi, Ho Chi Minh City and industrially developed provinces). It may cause inequality as being likely favour more socio-economic developed local governments.

Intergovernmental transfers

*Vietnam has a relatively transparent, rules-based system of intergovernmental fiscal transfers to narrow horizontal and vertical imbalance, including balancing transfer (or unconditional transfer) and targeted transfer (or conditional transfer)*⁶. Separate formulae are used to determine current and capital spending needs of provinces (and of districts). The formulae use population, geographic location (e.g. mountainous, rural/urban...) and other criteria to take account of the specific circumstances, and therefore funding needs of different provinces.

According to the SBL 2002, the local budgets may utilize revenue retained 100 percent by local authorities, revenue shared between central and local authorities and transfers from the upper-level budget to the lower-level budget to balance budget revenue and expenditure and ensure the implementation of the assigned socio-economic, national defense and security tasks.

The current system has improved equity in resource allocation across and within local governments, but shortcomings still remain. In fact, there is a wide variation in per capita spending across local governments. Provinces with highest spending per capita are 5.6 times higher than provinces with lowest one (Vu Nhu Thang, 2012). Moreover, principles and regulations on allocation have been developed but the 'negotiation mechanism' still exists. Some provinces do not actively attract investments and highly depend on targeted transfers for projects in the areas.

Local government borrowing

*According to the SBL 2002 and the Public Debt Management Law 2009, local authorities are allowed to borrow domestically to finance local infrastructure projects but not to meet current expenditures*⁷. Sources of local borrowing include: (i) the domestic capital market (local bonds, loans from commercial banks); (ii) borrowing from the State Treasury; (iii) borrowing from domestic development banks; and (iv) on-lending from the central government of external funds. All external borrowing is undertaken only through central government on-lending. Currently, share of borrowing by local authorities in Vietnam's total public debt remains small (the average of 3 percent during the period of 2003-2015).

The local borrowing limits help to maintain local debt at prudent levels. For local governments, Vietnam's provinces are required to maintain total outstanding debts below 30 percent of their capital budget (Hanoi and Ho Chi Minh City are exceptions with the ceiling at 100 percent of annual capital budget). In practice, some provinces with higher levels of capital spending needs and strong economic potential have breached their borrowing ceiling.

A ceiling based on annual capital budget is not based on economic rationale. The annual capital budget is unstable and heavily relies on the local revenue. The ceiling of

local government borrowing should monitor both debt service and debt stock that reflect debt sustainability, solvency and repayment capacity.

Aside from direct liabilities, indirect and contingent liabilities need to be closely monitored by local authorities. In fact, explicit contingent liabilities may be the most frequent type of indirect liability but implicit contingent liabilities are often more costly. The latter include bailouts of local SOEs, local governments and natural disasters contingent liabilities, which can significantly add to governments' balance sheet risk and may have a great impact on a country's fiscal position and debt sustainability.

Developments and Reforms

The revised SBL 2015, with effect from fiscal year 2017, ensures the uniformity of the state budget, increases fiscal decentralization and promotes the autonomy of the local governments. It also addresses the shortcomings of the fiscal decentralization in the SBL 2002 through major changes as follows:

Revenue source is classified more accurately and comprehensively and it aims to maximize revenue retained at local budget either through 100 percent local retained or central-local shared revenue, i.e. revenue from fines for administrative violations and other fines is not clearly specified in the SBL 2002 but is mentioned in the SBL 2015 as the central revenue; CIT of enterprises with uniform accounting shall be shared between central and local governments instead of the central revenue according to the SBL 2002⁸.

Intergovernmental fiscal transfers have some major changes. Firstly, according to the SBL 2002, balancing transfers keep unchanged in absolute values during the Stability period, thus difficulties may arise for provinces with limited fiscal capacity. However, the SBL 2015 prescribes that the competent authorities are able to decide an increase in balancing transfers from the higher level budget to lower level budget compared to the first year of the Stability period. Secondly, targeted transfer is well-defined in the SBL 2015 for specific cases as follows⁹: (i) To implement new policies enacted by higher level authorities those are not allocated in the budget estimate of the beginning year of the Stability period; (ii) To implement National target programs and programs/ projects assigned by the higher level authorities; (iii) To support for recovery from natural disasters, epidemics and disasters beyond the fiscal capacity of the lower level budget; and (iv) To support for several major and particularly important programs/projects that have a tremendous impact on local socio-economic development. The total capital investment of central budget transferring to local budget shall be capped at 30 percent of total capital expenditure of central budget.

*Local budgets are allowed in deficit*¹⁰. The state budget deficit includes deficits of both central and local budgets. Local authorities are allowed to borrow domestically but must maintain local outstanding debts under the threshold based on the debt servicing

capacity, i.e. (i) The SBL 2015 caps outstanding loans of Hanoi and Ho Chi Minh City at 60 percent of the revenue retained; (ii) Provinces which have their total retained revenue higher than local current expenditure are required to maintain outstanding loans below 30 percent of the revenue retained and (iii) Provinces which have their total retained revenue not exceeding local current expenditure must maintain outstanding loans below 20 percent of the revenue retained.

The Way Forward and Concluding Thoughts

Since the adoption of the SBL 2002, Vietnam has been achieving a number of positive changes regarding fiscal decentralization and improving the efficiency of allocating and using national financial resources. The proportion of local revenue in the total state budget revenue has been significantly increasing in recent years. Local governments play a more important role in public service delivery with over half of total government spending. Yet in spite of achievements, many shortcomings remain and that requires the revision of legal framework on state budget management. The issuance of the SBL 2015 may have a positive impact on fiscal decentralization and promote the autonomy of the local government. However, decentralization is a continuous process and not a stage that once reached remains immutable (Jorge Martinez-Vazquez, 2011). Consequently, further reforms should be done to improve fiscal decentralization in Vietnam and handle the remaining challenges, focusing on aspects as follows: (i) gradually eliminate the unique nested budget system; (ii) enhancing local revenue autonomy is one of the most significant policy issues, it can be considered through allowing local governments to set tax rates and tax bases for some selected taxes or determining fees and charges; (iii) more explicit assignments on service delivery for different tiers of government within a jurisdiction; (iv) improve local autonomy on budget appropriations; (v) complete the mechanism of intergovernmental transfers including both balancing transfer and targeted transfer in order to promote greater equity in resource allocation¹¹ and (vi) local governments should also closely monitor indirect liability to ensure the debt sustainability.

Fiscal decentralization reform is considered as an important requirement in the process of public finance management reform in Vietnam. However, there is general acknowledgement that decentralization may create a number of benefits but also imply risks. Strengthening fiscal decentralization should be accompanied by improving transparency and accountability of local finance.

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Notes

1. Indonesia: 17.4%; Malaysia: 25.2%; Philippines: 19.4%; Thailand: 22.3%; Singapore: 20.3% (IMF, 2016).
2. The share of current expenditure in the total expenditure increased from 47% on average for 2006-2010 to 63% for 2011-2015 meanwhile the share of capital expenditure in the total expenditure decreased from 29% on average for 2006-2010 to 24% for 2011-2015.
3. Vietnam's state budget reports budget balance, both including principal repayments as well as without it.

The latter is more in line with the Government Financial Statistics (GFS).

4. The higher levels of government have certain "veto rights" over budgets adopted by provincial and sub-provincial authorities (Article 47 of the SBL 2002).
5. Central government sets minimum allocations for specific areas (e.g. not less than 20 percent of total spending has to be allocated to education and at least 2 percent of total spending must be allocated to science and technology).
6. The balancing transfer or unconditional transfer is used to deal with the horizontal balance across local governments. Currently, in Vietnam there have been 50 provinces receiving balancing transfers from the central governments. The targeted transfer is used for specific purposes, i.e. to implement National Target Programs (NTP).
7. Only provinces are allowed to borrow to finance infrastructure projects.
8. According to the SBL 2002, CIT of enterprises with uniform accounting is the central revenue. However, these enterprises use local resources for their manufacturing, production and business activity. Therefore, it is more appropriate if CIT of these enterprises is shared between central and local governments.
9. Article 36 (3) of SBL 2002 only states that *an upper-level budget may provide purposeful supplementary revenue to support the lower-level budget when necessary important tasks emerge, and the latter is not capable of accommodating such tasks even after rearrangement of the budget, and utilization of budget provisions and financial reserve*. However, such tasks are undefined.
10. According to the SBL 2002, local budgets are not allowed in deficits.
11. It needs to complete a set of expenditure norms and criteria as the basis for the budget allocation between central and local governments in order to provide a better ground for strict control over state financial resources utilization. Currently, Decision on promulgating a set of quantitative norms for state budget allocation for investment expenditures in the period of 2016-2020 has been enacted.

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Entrepreneurship and Innovation Policy in Training Systems: A Case of South Korea

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Abstract

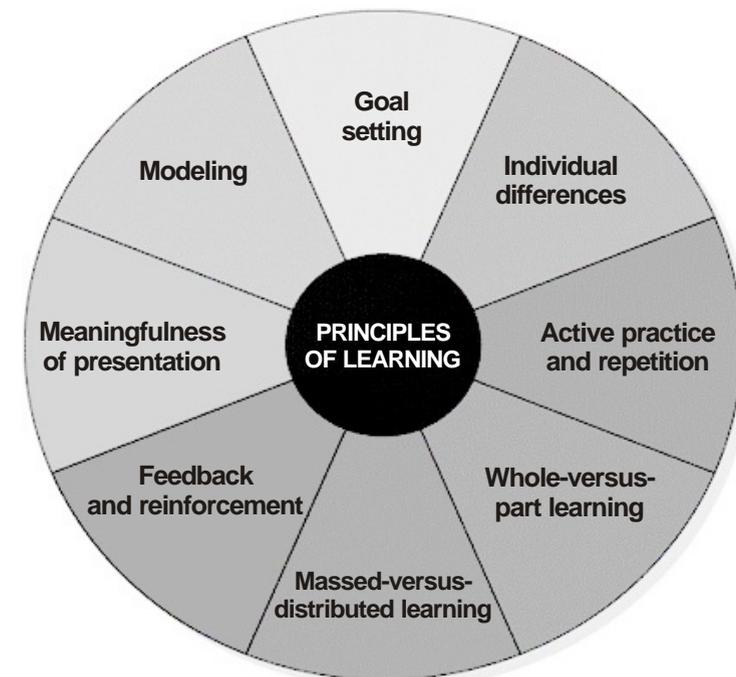
A good training program for officials is a composition of many things. It is designed to address and solve performance problems. In this composition, the main objective is to drive changes in the behavior of staffs in order to achieve performance improvement. But the main question is what kind of changes are needed? A possible answer would be changes that support a capacity building framework for innovation and entrepreneurship abilities of officials in the administration system and the public administration structure. This research is an attempt to discuss the question and its answer. By using a research based on literature review and an expert analysis approach, need definitions, and utilization of national needs of the public sector, the findings were categorized into functions and recommendations. This paper also deals with a case of success in South Korea: National Human Resource Development Institute (NHI) in implementing a new training system for public administration officials and their achievements in the field of application innovation and entrepreneurship in training system. The recommendations focus on the need for assessment centers, reviewing policies and procedures, project level monitoring, monitoring the governance arrangements in wider systems, enriching the context, aligning human resource policies and training strategies and finally designing two sets of roles for training organizations so as to implement innovation and entrepreneurship in their training system.

Keywords: Public Administration, Training, Developing Organizations, Innovation

Concept

Training is any planned activity to transfer or modify knowledge, skills and attitudes through learning experiences in order to maintain levels of competence and respond to the demands of changing circumstances (MSH, 2012). Training is an effort to increase the knowledge, skills, and abilities (KSAs) of employees and managers so they can better do their jobs (Berman, 2016). Principles of learning must be considered in all training activities for officials (Figure 1) (Snell, 2014).

Figure 1: Principles of learning



Source: Snell (2014)

Training and development are used as a strategy for increasing the capacity of broad occupational categories, such as ensuring adequate numbers of procurement and program management officials (Clark, 2013).

The training environment for smart organizations has been changed due to new challenges; globalization, complexity, an aging population, immigration and transition to a knowledge based society. On the other hand, many national programs are not in a position to handle comprehensive training for policy makers and top level managers. Many of them did their educations through general system of state education but they have not been trained especially to be innovative and entrepreneur managers or officials (MSH, 2102).

The idea of training high-level officials like vice-Ministers or General Directors to be more innovative is still uncommon in many countries, even in developed countries. Sometimes it is said that these officials are already "very excellent" and in some cases "very committed" (to satisfy others why he is in this position!) and, hence, not in need of training. The typical perception of training is that it is needed by middle and lower level officials, while no emphasis is placed on the needs of higher level officials. It is the time to recognize that high level officials need more learning opportunities to deal effectively with big surprises as well as other nonrusting affairs, including economic

stagnation, pandemics, climate change, natural disasters, and glocal (global + local) issues (Kim, 2016).

The literature in this research focuses at the following two questions:

- How to design and develop an effective training program for public officials? (National Development Innovation and Entrepreneurship Program)
- How to use modern training methods during the training process? (Innovation and Entrepreneurship Training Policy)

Challenges and Paradoxes

There are new challenges in Human Resource Management (HRM) environment including changes in the administrative system, formalization, openness, globalization, regionalization, specialization, technicalization and democratization. In order to respond effectively to these changes, we need to enhance national competitiveness on many fronts, particularly the competitiveness of the government. One of the key elements that determine the competitiveness of the government is discovering and developing excellent human resources. This is made possible by optimum training (Kook, 2016). The following challenges in this regard are considerable:

- Almost everyone emphasizes the importance of training for officials especially high level officials and all agree that in the past and in the present, these have been insufficiently emphasized but in action the training has been emphasized as a third category (Berman, 2016).
- In many public organizations, responsibility for training and development is shifted down-ward to individual employees, supervisors and units. This is a decentralization trend of training, which has occurred, and many organizations have eliminated training staff in human resource departments. This decentralization does not enable strategic perspective for training in organization. This trend does not emphasize the priority of training and development for employees and supervisors who are responsible for their training (Berman, 2016).
- In today's highly competitive environments in which competition is global and innovation is continuous, being able to adapt has become the key skills. The secret of being successful in comparison with other organizations is adapting to marketplace changes. If any organization wants to be protected from failure, it must be flexible and prepared for the fluctuations of the market because the situation of the market will never be stable for a long time, and organizations should have different plans for different situations in order to survive and being productive and successful (Snell, 2014). This trend is not so clear in public organizations, but innovation and entrepreneurship can foster the abilities.
- Countries' national education program itself is not in a position to handle comprehensive training for policy makers and mid-level managers as many of their

learning objectives are best handled through general management training (MSH, 2016).

- When the officials are provided with adequate training, they can strengthen their job capabilities and help make their government become more competitive. To achieve this ability, we need a shift in the paradigm of training and education in public sector for officials. The traditional paradigm of training emphasis is on planning and control, but the new one emphasis on the ability of competence (Soo, 2016).

Strategic Approach

Training like many strategic activities needs a strategic approach (Hitt, 2014). Strategic planning is, by definition, about intent integration, long-term competitive based thinking and a comprehensive approach to decision making. It is also about innovative fact finding, involvement of differing interests, strategic wants and issues and general agreements of priorities.

Creating a planned approach, focused on agreed challenges and opportunities, and identifying responsibilities for making things happened (Duthchas, 2016). Also strategic approach is the definition of a strategy in which the means are prioritized to achieve an operationally defined strategic goal (RAND, 2009).

The training approach for officials is a strategic one. These strategic focuses include the followings: (Berman, 2016)

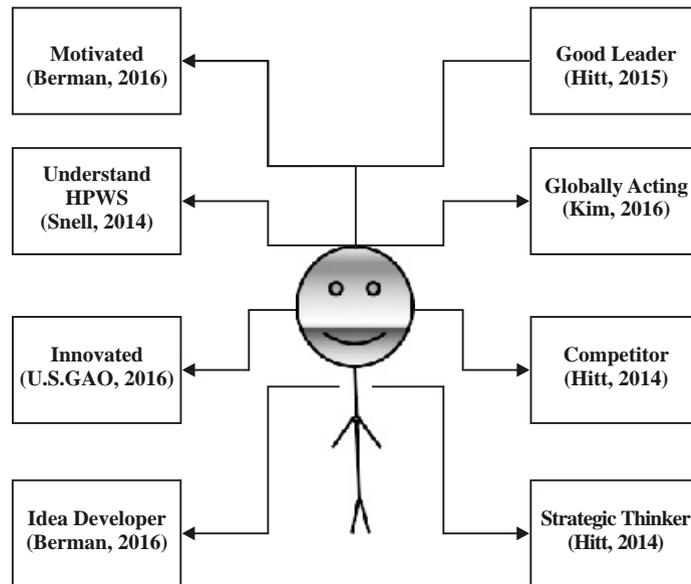
- Helping exiting officials to adapt to new tasks as a result of promotion, restructuring or other reassignments (performance).
- Assisting new employees to get updated on the unique procedures, equipment, or standards of the organization (performance and risk management).
- Ensuring that personnel in the jobs critical to the organizations performance and that have high costs of failure-perform in satisfactory ways (risk management).
- Using training and development (T&D) as a tool to ensure that desirable employees and managers stay current and develop themselves for future roles and hence stay committed to the organization (retention of human capital, talent management).
- Ensuring that all employees have knowledge, skills, and abilities (KSAs) that are consistent with what they need to help the organization move forward (planning).

Who is a trained official?

This is an important question: who is a trained official? On the other words, when we are talking about a trained official what do we mean? (Figure 2). Government innovation starts with human resources innovation, and the development of high-calibre human resources is a driving force of human resources innovation. Future talents

fostered in accordance with new needs of administration public system and human resource development should stand the public innovation and enhancement of national competitiveness (NHI, 2016).

Figure 2: Who is a trained official?



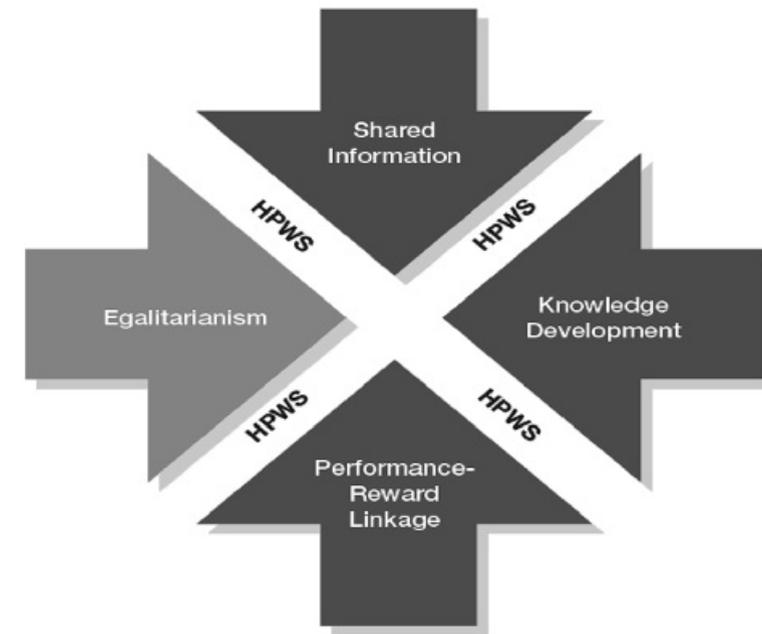
He or she is a motivated one

He or she learns better when he is eager to acquire knowledge, skills and abilities (KSAs), he is encouraged to seek out application opportunities and make them work. Motivation is the driver or energy that compels people to act with energy and residence toward goals. One strategy for motivation is to ensure that officials understand the need for what they explain the reasons for training and the second one is management support with the consequences of training (Berman, 2016).

He or she understands the HPWS

High Performance Working Systems (HPWS) involving a specific set of practices aimed at: increasing the quality of human capital by raising employee knowledge, skills and abilities; motivating employees to contribute greater discretionary effort; and empowering them to help deliver business goals and objectives, appearing to affect firm performance positively (Bacon, 2014). HPWS is a specific combination of human resources practices, work structures, and processes that maximizes employee knowledge, skill, commitment, and flexibility. Also HPWS is a system composed of many interrelated parts that complement one another to reach the goals of an organization, large or small (Figure 3) (Snell, 2014).

Figure 3: High Performance Work System



Source: Snell (2014)

He or she is an idea developer

He or she is able to generate and submit his or her idea for improving one's own work. These ideas can be evaluated based on creativity, feasibility and effectiveness and finally separated for implementation in separate processes. Organizations that adapt significant numbers of new ideas are likely to increase their responsiveness, performance and innovation (Berman, 2016).

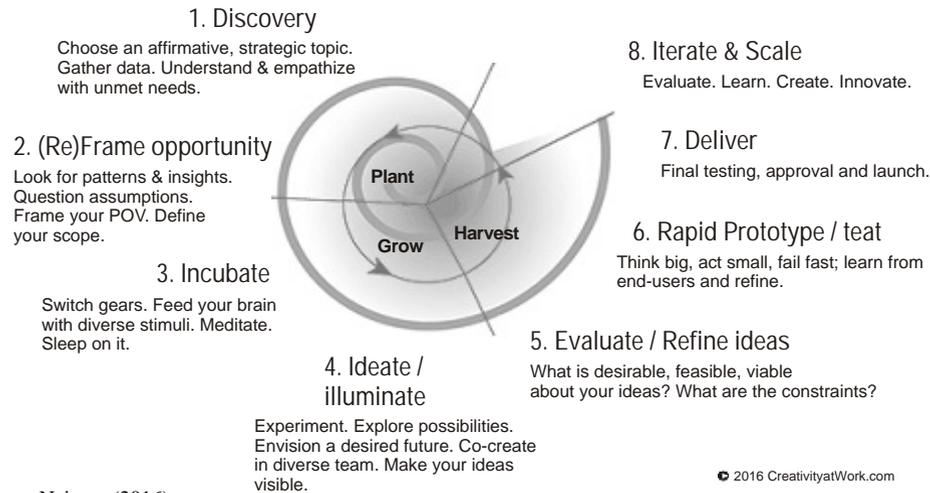
He or she is a strategic thinker

Strategic thinker knows how to develop winning strategies and strengthen the organization's capacity to drive innovation (Harvard, 2016).

- Build innovation into the strategy development process.
- Design innovative, go-to-market strategies that fuel growth.
- Create more value and secure a competitive advantage.
- Identify and exploit new markets that are uncontested.

He or she knows how to create a strategy for guaranteeing that innovation and creativity flourish in the organization? (Figure 4) (Naiman, 2016).

Figure 4: Creative Thinking Process



Source: Naiman (2016)

He or she is a good leader

A learning organization needs managers and leaders who support learning and the search for improvement that implies. This is the ability to manage strategically the changes, to lead people, to build coalitions, to manage business functions, to be results driven, to apply technical knowledge, to calculate risks, to be decisive, and to be customer focused (U.S.OPM, 2010). In addition, they must be able to provide qualities associated with forward looking, open to innovation, able to implement change, and able to bring out these qualities (Berman, 2016). Good leaders enable community building (Trust), foster innovative communities (Creativity), judiciously share power (Wisdom) and inspire change (Courage) (Dumster, 2015).

National Human Resources Development Institute (NHI)

It is a well-known fact that national development in Korea especially in the rapid economic growth has taken place largely because of the country's highly educated human resources (Kim, 2014). The education has two parts: one by regular education systems done by schools and universities, and second by training institutes.

National Human Resources Development Institute NHI (former COTI) was established in Seoul as the National Officials Institute in 1949, and was recognized and renamed as the Central Training Institute in 1961. It was relocated to Daejeon in 1974 and had its current home at the front of Gwanak Mountain in Gwacheon in 1981. NHI is scheduled to open a new campus in Jincheon in late 2016.

NHI operates under Ministry of Personnel Management (MPM) of Korean government under a vice-ministerial structure. The number of staffs at NHI is 144 now, and NHI provided training to 296,000 public officials over the past 67 years. NHI

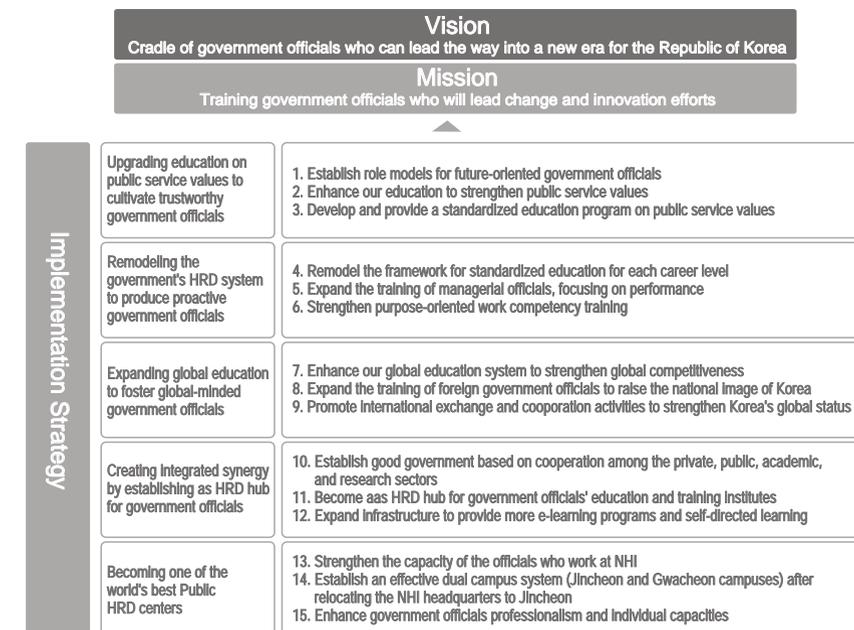
provides leading training services to public officials, giving in-class training to 10,000 officials and cyber training to 100,000 officials every year. More than 4,500 foreign officials from 133 countries have completed training at NHI since 1984 (NHI, 2016). NHI is an important and top priority center for Korea government, since 1981 the Korean president has attended NHI training programs, including the National Strategy Seminal, 28 Items.

Vision and Mission

NHI plays an important role as the national training and education hub by setting standards in public service values and leadership; engaging in the research, development, and evaluation of training courses for public officials' competency development; and leading exchange and cooperation activities with public and private training and research institutes at home and abroad (NHI, 2016). In this regard, based on the NHI mission and vision (Figure 5), the main objectives are:

- To develop outstanding government officials by providing general and specialized training for central government employees.
- To serve as a support center for other public-sector training institutes across Korea while promoting cooperative and exchange activities with private-sector HRD centers.
- To widen Korea's global network through international training and exchange activities with internationally recognized institution.

Figure 5: NHI Mission and Vision



Source: NHI (2016)

As the president of NHI stressed, NHI has established a Human Resource Development (HRD) strategy for a new start. This strategy is an attempt to: (NHI, 2016)

- Strength education on public service values by arranging a set of courses on public service values and providing the training of officials and playing a role as a strategic partner of the current government administration by sharing and publicizing its national vision.
- Ensure quality training by offering customized training to government officials and creating a director level leadership course to enhance the capability of managerial level officials.
- To implement HRD 3.0 as a new paradigm for government operation that features communication, openness and sharing and to build cooperation networks with other public officials training institute and universities, research center and advisory panels.

Based on these attempts, NHI is preparing major reforms by implementing new strategies and new operational framework (figure 6) in its structure to become one of the best HRD institutes, an institute that fosters Korean public officials into the best talents, and an institute that spreads public service values, leadership, and competency development programs to other domestic and foreign institute (NHI, 2016).

Figure 6: Operational Framework of the National HRD Institute



Source: NHI (2016)

Training programs of NHI are combinations of seminars, speeches, workshops, development program for leaders and officials, competency development program, national strategy seminar and international programs for foreign government officials in face to face and virtual structure in a four stage processes. NHI has arranged a set of courses on public service values and provided the training to Korean officials. By the training program, NHI seeks to disseminate public service values among high ranking officials who are responsible for policy initiatives. These programs are managed in 5 levels (Figure 7).

Figure 7: 2016 NHI programs at a Glance

| | Public Service Values | Leadership | Global Mindset | Professional Training |
|--|--|---|---|---|
| Primary Content | <ul style="list-style-type: none"> Understand and practice Public service values including perspectives on The nation, public service, and ethics Share and disseminate the current administration's philosophy and policy direction | <ul style="list-style-type: none"> Define the role of each grade and increase core competence Increase professional competencies, such as the knowledge needed for the performance of public duty | <ul style="list-style-type: none"> Understand the global environment and promote global thinking policy mind-set Strengthen professional global competencies including the ability to carry out international affairs | <ul style="list-style-type: none"> Government policy initiatives and job skills training Computer literacy and organizational dynamics |
| Deputy Ministers - Directors General (Senior Civil Service) | Major Government Projects Seminar | Senior Executive Program | | |
| Division Directors (Grades 3-4) | Intensive Program on Public Service Values | New Senior Civil Service (SCS) Members Program | Global Foundation Programs Global Professional Programs Long-term Overseas Fellowship Programs | International Programs for Foreign Government Officials |
| | | Senior Executive Service Candidates Program | | |
| | | New Division Directors Program | | |
| | | Division Director Candidates Program | | |
| | | New Grade 5 Officials Program Grade 5 Candidates Program | | |
| Grades 4-5 | | New Grade 7 Officials Program (Open recruitment) New Grade 7 Officials Program (Recruitment via recommendation, by region) | | |
| Grades 6 and below | | New Grade 9 Officials Program (Recruitment via recommendation, by region) | | |
| | | - Part-time Employees Program - Disabled Employees Program - Professional Specialists Program | | <ul style="list-style-type: none"> State Policy Initiative Common Core Job Training Computer Literacy Organizational Dynamics |

Source: NHI (2016)

NHI also operates education courses for foreign government officials to support the development of developing nations by sharing Korea's experiences in national development and establishing mutual cooperation systems through exchanges between government officials of many nations, thus enhancing the international image of Korea and contributing to global society.

Trends and Challenges

To achieve its new vision for becoming "a leadership center for a greater Republic

of Korea", NHI needs to provide training that changes public officials' "way of thinking". Thus, with a view to inspiring public officials to think in a bigger, faster, and fairer way, NHI has strived to increase trainees' satisfaction, and has drastically improved its training infrastructure and environment by introducing new training programs and private-sector training techniques (COTI, 2013).

Believing that the quality of lecturers determines the quality of training, NHI is endeavouring to invite the best lecturers to its programs. Because it is a public officials training institute, NHI is subject to some unique constraints, such as only being able to offer lecture fees that are one-third of the amount paid in the private sector. Nonetheless, by introducing the Best Lecturer Award and improving the lecture fee payment system, NHI has been able to arrange for the best lecturers, and thus improve the quality of training.

New attempts have been made to improve public officials' emotional sensitivity. The House of Communication, an open-air tent-like structure, is operated at NHI so that public officials not only receive training at the institute but also enjoy the pleasure of forming new relationships and communicating with others. NHI is transforming the formerly rigid civil service culture into a communicative one by promoting communication and friendships among trainees and between trainees and teachers.

The creativity and innovative approach of public officials is essential for national development. So various cultural and arts programs, such as arts performances and cultural lectures, were introduced by making a cooperation agreement with the National Theater of Korea and the National Museum of Contemporary Art. Meanwhile, NHI developed the Olle Trail, a walking trail lined with herbs and wildflowers and offering a viewing platform, which has made the institute a bright and vibrant space that satisfies the five senses.

To achieve these goals HRD will become increasingly important to support the success of state administration. This means that the role of training institutes will be emphasized more in implementing national development items. In addition, there must be a variety of customer-oriented target-specific training programs. NHI must provide specialized training reflecting officials' grade-levels and personal preferences, and offer retraining to build the competencies found lacking, through feedback from other trainees, in individual officials by considering the following items:

- Expanding training programs aimed at helping share and disseminate the direction of the new government's state affairs management.
- Fostering the competency of government officials by strengthening public service life cycle-based training.
- Providing full-fledged Smart Learning using new learning models.
- Enhancing training programs aimed at strengthening cooperation with foreign countries and the private sector.

- Seek to strengthen the international competitiveness of Korean officials.
- Put sizeable effort into expanding and developing its international programs available to foreign government officials, as part of an effort to increase the number of Korea's cooperative partners in the international area.

Methods for officials training

As mentioned in concept, training is any planned activity to transfer or modify knowledge, skills and attitudes through learning experiences to maintain levels of competence and respond to the demands of changing circumstances (MSH, 2012). Training is the effort to increase the knowledge, skills, and abilities (KSAs) of employees and managers so they can better do their jobs (Berman, 2016).

A usual program for training can be made up of five modules: public service values and the current government's administrative philosophy, general administrative skills, leadership and management competencies, sensitivity training, and communication skill. The training of the employees in South Korea managed by NHI is a process which involves four steps:

Step 1: Needs assessment

Step 2: Developing the training program

Step 3: Implementation the training program

Step 4: Monitoring and evaluating the training program

Step 1: Needs Assessment

There are many needs in the field of officials training that must be covered by content and also new methods of training. Such needs can be characterized as the following: (Sub, 2014)

- Need to enhance training on the administration's philosophy and on administrative tasks. In this regard it is very important to consider local needs and think about native methods.
- Need to reflect a global trend for training center to develop creative human resources with multidisciplinary competencies.
- Need to respond to changes in education environment.
- Need to create public officials with multidisciplinary competencies and global mindsets.
- Need to customize training for each participant.
- Need to establish "smart" training changes in the education environment to keep up

with developments in information technology.

To meet these needs, many old and modern approaches are discussable: on-the-job training, mentoring, in-house seminars, web based learning, professional conference attendance, formal education and etc. (Berman, 2016). But this research stress is on some new methods for officials like those are more capable to promote the abilities of innovation. Approaches like innovation and development hubs, centers and labs, simulation, role-playing, idea development, creative thinking, ethics training, future studying, talent pool, elite management and etc.

Step 2: Designing the Training Program

In this step of training, the goals of training program must be determined, and the training method chosen should be suitable for organization goals and needs. The program must be able to explain the suitable situation for implementation of the training program based on instructional objectives that represent the desired outcomes of a training program (Snell, 2014).

Step 3: Implementation the designed training program

The next step is preparing the situation for implementation of the designed program. It is better to choose the examples from the real environment because the subjective or mental examples and training don't conceive easily by trainees.

Step 4: Evaluating the Training Program

One of the weakest parts of public officials is lack of evaluation system or monitoring procedures in place to assess the effectiveness of training. It is important to conduct a satisfaction survey of participants immediately after the completion of the training program. The monitoring team must conduct cost-effectiveness analyses and feasibility studies on training programs on a regular basis and establish a system of evaluating the program after they are implemented (Soo, 2016).

The evaluation of innovation concept in training program as a policy instrument in training process for governmental officials is a vital task. It must be monitored regarding the value of efficiency and considering performance measurement and quality. In some cases, it can be focused on quality assurance systems. In other words, it has strong affiliations with the concepts and methods of providing innovation management and with concepts that whether the program has been able to increase the skills of innovation and entrepreneurship of officials.

Through the development programs of training based on innovative approach, research centers, and training centers must raise new questions about the quality and relevance of their systems and approach for program evaluation. This trend can be seen as a response to the increased size, complexity and diversity of the public organizations in terms of human resource capacity building, administrative, financial, employment

and organizational affairs. So they need developments in their program with special attention to the issues accrediting state long term innovation program. In the case of effectiveness, balancing the combination of three capacities: creation of knowledge, diffusion of knowledge, and absorption of knowledge must be achieved (Nauwelaers, 2008).

After the implementation of training programs, the designer usually prefers to evaluate the training programs. The evaluation of the programs helps us find the advantages and disadvantages of the designed programs. Usually we use four criteria for assessing the success of the programs: relevance, effectiveness, efficiency, impact and sustainability (Lee, 2016).

Training Strategies

Today developed organizations try to establish an innovation based system to deal with new challenges and opportunities to achieve knowledge economy. In this strategy, training institutions play an important role as a major source of job creation and entrepreneurship (European Commission, 2002). In this process, enhancing public sector innovation performance is a key element for government. Successful organizations understand that improving service delivery requires implementing the right innovation management strategy by empowering the officials of public sector.

In this regard, the national training system as the main holding factors in developing countries are important, but the research presents the idea of a shift from the regular training system of innovation, to professional training institutes as the major engine for creation innovation in developing countries management system based on a knowledge based system training.

To meet the needs, many modern approaches are discussable: on-the-job training, mentoring, in-house seminars, web based learning, professional conference attendance, formal education and etc. (Berman, 2016). But this paper stresses that some new methods for officials are more capable to promote the abilities of innovation. So new approaches can be useful in this regard:

Innovation and development hubs: Some pioneer public organizations have created innovation hubs to provide spaces in which groups of employees and managers can discuss common challenges and find support in implementing new solutions. These hubs can be small offices staffed by a few employees who are able to assist in the development, awareness, and diffusion of new processes. Such efforts acknowledge that while mentoring, in-house presentations, and webbased learning and largely individual centered, group support is also needed to help foster organizational change (Berman, 2016). A good example of mentioned hubs is U.S. Office of Personnel Management Innovation Lab, which started in 2013 to generate concrete solutions for problem in HRM (U.S. GAO, 2013).

Simulation: Vestibule or simulation training is the use of separate areas where workers practice skills or accesses without disrupting on-going work activities. Such experiences help managers to assess staff performance under real-life conditions (Gillespie, 2002). During these trainings, officials are advised of new expectations and are provided opportunities to discuss how they can best handle service challenges (Berman, 2016).

Idea development: The practice of officials generating and submitting ideas for improvement can be a vital method for promotion of officials' innovation. They learn how to produce ideas and how to manage the evaluation of the large number of ideas. Results show that the proportions of officials who view their divisions as innovative are more than doubled, suggesting that such efforts can indeed jump-start innovation in public sector (Berman, 2016).

By this method, officials are able to generate and submit their idea for improving their own works. These ideas can be evaluated based on creativity, feasibility and effectiveness and finally separated for implementation in separate processes. Organizations that adapt significant numbers of new ideas are likely to increase their responsiveness, performance and innovation. There are a lot of good experiences for idea development in Japanese production processes and Seoul Metropolitan Government (Berman, 2016).

Capacity Building for Entrepreneurship and Innovation

Public organizations in developing countries need structural and technical assistance in the form of entrepreneurship and innovation capacity building based on new accepted paradigm in their national education and training system. This capacity building focuses on public training institutes as the second innovators in national innovation system after formal innovation system in schools and universities. This entrepreneurship and innovation training structure enables the public organization to achieve measurable results that will be acceptable to reinvent entrepreneurship and innovation capacity building structure in public sector based on knowledge sharing and knowledge society practices.

On the other hand, in pioneer training institutes, there is a visible trend in improvements, particularly with the capacity building programs in public management sector that increase entrepreneurship capacity of public activities. So it is important to support these experiences in developing organization training system, build on the existing results and achievements and focus on furthering innovation in training section.

The key factor for successful implementation of entrepreneurship and innovation capacity building structure is acceptance of the priority and results by all stakeholders in public sector. This ensures the sharing of responsibilities for entrepreneurship and innovation management and facilitates the transfer of entrepreneurship and the experiences gained. These factors will contribute to the sustainability of the training

project outputs and results. The development and application of produced knowledge must be relevant and in context to the public sector's objectives and the stakeholders needs. Optimum entrepreneurship application is only delivered as part of the innovation processes of the training programs. The objectives and measures of each training program must be common. Most importantly, knowledge growth and use must be specifically related to the individual and organizational objective setting, incentive and reward mechanisms of the organization.

On the other hand, successful entrepreneurship and innovative training programs focus on aligning knowledge and employee development with strategic initiatives in public sector. To achieve this goal, training activities must be integrated into the administration processes that drive entrepreneurship and innovation performance. Linking entrepreneurship and innovation with corporate strategy in the training process has two components:

- Training systems must be integrated with administrative operations systems.
- Training management must be managed as a mission-critical component required advancing and achieving an organization's objectives.

Reinventing capacity building structure for entrepreneurship implementation in training section of developing public organizations must present ambitious objectives to be achieved in a highly diverse environment. It will jointly require a focus on specifics, such as the details of individual directives, and wider generalities such as strategic issues. This is particularly relevant while development and application of the benchmarking tools tailored for the training participants. This diversity requires an effective management and co-ordination structure and a clear statement of objectives, roles and responsibilities.

So the objectives include:

- How to ensure that the capacity building activities and training modules will be developed with participation of officials that will ensure acceptance of the results and commitment?
- How to ensure that substantial research and analysis on the international benchmarking in the field of innovation and entrepreneurship training practices will be undertaken?
- How to ensure the transfer of experience and knowledge to those stakeholders that are not able to be present at the training due to barriers or limited absorption capacity?
- Early development of clear communication mechanisms and channels of communication to facilitate data transfer and the development of working relationships between higher education sections and training institutes.
- Early definition of the exact objectives and expectations of the project from various

parties.

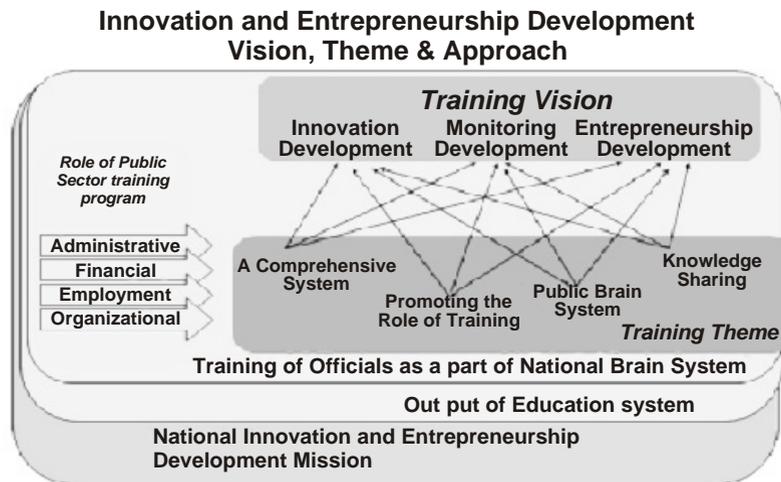
- Development of clear management structures, implementation procedures and formats.
- Strict timings for the different project steps and approval procedures within the project of training.
- Effective quality assurance allowing for comment by local parties/stakeholders.
- Regular monitoring and dissemination of progress reports to ensure continued relevancy to all parties in training.
- Ensuring that experts focus on providing practical advice in an implementable format which focuses on recommendations and the means for achieving and implementing them.
- Final assessment of e-readiness in training section of developing organizations.

Functions

Our focus on the capacity building process of the innovation and entrepreneurship training activities in public sector follows the participatory approach throughout all capacity building activities to have a better knowledge based system.

These tasks can be verified by making some changes in the design and performance of agencies providing training innovation in the public sector. These tasks must be done based on national development innovation and entrepreneurship program by allocating a large proportion of resources, devoting to the innovation section and it could be best served by improving the efficiency of the exiting evaluating system (Figure 8).

Figure 8: National Development Innovation and Entrepreneurship Program



It is well recognized that the current training activities for officials in developing countries are costly, time consuming, and require long term programming, and in many cases do not have adequate efficiency and productivity. In order to minimize the risks as well as to ensure acceptance and sustainability of the capacity building programs, the following tasks must be strictly followed and monitored:

- Task 1: Entrepreneurship and innovation need assessment in training section of public officials.
- Task 2: Identify the main stakeholders in an entrepreneurship and innovation based training system.
- Task 3: Conduct "Focus Group" discussion with the beneficiaries.
- Task 4: Monitor Participation and Satisfaction of officials/ Participants.
- Task 5: Creation a National Structure or Network pattern for entrepreneurship and innovation training in public sector.

Recommendations

The recommendations in this paper have been compiled from the training protocols in literature, policies and procedures submitted by governmental training organizations based on the concept of discovering core competencies in some countries providing smart systems in the structure of domestic training for officials in public section. The results and experiences are applicable for other organizations based on innovation and entrepreneurship training policy which is a component of strategy implementation and training inputs-outputs (Figure 9).

Figure 9: innovation and Entrepreneurship Training Policy



These recommendations focus on the needs of assessment centers, reviewing policies and procedures, project level monitoring, reviewing the governance arrangements in wider systems, context of official training, alignment of human resource policies and training strategies and finally designing two sets of roles for training organization to be able to implement innovation and entrepreneurship in their training system:

The first set of roles can be verified by making some changes in the design and performance of training agencies providing various kinds of researches, and also innovative actions to provide better environment for official training. The second set of categories that can be alleviated by a major change in national training system objectives would give very high priority to an innovative development program.

In recent years, a variety of changes have been made at different levels of education and training of officials. All these changes must be balanced together in all educational and training institutions and government policy centers in order to develop and take advantage of innovation and entrepreneurship training management. The following recommendations are:

- Good training programs for public officials depend on cooperation of all institutions that are responsible for the good governance and ethical in public sector. During the training, stages of the planning and conducting trainings (needs assessment, objective, institutions, trainers, training materials, program, and evaluation) must be discussed.
- It is important to use active learning methods where officials work collaboratively, discusses materials while role-playing, debate, engage in case study, takes part in cooperative learning. Active training methods for public management skills trainings are typical approach for innovative trainings and to deliver knowledge and to improve compliance. It is very important to demonstrate active methods to conduct useful trainings in practice, taking into account specific aspects of the innovative culture, local public administration paradigm, entrepreneurial aspects and the trainings that increase the ability of competence.
- Make the training atmosphere of officials brighter and more positive to enhance the trainers competencies based on a customer oriented training system to through actual experience.
- Organizing new attempts to improve public officials' emotional sensitivity based on this understanding that the creativity of public officials is essential for national development.
- Provide training that changes public officials' way of thinking (thinking ahead, thinking again, and thinking across) with a view of inspiring public officials to think in a bigger, faster, and fairer way to increase trainees satisfaction and self-stem based on a customer oriented training.

- Re-elimination of the existing policies in the field of innovation policy and knowledge management in public sector with concentration on knowledge sharing.
- Considering innovation agencies as a public brain system to advocate changes that will improve knowledge practice.
- Exiting an evaluating system as the main engine for creating innovation especially in e-government structure.
- Process innovation based activities as a major source of job creation and entrepreneurial results to achieve knowledge based society.
- Optimum innovation system empowers social vision that encompasses plurality, inclusion, solidarity and participation.
- Developing and strengthening the Centers of Excellence to support national development priorities.
- Do the implementation of science, technology and innovation policy reviews requested by governments to help them ensure that their policies in these areas support national development innovation and entrepreneurship priorities.
- Consideration of a shift in paradigm of training and education in public sector for officials. As the traditional paradigm of training emphasis is on planning, process and control but the new one emphasis on the ability of leading the individual, organizational and national (Soo, 2016).
- Considering the development of high-calibre human resources as a driving force of human resources innovation in accordance with new needs of administration public system and human resource development regarding enhancement of national competitiveness.
- Establish an effective plan for the placement of the trained resources at the right time in the right place by right costs regarding public human resources development elements.
- It is essential to foster top-level human resources for both the public and private sectors. So it is important to implement a long term national plan regarding public policy in innovation and entrepreneurship regarding the governmental studies to achieve global standards.
- It is important to think about new structure of monitoring for training of officials.in this regard it is important to move away from the previous direction, which focused on scale monitoring to a method on SWOT monitoring.
- It is important for public organizations to improve the competency of public officials focusing on sustainable resources refers to a resource to be able to survive in all conditions .in this regard professionalism and creativity are important as they enhance public service values education for public officials.

- Consideration of a shift in paradigm of training and education in public sector for officials. As the traditional paradigm of training emphasis is on planning and control but the new one emphasis on the ability of competence by the following items (Soo, 2016).

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The Role of the State in Economic Development: Expansion of the Government's Role in Japan from 1945 to 2000

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Abstract

The post-WWII economic development in East and Southeast Asia was a process of catching-up with other industrialized economies in the West. This article aims at explaining why the Japanese Government continuously engaged in the post-WWII economic development and how it contributed the country to an economic prosperity prior to the 1990s. Compared to market-driven approach in understanding the Japanese economic miracle, the author points out that the notion of 'developmental states' (also known as state-led approach) remains most influential explaining the rapid economic growth, at least stabilizing the economy of a country after the bursting of bubble economy. Referring the case of the post-WWII Japan, both the relevant quantitative and qualitative data included in this article clearly proves that the notion of 'developmental states' did constitute as a kind of legitimate and effective industrializing strategy to help promote the economic growth before the 1990s, even under the economic recession in the 1990s, this approach was still able to provide its convincing argument to illustrate how the Japanese Government accommodated, if not kicked out any globalization force, in effect, the economic pressure from the US, which was capable to continue its hegemony in the national economy. Although it has had the growing number of people and scholars to question the validity of 'developmental states', the author argues that the notion of 'developmental states' still had the most significant role to play in the Japanese economy from 1945 to 2000, whether or not Japan experienced its prosperity.

Keywords: Developmental States, Political Economy, Free Market, Post-WWII, Cold War, Economic Development, Japan, Japanese Government, Economic Miracle, Globalization, Bubble Economy, Economic Recession

Introduction

Background

Economic climate and political development are always shaping the lives of people in various sectors of Asian societies. Comparing to those Southeast Asian countries, a great number of East Asian countries were doing well in economic development, at least the rapid GDP growth, particularly before the economic downturn in 1997. After the WWII, Japan was typically seen as a template in all economic miracle for other less

developed countries to learn. In terms of the net household saving of the post-WWII Japan, as indicated in *Table 1*, the Japanese ranking always situated at the second or third highest all around the world (OECD, 2002).

Table 1: Net Household Saving as a Percentage of Disposable Household Income

| | 1960 | 1975 | 1985 | 1990 | 1997 | 2000 |
|---------|------|------|------|------|------|------|
| US | 7.2 | 8.9 | 6.6 | 4.9 | 5.0 | 7.6 |
| Japan | 14.5 | 22.8 | 15.6 | 14.1 | 13.1 | 13.7 |
| UK | 4.5 | 11.4 | 5.4 | 4.4 | 7.4 | 6.9 |
| Germany | 8.6 | 15.1 | 11.4 | 13.9 | 11.6 | 8.6 |
| Italy | 16.5 | 26.9 | 17.8 | 15.6 | 14.5 | 10.8 |
| Canada | 3.8 | 12.7 | 13.4 | 10.5 | 4.7 | 16.6 |

Source: OECD (2002)

Why was the Japanese Economic Development from 1945 to 2000 a Matter?

Borrowing the words from Chase-Dunn and Grimes, '[T]he current world-system is a power hierarchy between core and periphery in which powerful and wealthy "core" societies dominate and exploit weak and poor "peripheral" societies. Within the current system, the so-called "advanced" or "developed" countries constitute the core, while the "less developed" countries are in the periphery. The peripheral countries, rather than developing along the same paths taken by core countries in earlier periods are instead structurally constrained to experience developmental processes that reproduce their subordinate status. In this moving context, core and peripheral countries generally retain their positions relative to one another over time, although there are individual cases of upward and downward mobility in the core/ periphery hierarchy' (1995). Put it simply, the world-system theory above clearly pointed out the structural relations of power or class relations as the fundamental cause of inequalities among states in an international political economy.

To be an exception, the post-WWII Japanese economic development (from the 1960s to the late 1980s in particular) had been unparallel and its economic miracle actually represented an ideal economic institution and practice in East Asia. Such phenomenon before the 1990s could least likely be explained by the world-system theory. Losing almost one third industrial base during the WWII, this defeated country could effectively upgrade to the richest G7 nations within several decades (Vestal, 1993). In the 1990s, however, such miraculous economic boom seemed to come to an end. Its economy since then has not grown very much, unemployment rate has gradually increased and the value of stock market has sunk to one third its 1990 size. Has the economy looked like it might become one of the powerhouses in the post-WWII world really fallen into economic stagnation? If this is the case, how long will it remain there? Is Japan no longer being a good model of economic development of other less developed countries to learn?

Undoubtedly, all questions above seem to be quite difficult to answer at one go since the answer will highly depend on how the role of state (i.e., the Japanese Government) to successfully evolve in the economic arena. However at least, we

understand that history would repeat itself. The study of history provides people with skills which are not confined to the study of the past, so that we are able to further understand what the good of the past was and more importantly we will not commit the similar mistakes in the foreseeable future. In the twenty-first century, what are the economic lessons that the Japanese Government can learn from the past? The objective of this article focuses on the powerful role of state in the Japanese economic development after the WWII. It hopes to allow readers to grasp a more all-rounded scenario regarding why and how the post-WWII Japanese Government devoted remarkable and more significantly sustainable input on the economic development from 1945 to 2000, whether Japan experienced its prosperity or recession.

Conceptual Framework: Market-driven Approach vs. State-led Approach

According to World Bank (1993), economic development could be simply understood as a substantial increase in national income, which mainly measured by the rate of GDP or GNP growth. With respect to the post-WWII Japan, *Table 2* indicating both economic boom as well as the recession (Ichimura, 1998) was actually happening on irregular basis as time goes by.

Table 2: The GDP Growth Rates of the Post-WWII Japan

| Period of Postwar Years | GDP Per Capita (in US Dollars) | Real GDP Growth Rate |
|-------------------------|--------------------------------|----------------------|
| 1945 - 1952 | 380 | 5.0 |
| 1952 - 1960 | 760 | 9.2 |
| 1960 - 1970 | 966 | 10.4 |
| 1970 - 1980 | 4,789 | 5.2 |
| 1980 - 1990 | 14,387 | 3.8 |
| 1990 - 1998 | 32,496 | 2.2 |

Source: Ichimura (1998)

Being an important sub-system throughout the whole society, it is not strange for us to call into question whether the subject of economic development should be mostly driven by the market force, or the state-led effort. In the current literature, there are two bi-polar perspectives which attempt to discuss so. In this article, the author argues why the market-driven explanation is unable to offer as a kind of convincing stance on the Japanese economic success or turmoil but only the state-led force can help provide an all-rounded answer on this.

The Mainstream Perspective: A Market-driven Approach

In the West, the mainstream perspective was originally founded on the assumption that every individual was treated as a rational-choice making agent and as a result maximized personal benefits at the least cost (Allingham, 2002). With regard to the interpretation given by Petri (1993), most economic miracle occurred in the post-WWII East Asia was simply because those countries did seize all 'right fundamentals', including a stable macro-economic environment for saving and investment, as well as a competitive, open economic structure that encouraged the development and growth of enterprises. Put it simply, despite the market failure and the consequent inefficient

allocation of resources, market force can be regarded as the paramount dynamism to lead the economic development without any state intervention.

Regarding the economic miracle occurred in the post-WWII Japan, Denison and Chung (1976) proposed such miraculous economic growth that could largely attribute to a world of 'right fundamentals' such as the high investment level supported by the low-interest rate bank loans, particularly the low-interest rate after 1986, which came from the huge amount of net household saving as listed in *Table 1*. Therefore, a large and active government would just slow down or even worse upset the economic growth.

Undeniably, the mainstream perspective can to a certain extent provide a series of logical and valid arguments how different factors contribute to the economic growth and success, but it is less likely taking into account why the 'right fundamentals' were coming to Japan at that moment. In the words of Friedman, it was obvious that '[A]ppplied to this issue of explaining rather than describing the Japanese economic success, however, the (market regulation) thesis encounters problems. The most serious objection is that references to market efficiency really provide no explanation for Japanese growth at all. If Japanese producers did a better job of responding to market demands, we need to know why they were more capable than manufacturers elsewhere. If the market operated more efficiently in Japan and hence disciplined producers more effectively, we again need to know why this was so' (1988).

Tracing back the explanation made by Denison and Chung for further illustration, this school of thought has not really explored why there was a lower interest rate bank loans to support the high investment rate in Japan during the mid-1980s. To bear a closer analysis, almost everyone can discover whether this perspective has overlooked a deeper and basic factor which was the role of state playing in the Japanese economy. The truth was, to get out from more than one year of economic downturn caused by the revaluation of *yen*, the Japanese Government initially reduced interest rate during the mid-1980s in order to stimulate the domestic demand and subsequently the relevant corporate investment.

The Revisionist Perspective: A State-led Approach

As we can see so far in the above explanation, the mainstream perspective can be merely noted as a kind of supplement because of its structural defect in presenting the ideas. Opposed to the market-led approach, the state-led approach as discussed below mostly viewed an outstanding economic growth and success in East Asia to be the expected result of 'state intervention' instead of 'stimulates a free market' (Wade, 1993). In other words, 'free markets' never exist behind the miraculous economic growth and more importantly the mainstream argument about 'government failure' in East Asia is just an illusion rather than a reality. In the understanding of Wade (1993), he further pointed out that '[B]igger and better markets do often need bigger and better states, while bigger states do often seek to control or eliminate markets.' Clearly here, in the eyes of revisionists, the market dilemma occurred is just a popular appearance of the

post-WWII East Asian economic development.

The leading revisionist to explain the post-WWII Japanese economic development was absolutely represented by Chalmers Johnson. As Araki (2004) wrote, the notion of 'development states' was firstly noted from his classic work, *MITI and the Japanese Miracle: The Growth of Industrial Policy*. With regard to this classic work written by Johnson, the post-WWII Japan could just be seen as a 'developmental state' more than a 'regulatory state' in the context of economic development (1982). Certainly, it does not necessarily mean the Japanese Government was always regarded as a strong state in guiding the country throughout the process of economic development. In fact, the post-WWII Japan even in the twenty-first century has just been in the sense of 'goal rational' and then being a 'developmental state' on one hand, whereas the one in the US has been seen as 'market rational' under 'a regulatory state' on the contrary.

With respect to the economic miracle occurred in the post-WWII Japan prior to the 1990s, Johnson meticulously noted that its success could be attributed to two main reasons, namely the dual functions of industrial policy in industrial rationalization and meanwhile industrial structure policy, under the strong administrative guidance of MITI (1982). As a result, there is no denying that the MITI was mostly playing a crucial role to ensure the abandonment of outdated and bad practices among the Japanese industries. More than that, the strong bureaucrat-business link (also known as 'iron triangle'), namely those MITI's technocrats in close relations with both *Keiretsu* and *Zaikai* (Kerbo and McKinstry, 1998; Sugimoto, 2003) were going a step further in the obvious contribution of initial reconstruction and later development of the post-WWII Japanese economy.

By viewing the role of MITI from another angle, it could at the same time be noted as a new form of nationalism to substitute the failure of militarism following the end of the WWII. As Samuels interpreted in details, such new form of nationalism (techno-nationalism) was considered as an effective political tool for the post-WWII Japan to resolve an ideological conflict between industrialization and democracy (1994) in favor of national unity and social cohesion.

Discussion I: Why was 'Developmental State' Valid to Help Promote the Post-WWII Japanese Economic Growth Prior to the 1990s?

As already examined in the conceptual framework, the explanation obviously proves the groundless arguments of the mainstream perspective at least in the case of Japan after the WWII. Indeed, merely the revisionist perspective is able to offer a more in-depth understanding to explain its continuous economic growth and even miracle, particularly from the 1960s to the late 1980s. In the following, three more factors will be introduced from one to another to help illustrate why the notion of 'developmental states' would be more valid to shape the post-WWII Japanese economy prior to the 1990s.

Historical Factor: Origin of State-led Approach in the Pre-WWII Japan

The origin of state intervention in the Japanese economy can be traced back to the late Tokugawa to the early Meiji period and its successful experience also rooted from what had later been adopted in the post-WWII era at large.

Being challenged by the West since the mid-1850s, in the purpose of 'Rich Country, Strong Army', the newly-established Meiji Government did pay remarkable efforts to put in place the infrastructure of a capitalist industrial economy by the early 1880s (Gordon, 2003). For those industries supported by the government's funding, they were always capital-intensive, producing high-value goods and paying high wages as well as benefits for their employees. In addition, those large firms tended to initiate a lifetime employment system by offering job security to all skilled workers who were in short supply.

Those large firms, were also noted as *Zaibatsu* (just as *Keiretsu* in the post-WWII Japan), started to play a dominate role in the Japanese economy by 'swiftly mobilizing scarce resources of capital, skilled labors and technology in new industrial endeavors' (Gerschenkron, 1962). Referring the Japanese economic map before the WWII, the top four *Zaibatsu* were called *Mitsui*, *Mitsubishi*, *Sumitomo* and *Yasuda* in order of size. After the depression occurred in 1907 and 1908, many medium and small size enterprises had become bankrupt, leading to further development of *Zaibatsu* and their expanding financial influence over Japan.

Beyond Japan gained back its independence from the US in 1952, the basic policy of the Japanese Government was to strengthen this defeated nation by trade and put its top priority on export. 'Export or die' was a popular thinking in those days (Ohno, 2006). Most people at that time strongly believed that they should earn money by export in order to purchase raw materials which they always lacked. In this way, this should be the most crucial point why the Japanese Government set up both Economic Planning Agency and MITI in 1952 in order to achieve the goal of economic independence (without the economic support from the US) and hence offered technological support for those Japanese enterprises.

Cultural Factor: *Nihonjinron* as a National Discourse to Promote the Post-WWII Japanese Economic Growth

Culture is a fundamental but meanwhile complicated term in different cases, which can be noted as the central concept to further understand how a society works. Actually, there is no one true meaning of culture since its definition ('a particular way of life') varied in temporal-spatial situations (Williams, 1982). Borrowing the ideas from Sugimoto, cultural determinism just put the focus on the idea of the cultural uniqueness of Japanese that could help defend its national sense of self against other oppositional ideologies (2003). In fact, such national discourse could be traced back to the pre-WWII era (Kowner, 2002) and in the meantime had its deep roots as discussed in *The*

Chrysanthemum and The Sword, a popular study of Japan by the US anthropologist Ruth Benedict in 1946.

In the post-WWII Japanese economic growth and even miracle, *Nihonjinron* did appear to be a genre again for projecting the indigenous merits of Japaneseness (Morris-Suzuki, 1998). In the words of Kowner, there were premises of *Nihonjinron* including but not limited to the cultural homogeneity of Japanese which 'share a single language, religion and lifestyle and belong to a single race' (2002). Because Japanese people are unique, the implication is that they are superior over foreigners, whether or not in economic achievement.

To be clear, cultural determinism stresses that the Japanese economic success should be an outcome of the unique Japanese character and culture. Since Japan is a vertically-constructed society and most Japanese are of strong group orientation, they are so willing to strictly follow the state guidance or intervention in terms of economic development. In the understanding of Petri, authoritarianism was in this regard legitimated by Confucianism, meaning the long-term political stability in favour of the economic growth (1993). Put it in a concrete way, since most Japanese workers were fine to devote themselves to their corporations because of their 'neo-feudal loyalty' under the Japanese management just as life-long employment (Dohse et al., 1985), this kind of unique Japanese character and culture in all *Keiretsu* and *Zaikai* as a result helped revive the post-WWII Japanese economy within a very short period of time (Glazer, 1976) and even created a brilliant economic miracle thereafter.

Geopolitical Factor: Economic Support from the US to the Japanese Government in a Bi-polar World

After the WWII, the US initially planned to punish Japan in the first year of occupation. However, the Cold War promptly occurred after the WWII and the establishment of China in 1949 drastically changed the US mind. The US Government since then strongly believed that a reliable ally (Japan) under the US control was a must in Asia in the purpose of promoting containment policy to stop the spreading of Communism (Best, 2008). In other words, Japan should not be a threat to the US and its specific geographical location would be further helpful for the capitalist bloc to resist the communist regimes led by both the USSR and China.

In order for Japan to be integrated into the Cold War capitalist order (also known as Bretton Woods System) and thus act as a bastion against Communism, the Japanese Government must be strengthened by the US substantially because Japan might be turned as a Communist state if this defeated nation was too weak in the bi-polar world. With the entire support from the US, the post-WWII Japan was successfully integrated into a semi-peripheral role in the global political economy, in line with the US global policy (Cumings, 1993) against the communist countries.

On one hand, the US stopped its hostility towards Japan starting from the

introduction of Dodge Line in 1949 (Ohno, 2006). Further funds provided by the US Government were injected to ease the Japanese financial deficit and inflation, as well as to limit the over-issuing currency. As expected, the Japanese economy was gradually stabilized. From the early 1950s, the US even did not request Japan to pay any war indemnity as previously mentioned. More notably, Japan had just dismantled 7% machinery required in the indemnity plan, that helped a lot the economic recovery. On the other hand, with the full support from the US, Japan was at the same time allowed to join those economic international organizations under the Bretton Woods System the World Bank and IMF in 1952; GATT in 1955 (Brown and Ainley, 2009). Since China had been contained by the capitalist bloc specifically after the Korean War, the non-Communist economies of Southeast Asia became to the fore as both a source of important raw materials and a market for the Japanese export-oriented economy.

What finally deserves to highlight at this point would be the special procurement brought by the Korean War and the later Vietnam War from the US Government towards Japan. Not only the revenue and consuming power of most Japanese people had greatly increased which led to a great prosperity in consumption, but also numerous foreign reserves were earned by the Japanese Government as a powerhouse to keep implementing those huge economic plans in every three to five years thereafter.

Discussion II: How did 'Developmental State' Work in the National Economy, whether Japan was in Prosperity or Recession from 1945 to 2000?

The Occupation Period (1945 - 52)

Japan was defeated in the WWII and surrendered to the Allied Forces in 1945. Referring the data indicated in *Table 3*, as the defeated country in Asia, one fourth of national assets was destructed in such aggressive wars and this scenario was noted as the main reason to explain why Japan had only achieved the very limited GDP growth in the early recovery period, as previously shown in *Table 2*.

Table 3: Destruction of National Wealth (Billion yen)

| | Total Damage | Estimated Value of Undamaged State | National Wealth Remaining at War's End | Percentage of Damage | National Wealth in 1935 (Calculated at Value at War's End) |
|--------------------------------|--------------|------------------------------------|--|----------------------|--|
| Gross Value of National Assets | 64.3 | 253.1 | 188.9 | 25 | 186.7 |

Source: Takafusas (1994)

During the occupation period until 1952, Japan was occupied by Allied Forces, in effect the US force. General Douglas MacArthur, Supreme Commander for the Allied Powers, was in charge of the Occupation Authority and meanwhile he embarked on a series of reforms in the post-WWII Japan (Gordon, 2003). In 1946, *Keizai Antei Honbu*

(also known as Economic Stabilization Board) was established to formulate a national policy and reconstruction. The Board had extensive and peremptory powers, which absolutely made it play the role of powerhouse in economic planning in the occupation period and it obviously marked the beginning of state-led economy again in the post-WWII Japan. In 1947, a radical reorganization leading to a considerable expansion in the size of Board was further carried out, including the formation of MITI (Uchino, 1983) which was to be clear lining with the state-led approach. The function of MITI, in the words of Wolf, this was 'a system of business activity which can best described as "economic totalitarianism", government-directed enterprise in which all the energies of Japan have been mobilized to overwhelm world competition' (1983). To make this in simple, the joint collaboration of business, government and party (The Liberal Democratic Party since 1955) in power would be at the same time responsible for the initial economic recovery and later economic growth.

According to Takafusas, there were three main themes regarding the economic reform arena in that period of time, which included the dissolution of *Zaibatsu*, the anti-monopoly law and deconcentration, and democratization of labors (1994), with the goal of liberalizing Japan with never to be a possible threat to the world peace after 1945. Perhaps the half-hearted *Zaibatsu* dissolution was a convincing way to further help illustrate how the post-WWII Japanese economic reforms were introduced with political motives. Since the *Zaibatsu* had had close correlations with most politicians during the inter-war period and this had somehow furnished to the later outbreak of the WWII, the Occupation Authority under the US leadership therefore determined to dismember all *Zaibatsu* according to the Yasuda Plan in 1946. Yet, from 1948, such dismemberment policy drastically changed to the reconstruction of new *Zaibatsu* as it was hoped to safeguard Japan to stand on its own foot by getting rid of communism in the bi-polar world.

The Reconstruction and High Growth Period (1952 - 73)

When the American occupation came to an end during the early 1950s, the post-WWII Japanese economy was going to stabilize. According to Vestal (1993), from 1951 to 1954, the real GDP growth rate was 7.4% in average per year. This could be probably explained by the outbreak of the Korean War in the early 1950s so that the US had made use of Japan as a base of operations and providers of wartime materials to fight against the communist bloc. Needless to mention, the wartime demand was a remarkable boost to Japanese economy and therefore provided the funding Japanese needed to get their economy going.

With the help of sufficient funding, the Japanese Government tried to launch its targeted industries like petrochemicals, coal, iron and steel, electric power, and fertilizers. This targeting was mostly done by MITI and companies that followed MITI's directions received bank loans made possible by the government's support (Johnson, 1982). Textiles were the first main foreign capital earner. They were quickly followed by shipbuilding. In the late 1950s, Japan became the world's largest ship building

industry in the world. And throughout the 1960s, Japan began to develop its strengths in automobiles, motorcycles, electronics and capital equipment. At that time, the Japan's motor vehicles had monopolized the domestic market and gradually started to compete in the overseas including but not limited to the US market as well.

In every three to five years after the occupation period, the Japanese Government kept announcing eye-catching economic plans to stimulate the GDP growth as highlighted above. After the Economic Self-reliance Five-year Plan held in 1955, the Prime Minister Ikeda Hayato further announced a Ten-year National Income Doubling Plan in 1960. He did set a goal of 7.8% annual growth during the decade (1961 - 70), in the purpose of significantly raising most Japanese living standard by increasing infrastructure construction, advancing technology, developing expertise, restructuring certain industrial sectors and improving external trade with international cooperation (Lin, 2005). In order to help achieve the goal of this plan, the Japanese Government subsequently formulated its financial policy, reduced tax and interest rates, and injected more public funding for the development of transport infrastructure. In terms of the development of transport infrastructure, there was an opening of the Tokaido bullet train between Tokyo and Osaka in 1964. Besides, a superhighway between Komaki and Nishinomiya was constructed in 1965.

The Japanese economy in 1945 had adversely retreated by twenty-five years. Yet, *Table 4* below indicating the economic planning of the Japanese Government aimed at expansion of the industrial base to be obvious proved exceedingly successful to meet the official expectation, which the economic situation in Japan (excluding external trade) could recover to the pre-war level in the 1950s. The 1960s was the most remarkable decade of the Japanese economy. By 1968, Japan did surpass the West as the second largest economy in the world, just next to the US. The 1960s unemployment rate at the same time was low, less than 1.4%, except for 1960 when it was 1.6% (Hamada, 1996). During the early 1970s, following the prior government's anticipation, national income in Japan had actually doubled with achieved an average annual growth rate of 10%.

Table 4: GNP, National Income and Personal Consumption Expenses (Trillion yen)

| Year | GNP | National Income | Personal Consumption Expenses |
|---------------------------|-----|-----------------|-------------------------------|
| Base Year (1956) | 9.5 | 8 | 6 |
| Target Year (1970) | 26 | 21.5 | 15.5 |

Source: Lin (2005)

The Restructuring Period (1973 - 90) and the Bursting of Bubble Economy during the 1990s

After the rapid growth period, the economy in Japan to be unfortunate encountered unavoidable challenges. It often fell into recession, but always managed to restructure itself and came out stronger. Instead of continuing to discuss how the Japanese Government chipped in continuous efforts to maintain the economic prosperity during

this period, what the illustration below focused on how the Japanese Government in the contribution of the formation of bubble economy and most critically its dealing method after the bursting of bubble economy.

Being an island country which lacks most natural resources, Japan has always relied on export-oriented industries to generate its revenue to import what is needed from overseas. From the high-growth period, the Japan's competitive strength was going to overwhelm the industries of the US and Europe, which unavoidably bringing the seriousness of trade conflicts between Japan and a number of European countries. In the explanation of Kanemitsu (1989), the trade relations with the US at that period (1974- 82) could be noted as competing partners rather than patron-protégé as in the previous decades. In fact, the immense trade surplus enjoyed by Japan was mostly based on the enormous trade deficit of the US (Iyoda, 2010). Hence, on one hand, the US Government tried to activate neo-protectionism to restrict the quantity of the Japanese export through the Voluntary Export Constraints (VERs) in terms of the textiles, color TVs, steel, machine tools and automobiles through the Japan-US Structural Impediments Initiative Talks in 1990. On the other hand, the US Government kept putting great pressure on liberalizing the entire Japanese market, and even called to amend the structure of 'iron triangle' and hence informal practices of political economy in Japan (Ito, 1993).

Facing the diplomatic and economic pressure mainly from the US, following the Plaza Accord as a kind of globalization force to be effective in 1985, the Japanese Government had no more alternative but to promise to increase the value of *yen* since then, which then unavoidably marked the beginning of the formation of bubble economy. It never rained but it poured, i.e., such kind of the globalization force without doubt exposed Japan to labour force dispersal (Befu, 2001). The bygone optimistic economic environment in Japan as a result forced those discontented labour force to seek opportunities outside Japan. The increasingly frequent interactions by virtue of more efficient but cheaper transportation and information system, really facilitated a great number of job applications to foreign companies and overseas business establishment. Although the globalizing force superficially contributed a lot to the affirmative development of Japanese economy, we should not forget that the impact of *yen's* appreciation which will be further discussed as below because of its relatively higher maneuverability by the Japanese Government (through both fiscal and monetary policies) while comparing to that of other possible factors resulted by globalization and also by social development, e.g., human dispersal and aging population respectively.

Doubtless, the increase the value of *yen* to be affected by globalization would inevitably compress the living room of most Japanese enterprises because of the cost of their exports would sharply increase at the same time. To compensate the loss of such Japanese enterprises, Japan Bank finally decided to lower the interest rate more than a half from 1986 to 1987. The low-interest rate under the strong state intervention unavoidably made the speculation of real estate for many Japanese enterprises to

borrow money from *Jusen* (also known as Housing Loan Company) very popular during the late 1980s as listed in *Table 5*.

Table 5: The Percentage of *Jusen* Housing Loans to Individuals and Business

| | 1971 | 1975 | 1980 | 1985 | 1990 | 1991 | 1992 | 1993 | 1994 |
|---|------|------|------|------|------|------|------|------|------|
| Housing Loans to Individuals (Percentage) | 100 | 99.5 | 95.6 | 67.0 | 21.4 | 21.4 | 21.6 | 21.4 | 20.6 |
| Housing Loans to Business (Percentage) | 0 | 0.5 | 4.4 | 33.0 | 78.6 | 78.4 | 78.4 | 78.6 | 79.4 |

Source: Hori (2005)

Worse still, a great number of Japanese enterprises were increasingly turning to the stock market to fulfill their capital needs, which once again motivated banks to compete in obtaining business from other borrowers. Combining all such factors to be unfortunate led to inflation of stock and also real estate prices. To be affected by the mechanism of 'iron triangle', most Japanese banks encountering such situation did not carefully examine the credit worthiness of many of the borrowers or the worthiness of their proposals very well. As Misawa observed, the loan was just approved in accordance with the related bank's analysis, evaluation of information collected and systematically accumulated by the bank through its historical transactions with that corporation (2006). In other words, no formal or reliable mechanism was taken to secure bank's interests such as collecting loans from those target corporations or if necessary dealing of non-performing loans under the unexpected or disastrous situation.

Such madness speculation in both stock and also real estate markets eventually made the bursting of bubble economy in the early 1990s, most Japanese banks could be seen as the victims in this economic turmoil. Bankruptcies of financial institutions including banks and the resolution of non-performing loans did become a serious problem. In particular, a huge amount of credit (i.e., around forty trillion *yen*) secured by the real estate sector was not recoverable (Misawa, 2004). As discussed in the earlier paragraph, *Jusen*, funded by both commercial banks and agriculture and forestry-related financial institutions, sharply increased lending to the real estate sector without careful consideration in the 1980s, and they were severely saddled with massive non-performing loans in the early 1990s. *Jusen* problem was in fact the first of a series of crises in the Japanese financial sector after the bursting of bubble economy. For such paradigmatic circumstance, there were indeed growing number of people and scholars to severely criticize the financial regulatory failure (Milhaupt and West, 2004) of the Japanese Government. However, it would just be seen as a kind of one-sided explanation, if not an illusion to wholly indicate the ineffectiveness of state-led approach in the 1990s. In my understanding, the proposed solution by Ministry of Finance (MOF) with the bankruptcy of Long-term Credit Bank of Japan (LTCBJ) was a counter convincing proof to help me do the relevant refutation.

LTCBJ was one of the banks that was so aggressive in lending loans to construction and real estate related industries during the 1980s, and just as the case of *Jusen*, most of these loans turned out to be bad-debts (Misawa, 2006). Although MOF's

bureaucrats intended to take a series of conservative means (i.e., state-led approach) instead of rely on market or globalization force to solve the LTCBJ's bad-debts, their proposed solution as expected was quite effective in the very beginning if not to be always interfered by other factors that were out of control by the Japanese Government. In particular, the public resentment in Japan against the official action to save the failed financial institutions was so strong since 1995, that it became a political taboo to refer to use of any public funds to address the banking problem (Basel Committee on Banking Supervision, 2004) just as the situation of LTCBJ before its bankruptcy in October 1998.

As an alternative to save LTCBJ, what the Japanese Government could do by then was quite limited but state intervention was still able to step in to deal with LTCBJ's problem as much as it could. In June 1998, Sumimoto Trust Bank was selected to be lobbied, if not coerced by the Japanese bureaucrats behind the scene to reach a merger agreement with LTCBJ. Unfortunately, the bi-polar insights between these two banks indicated in the merger press conference held on 26 June had seriously triggered investors' concern, which both banks' stock prices drastically dropped (Tett, 2004). Such unexpected result from the stock market that was without any relationship of state-led approach's effectiveness or ineffectiveness issue had announced the end of 'cooperation' between both banks and more critically marked the prelude of LTCBJ's eventual bankruptcy. Rather than a brutal shakeout, which would result to demise of weaker financial institutions just as LTCBJ since the mid-1990s, MOF's proposed solution mostly preferred to keep such failed bank afloat in the last minute so as to avoid the ripple side-effects of bankruptcies and unemployment (Hori, 2005), in order to secure the interests of the Japanese bank sector and as a whole most population of this country. The above mentioned consideration and proposed solution in solving LTCBJ crisis by the Japanese Government to be clear was noted as a kind of reflection that most of the things in this case were worked out under the notion of 'developmental states' step-by-step successfully.

In addition to those orderly attempts made by the Japanese officials to save LTCBJ, there were still quite a great number of substantial proof after that to let us understand how the notion of 'developmental states' still played its hegemonic role in the national economy during the 1990s. The LTCBJ crisis as highlighted earlier actually led to two new pieces of important legislation in Japan, which were Financial Reconstruction Law and Financial Function Early Strengthening Law (Basel Committee on Banking Supervision, 2004) as the systematic management to deal with the potential bank sector's crisis if necessary. With the new comprehensive safety framework in place, the Japanese Government since then was more capable to save a failed bank especially in the early stage and of course without triggering the negative concern of most populace or mass media. Based on the above new financial laws, tax revenues of more than seven trillion *yen* were used to prop up the faltering fifteen financial institutions in 1999 (Misawa, 2004) to rebuild the creditability and reliability of the Japanese bank sector. With the similar purpose, the Deposit Insurance Law was further amended in 2000 to

fully protect deposits with two or three more years. Despite the wave of globalization, state-led approach to be obvious engaged in the whole 1990s would still be seen as a capable engine to exert its notable influence to the Japanese economy.

Conclusion

The politico-economic process involved in the post-WWII Japan is as highly complex as in other countries in East and Southeast Asia. Just referring what has been discussed and analyzed in this piece of article, the above review clearly illustrates that the state-led economic development in Japan would be mostly effective, what the difference before and after the 1990s is how much efforts that the government should accommodate or co-work with the globalization or market force. To make it in simple, the success of the national economy in my understanding mostly depends on how 'good' economic choices can be eventually made by the specific political characters and even the entire government. To understand the intricate interactions between politics and economy in an in-depth way, more and ongoing related quantitative and qualitative studies are essential in order to formulate a set of more accurate conceptual framework to explain such political economy's model, and as a result provide a set of more all-rounded underlying reasons of illustrating both economic boom and downturn in particular.

Compared to the situation in the 1990s, the twenty-first century's economic hardship in Japan has undeniably been lessened under the guidance of state-led approach but is still difficult to explicitly predict whether or not the Japanese Government would continuously implement such structural reform programmes starting from the Prime Minister Junichiro Koizumi to stimulate the economic growth. For instance, the current state-led, or more accurately, Abe-led economic policy recently aims at exploiting the economic potentiality of Japan through the active sustenance of an inflationary environment (Mark, 2016). It is no denying that the ultimate goal of Abenomics is to boost the stagnating the Japanese economy by initiating reflation. Although the affirmative effects, namely, the hike of stock price and GDP, as well as the declining unemployment rate, are observed, the rise in consumption tax really hinders the upward motive force of the entire Japanese economy (Wakatabe, 2015). Reasonably, the aftermath of Abenomics remains opaque in the current stage but myriad adjustments and adaptations among the economic sectors in response to the fiscal and monetary changes brought by Abenomics and the consequent political and intellectual resistance are expected. As a result, it is still far too early to assess or even speculate the possible outcome and consequences of Abenomics to the Japanese as well as to the global economy.

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PUBLIC ADMINISTRATION AND POLICY An Asia-Pacific Journal

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Scott, I. (2010). *The Public Sector in Hong Kong*. Hong Kong: Hong Kong University Press.

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Cross-border Partnerships in Higher Education: Strategies and Issues, 169-190. New York: Routledge.

Mok, K.H. (2003). Globalization and Higher Education Restructuring in Hong Kong, Taiwan and Mainland China, *Higher Education Research & Development*, 22, 117-129.

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