Economic Crisis and Corporate Restructuring in Korea
Reforming the Chaebol

Asian business conglomerates have clearly been successful agents of growth, mobilizing capital, borrowing technology from abroad, and spearheading Asia’s exports. However, these firms have long had a number of organizational and financial weaknesses, including heavy reliance on debt, that make them vulnerable to shocks. Nowhere was this more true than in Korea, where the large corporate groups known as chaebol have dominated the economic landscape. This collection of essays by leading political scientists and economists provides a comprehensive examination of the chaebol problem in the wake of the Asian financial crisis. The authors consider the historical evolution of the chaebol and their contribution to the onset of economic turmoil in 1997. The book analyzes the government’s short-run response to corporate and financial distress, and outlines an agenda for longer-term reform of the financial system, corporate governance and the politics of business–government relations.

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Economic Crisis and Corporate Restructuring in Korea
Reforming the Chaebol

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Preface and Acknowledgements

The origins of this project go back to a grant that Lawrence Krause submitted to the Korea Foundation just as the economic crisis in East Asia was unfolding. At the time, Krause was the Director (and founder) of the Korea Pacific Program (KPP) at the Graduate School of International Relations and Pacific Studies (IR/PS) at the University of California, San Diego. With this generous grant in hand, Krause and Stephan Haggard, also at IR/PS, approached the Korea Development Institute (KDI) about the prospect of collaborating on a project on the crisis and its aftermath.

On coming to office, Kim Dae-jung had outlined an ambitious reform program in four areas: corporate restructuring; the financial sector; labor markets and social policy; and government institutions. All posed challenging inter-disciplinary issues, but after consultation with colleagues at KDI and the KDI School, including Hong-Tack Chun, Seong Min Yoo and Sang-woo Nam, Haggard and Krause narrowed their focus to the area of corporate restructuring. Reform of the chaebol has long been a privileged issue in Korea, and the economic crisis added a new sense of urgency to it. They presented their ideas to KDI president Jin-soon Lee and got a supportive response.

The Asian financial crisis and the issue of corporate restructuring had already captured the attention of both institutions. At IR/PS, Haggard and Krause had convened a faculty seminar on the crisis that included among others Peter Gourevitch, Takeo Hoshi, Miles Kahler, Euysung Kim, Andrew MacIntyre, John McMillan, Peter Timmer, and Christopher Woodruff. That seminar spurred a substantial and diverse body of research. Krause had been commissioned by the Council on Foreign Relations to write an early assessment of the crisis, which appeared as The Economics and Politics of the Asian Financial Crisis of 1997-98. Krause’s analysis was the first to include serious consideration of political issues. Fred Bergsten at the Institute for International Economics encouraged Haggard to write a book on the politics of the crisis, which appeared in late 2000 (The Political Economy of the Asian Financial Crisis). Hoshi had been working on the Japanese financial system for
some time, and published important work on the topic including *Crisis and Change in the Japanese Financial System* (co-edited with Hugh Patrick, 2000) and *Corporate Financing and Governance in Japan* (with Anil Kashyap, 2001). Haggard and MacIntyre collaborated on several articles on the crisis, and MacIntyre initiated a book that offered a comparative look at the Southeast Asian cases (*The Power of Institutions: Political Architecture and Governance*, 2002).

As a public research institute supported by taxpayers, KDI was intimately involved in the policymaking process in the wake of the crisis. Jun-Il Kim participated in Korea’s debt rescheduling negotiations and provided policy advice to the Minister of Finance and Economy as his Senior Adviser. Bum Soo Choi and Seong Min Yoo held similar positions at the Financial Supervisory Commission and the Fair Trade Commission. At KDI itself, an institute-wide effort was organized to craft a master plan to clean up nonperforming loans and carry out structural reform. This effort culminated in the publication of *A Master Plan for Overcoming the Crisis and Restructuring the Economy* (in Korean) in April 1998. In the summer of the same year, Dong Chul Cho argued that the IMF’s high interest rate policy had served its purpose and made a strong and ultimately successful case for reflationary policy.

As the tumultuous year of 1998 came to a close and the Korean economy began to show signs of recovery, KDI researchers finally found time to turn to more academic endeavors. Youngjae Kang and Il-Chong Nam organized a conference with OECD on corporate governance in Asia, later published as an OECD report. Dong Chul Cho, Joon-Ho Hahm, Chin Hee Hahn, Kiseok Hong, Sung Wook Joh, and Inseok Shin collaborated with American economists to publish *The Korean Crisis: Before and After*. In a joint project with the National Institute of Research Advancement of Tokyo, Ha Won Jang, Youngjae Lim, Wonhyuk Lim, and Jung-Dong Park worked with Japanese scholars to produce *An Institutional Perspective on the Korean Crisis and Implications for Japan*.

The definition and initial organization of this project were undertaken by Stephan Haggard and Seong Min Yoo, but Yoo left KDI in February 2000 and the management of the project there was taken over by Wonhyuk Lim. Euysung Kim (IR/PS and KDI School at the time) also joined the team. They quickly saw eye-to-eye on two critical issues. First, although the area of corporate restructuring involved a number of complex economic questions, it also engaged the domains of law, public policy and politics. Although most of the participants in the project were economists, it would be important to draw in political scientists and to urge economists to consider political economy and legal issues. Chung-in Moon, Byung-Kook Kim and Jongryn Mo all agreed to
Preface and Acknowledgements

participate early in the project adding their strong reputations to the project. Second, the co-editors agreed that the breadth of the project required that it draw talent from as wide a pool as possible. Connections to a variety of institutions, including Korea and Yonsei Universities, the Korea Institute for International Economic Policy (KIEP) and the Korea Institute of Finance (KIF), allowed us to identify a diverse and high-quality team of participants.

The first project meeting was held in Seoul in March 2000. In addition to the paper presenters, the workshop had the benefit of high-quality commentary from Sriram Aiyer, Peter Beck, Sea-Jin Chang, Eun Mee Kim, In-young Kim, Seung-Cheol Lee, Robert Liu, Sangwoo Nam, Kap Soo Oh, and Yong-Seok Park.

A second project meeting was held in La Jolla in October 2000. As with the first meeting, that workshop was deepened by the participation of a number of outsiders, including Young-Nahn Baek, Peter Beck, U Tak Chung, Tamio Hattori, Takeo Hoshi, Satoshi Koibuchi, Larry Krause, Chung Lee, Bill Mako, David McKendrick, Marcus Noland, Bee Roberts, James Shinn, Yoshio Tsutsui, and Meredith Woo-Cumings.

All academic research depends on financing, and this project was no exception. Particular thanks are owed to the Korea Foundation for getting the ball rolling; without their initial support, the project would have been impossible. Ms. Young-Joon Min deserves a special note of thanks for the assistance she provided the project throughout.

KDI made the largest financial contribution to the venture, but even more importantly, freed the time of its researchers to work on this effort. The Korea Pacific Program at IR/PS contributed resources and we were fortunate to get financial and moral support from Peter Beck at the Korea Economic Institute (KEI) as well. KEI financed the attendance of several participants at the October 2000 workshop and Beck’s comments and leads proved valuable at a number of points.

No project of this magnitude can work without administrative support, and Haggard and Kim would like to extend particular thanks to Kay-Marie Johns for her management of logistics and editing. Karen Johns also contributed to this task. Lim would like to thank Hyun-Ok Chung for taking care of the logistics of the workshop in March 2000. Jina Yu also contributed to the project.

As the project began to take shape, Haggard opened discussions with John Ravenhill, editor of the series on Asia-Pacific Studies, on bringing the project to press. John’s encouragement played an important role in bringing the book to publication at Cambridge University Press. At the Press, the authors would like to thank Marigold Acland, Karen Hildebrandt, Paul Watt and Amanda Pinches, as well as Janet Mackenzie.
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Two anonymous reviewers provided unusually detailed and useful comments; those comments spurred more revision of the manuscript than they might know.

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Policy Planning. He is the co-author of Financial Reform in Korea (1997) and The Financial Supervisory Authority Reform in Korea (2000), and has written numerous papers on financial and corporate reform.

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A Note on Usage

This book is about the chaebol: the conglomerate corporate form typical of the largest Korean groups. Given that this term is widely used and increasingly known outside Korean studies, we have chosen to retain it. In Korean chaebol can be either singular or plural, and we have followed that usage.

All dollar sums are in US dollars.
Abbreviations

BIS  Bank for International Settlements
CSIP  Capital Structure Improvement Plan
DLP  Democratic Liberal Party
EPB  Economic Planning Board
FDI  foreign direct investment
FEB  Finance and Economic Board
FSC  Financial Supervisory Commission
GATT  General Agreement on Tariffs and Trade
GNP  Grand National Party
HCI  heavy and chemical industry
IBRD  International Bank for Reconstruction and Development
IMF  International Monetary Fund
KAMCO  Korea Asset Management Corporation
KDI  Korea Development Institute
KDIC  Korean Deposit Insurance Corporation
KFTC  Korea Fair Trade Commission
M&A  mergers and acquisitions
MCIE  Ministry of Commerce, Industry and Energy
MOF(E)  Ministry of Finance (and Economy)
MOU  memorandum of understanding
MRFTA  Monopoly Regulation and Fair Trade Act
MTIR  Ministry of Trade, Industry and Resources
NBER  National Bureau for Economic Research
NBFIs  non-bank financial institutions
NICE  National Information and Credit Evaluation Inc.
OECD  Organization for Economic Cooperation and Development
SMEs  small and medium-sized enterprises
TFP  total factor productivity
ULD  United Liberal Democrats
WTO  World Trade Organization