

The Sixth Republic and Economic Crisis, 1987-1997: excerpts from Joel R. Campbell's "Tigers, Hard Workers, and Online Gamers" from *Education About Asia* 18, no. 3 (2013) at <http://aas2.asian-studies.org/EAA/EAA-Archives/18/3/1141.pdf>

The Roh Tae-woo presidency (1988-1993) was primarily a transition from the military regime to democracy. As such, Roh's government concentrated on political reform while pursuing innovative foreign policy initiatives. Economic reforms were relatively mild and did not disrupt the overall structure of the developmental state—what foreign observers were now calling "Korea, Inc." The new government concentrated on drastically reducing authoritarianism and expanding individual and institutional freedom. Economic policy changes centered on the inclusion of social welfare concerns in economic planning for the first time, curbing the EPB's powers and liberalizing the financial industry. Responding to criticism that these reforms could hurt foreign trade, the government insisted that they were not aimed at restraining, but at promoting small and medium enterprises. The government talked about forcing the conglomerates to specialize, but beyond suggested realignments, little was done.

The merger of Roh's party with two major opposition parties in 1990 created a strong new ruling party that put former opposition leader Kim Young Sam in position to win the 1992 election. The economy continued to grow at nearly double-digit rates, exports still surged, and Korea became only the second Asian country to join the OECD. Like Roh, Kim talked about the need for reform, but his only significant change was a requirement of real names for bank accounts, promoted as an anticorruption measure. Kim failed to warn the country about the dangerous foreign debts being piled up by the conglomerates. Foreign loans soared from \$89.5 billion in 1994 to \$174.9 billion three years later. By requiring companies to reveal their long-term borrowings, companies were encouraged to borrow short-term, which raised their interest costs and created the danger of sudden liquidity shortfalls.

Various factors aided the rise of the chaebŏl but led to their downfall. The conglomerates' large size was intended to capture market synergies by cutting costs of allied companies, but there were no checks on group chairmen's expansion ambitions, and ill-considered acquisitions squandered corporate synergies. Vertical integration of subsidiaries helped save production costs but built inefficiencies and large overhead into production. Chaebŏls' use of debt financing allowed founder-families to maintain control over corporate groups, yet there was no mechanism to reduce corporate debt. Cross-ownership of shares merely reinforced mutual complacency and strengthened the families' corporate control instead of cultivating professional management that could have avoided the late 1990s crash. Government encouraged banks to continue lending to the large companies, creating a kind of moral hazard that made the financial crisis possible, and there was little government oversight of corporate investments. Also, control of nonbank financial companies prevented the financial industry from reining in such investments.

The 1990s had been a period of strong albeit uneven growth. Korea's economic fundamentals actually were fairly strong, eg, low debt, large foreign reserves, and high growth with low inflation. However, the current account deficit ballooned because a rising yen made Japanese industrial inputs more expensive. The year 1997 began ominously when Hanbo Steel declared bankruptcy after its banks turned it down for further loans. Ten more of the mighty conglomerates would fail over the next two years, most notably Kia Motor Corp. and Daewoo. The crisis in Korea was both a currency and credit problem. Initially, the Asian Financial Crisis centered on Southeast Asian economies, but as Hong Kong's stock market fell, the contagion spread to Northeast Asia. Nervous investors began to withdraw money from Korea. This put great pressure on the Korean wŏn, which the Bank of Korea futilely spent most of the nation's foreign reserves to prop up. As the government widened the trading band and the currency weakened, it was becoming increasingly difficult to pay off short-term international debts, which had mushroomed over the previous year.

On November 21, Korea's finance minister sought to arrange an informal bailout plan with Japan and the US—Korea's most important trading partners—but both countries insisted that any help had to come under the umbrella of an IMF package. Korea's request to the IMF rose from \$20 to \$50 billion. The IMF deal, agreed on December 3, gave Korea \$57 billion in loans in exchange for vast restructuring of the Korean economy and government budget cuts. Among the mandated changes were the closing or merging of failing financial companies, a more market-oriented foreign exchange system, the opening of Korean markets, and quick offloading of \$27 billion in bad loans. Amidst this panic, the Korea Development Bank failed to raise \$2 billion to service Korea's foreign debt, and the Halla Group conglomerate declared bankruptcy after defaulting on its loans. The wŏn fell to its lowest level ever, 1,891 to the dollar. US President Bill Clinton and Treasury Secretary Robert Rubin pleaded with New York banks to roll over Korea's debt, and that seemed to buy the Korean government enough time to begin enacting reforms.

Putting an exclamation point on a bad year, Korea held its third free presidential election. Kim Dae Jung, democracy advocate and dissident under Park and Chun, was widely expected to win due to the absence of a major candidate from the politically dominant Kyongsang region in the southeast. He may have hurt himself by calling for renegotiation of the IMF deal but managed a 40.3 percent plurality in a three-way race. As a populist unconnected to the government and with strong ties to the labor movement, Kim became the de facto president during the transition and, as the new president, was uniquely positioned to push through the most sweeping political economy reforms since the 1960s. The reforms covered corporate governance, financial market regulation, foreign investment in Korea, regulatory reform, corruption control, and privatization of state-run entities. With his

death in 2009, the OECD asserted that Kim should be remembered not just as a democratic crusader but as a leader who saved Korea from economic disaster.

The government's reform mandate involved three components: restructuring businesses (in many cases by combining units from separate conglomerates), reworking corporate finances to return companies to profitability, and improving corporate governance to bring stability and accountability to corporate operations. Business restructuring was not generally successful, as it did not produce high-performing companies, but efforts to improve corporate finances did bear fruit. By 2000, companies had significantly cut debt-equity ratios and reduced cross-company debt guarantees...