UNIVERSITY of SAN FRANCISCO

An annual publication of the **University of San Francisco Center for the Pacific Rim**

Asia Pacific: Perspectives
Center for the Pacific Rim
2130 Fulton St, LM202
San Francisco, CA
94117-1080

Tel: (415) 422-6357
Fax: (415) 422-5933
perspectives@usfca.edu

Asia Pacific: PERSPECTIVES

an electronic journal

Volume III · Number 1 May · 2003

CONTENTS

Asia Pacific: Perspectives is a peer-reviewed journal published once a year in May. It welcomes submissions from all fields of the social sciences and the humanities with relevance to the Asia Pacific region.* In keeping with the Jesuit traditions of the University of San Francisco, *Asia Pacific: Perspectives* commits itself to the highest standards of learning and scholarship.

Our task is to inform public opinion by a broad hospitality to divergent views and ideas that promote cross-cultural understanding, tolerance, and the dissemination of knowledge unreservedly. Papers adopting a comparative, interdisciplinary approach will be especially welcome. **Graduate students are strongly encouraged to submit their work for consideration**.

* 'Asia Pacific region' as used here includes East Asia, Southeast Asia, South Asia, Oceania, and the Russian Far East.

Persistence of Interlocking Institutions: Big Business Policy Under the Kim Dae Jung Government

by Jiho Jang, Ph.D.

Abstract
Based on historical institutionalism, this study argues that there is continuity in institutions, emphasizing the constraints created by existing structures and institutions. This study assesses the Republic of Korea as a case study analyzing big business policy under the Kim Dae Jung government. The result found in this study is that there is no rapid disappearance of institutional pattern of state activism in Korea. This study examining four institutions: 1) state-led ideology; 2) centralized and personalized power of the president; 3) bureaucratic system as a function of policy implementation; and 4) the state-advised financial sector. This study demonstrates that whereas formal institutions collapse or are dismantled, informal institutions such as operating procedures persist to shape the behavior of political actors. Institutional structure is so integrated that it cannot be easily divided into separate parts for the new regime in order to produce different or 'efficient' solutions to industrial restructuring.

Introduction

There is a significant variation in the policies adopted by various governments even during the neoliberal era. As an example of a country in which neoliberal policies have been significantly limited, this study treats South Korea (hereafter referred to as Korea) as a case study encompassing approximately three decades of state activism vis-à-vis corporations. Since the 1980s, the Korean state has adopted several deregulation policies in which the state attempted to "globalize" its economic structure. The rhetoric of bureaucrats and political actors has made them sound like free-market liberalizers. Moreover, the collapse of the economy and the apparent inability to regain economic momentum in 1997 strained the Korean government's role in economic processes, perhaps to its limits. However, state activism vis-à-vis big businesses (hereafter the chaebol) in Korea has been persistent. Actors in the Korean state apparatus, government policies and regulations, and politics generally have attempted to play a role in what, when, and how firms emerged and developed.

Contrary to conventional wisdom in which globalization invites or forces countries to converge on a universally superior pattern of organization and economic behaviors, this paper emphasizes the constraints created by existing structures and institutions. This analysis is based on a number of considerations: 1) the interlocking nature of institutions and thus difficulty of transforming them; 2) the persistence of attitudes, values, and practices that sustain and put those institutions in place; and 3) the way in which institutions reinforce the values, attitudes, and practices that created them in the first place.

Theoretical Considerations

A growing body of literature in the discipline of social science, in the name of new institutionalism, has conceptualized the relationship between institutions and individual behaviors. Individuals have mixed motives and thus existing institutions constrain their behavior and point them in certain directions in ways a rational choice assumption cannot capture. Historical institutionalism directs analysis to explore the manner in which the legacy of a former system is likely to shape any process of policy formation in certain directions, while militating against change in others. The value of historical institutionalism is that it explains persistence of policy patterns from continuity in institutions and places an emphasis on the constraints by existing structures and institutions.

Because institutional contexts vary from one country to another, they are embedded in their broader societies. Therefore each state differs in its responses to common challenges. Rather than focusing on an 'efficiency' assumption, historical institutionalists emphasize the character of interlocking institutions. Changes in one area that leave the other components of these national systems untouched do not bring about convergence. Even countries wishing to adopt the business practice presumed to be most efficient or effective can incorporate only those that are "consistent with the prevailing institutional logic" (Biggart and Guillen 1999, 726).

Moreover, historical institutionalists regard institutions as the legacy of a concrete historical process. They emphasize that previous choices have a strong influence over the subsequent behavior in that later decisions cannot reverse the previous ones. In other words, prior institutional choices condition future options and institutional capacities are a product of choices made during some earlier period. Once established, patterns of politics and institutional rules would often produce self-reinforcing dynamics.

Empirical Considerations

The 1997 financial crisis hit Korea, the eleventh largest economy in the world. In response to the crisis the IMF organized a rescue package of $57 billion, the largest in the history of the Fund. When the IMF provided a substantial rescue package for the crisis, state activism in Korea was condemned heavily as one of the culprits of the financial crisis because of its heavy-handed intervention in the market and its collusive ties with the private sector (KDI 1998). To receive the IMF reform packages, across-the-board structural changes were required including comprehensive dismantling of the old financial system, setting the stage for corporate restructuring, improving corporate liberalization and reforming labor market (IMF 1998 *World Economic Outlook*, May and October).

Based on these bailout programs, the Kim Dae Jung government, upon its inauguration in 1998, disclosed an extensive economic reform program. The Kim government accelerated capital market liberalization: introduction of a free floating exchange rate, abolishment of interest ceilings, easing restriction on long-term foreign borrowing, allowing foreign banks and security firms to establish local subsidiaries, and permitting foreign banks to merge with or acquire Korean financial institutions (Ministry of Finance and Economy 1999). Under the situation of severe international pressures, the main question is whether the implementation of reform plans under the Kim government (following earlier liberalization moves) would erode state activism in Korea and its traditional relations with big businesses. The conventional wisdom among skeptics of the state's economic role was to suggest that the crisis signaled the end of state activism in Korea. The crisis, mediated by the IMF agreement, is expected to alter directions of the state's economic policy in Korea. According to Moon (2000), the Korean experience lends powerful support to the convergence thesis, in which the crisis pushed Korea closer to the American form of free market. He argues that global standards, which are set by Western ideas, values, and norms, have dominated in discourses on crisis management, resulting in the "triumph of Anglo-American capitalism" and putting an epitaph to the Asian value and Korean capitalism (Moon and Rhyu 2000, 97).

Nonetheless, this study does not agree with the rapid disappearance of national diversity. Contrary to the globalization /convergence thesis, this study finds a significant variation in the state's role vis-à-vis the private sector, i.e. the extent to which the state is involved in the businesses of private firms. Understanding the different mechanisms for sustaining institutional persistence is the key to understanding why common international trends frequently have such different domestic consequences. Employing a 'historical analysis,' this study traces patterns of various policy measures of Korean government towards the chaebol and examines the continuity of interlocking institutions.

Conceptual Considerations: Four Institutional Constraints

Does the Korean state maintain its involvement in private corporations in spite of international pressures and political transitions? In order to examine empirical facet of this question, this study utilizes the concept of institutions. According to historical institutionalists, institutions are defined either as the (formal) products of constitutions, laws, etc., or as the (informal) result of values that are more diverse in origin, springing from historical practice and repeated interaction among actors who produce stable expectations over time. Similarly, in this study, institutions encompass state structures such as executive / bureaucratic branches, sets of formal rules such as those pertaining to the financial system, time-sanctioned standard operating procedures, and norms that are a product of custom and precedent.

This study examines four institutions: 1) state-led ideological orientation; 2) personalized presidency; 3) centralized bureaucracy; 4) financial control. The list is neither exhaustive nor mutually exclusive; instead, these four aspects constitute a useful framework for analysis.

State-led Ideological Orientation

Ideology for the state includes perceptions, models, and values of how the state shapes and understands its economy and political situation. The role of ideology is considered as an important factor in determining the nature of policy, in that ideology constrains the limits of acceptable action of the state. Particularly, the ideology tends to provide a set of ready solutions for policy problems. The first institutional feature of state activism in Korea is state-led ideological orientation: the belief that the state should play a purposeful role in industrial structuring. While Koreans have heard a lot of propaganda supporting deregulations of private sector, the state's ideological orientation of control over industrial structure remains essentially intact. The sense of duty and resolve of executives and economic bureaucrats determined to steer the nation's economy in the right direction remain as strong as ever.

When the economy was in trouble, regimes in Korea have often attempted to solve problems by relying on the state-led ideology of selective support or pressure for specific industries. At several points in the past, attempts have been made to force companies onto a new path. In the 1980s and 1990s, in the name of structural readjustment and industrial specialization, private big businesses were forced to give up particular subsidiaries and to choose main business areas. Table 1 shows that diverse types of industrial rationalization had been carried out under the coordination of the Korean government: company rationalization and industrial rationalization under the Park government of the 1970s; heavy industry adjustment program under the Chun government of the early 1980s; and core business specialization under the Roh and Kim Young Sam government of the 1990s. The state's industrial coordination programs are regular, resurfacing repeatedly as subject for state activism toward the chaebol. In the process of forcefully implementing industrial adjustment, cooperative companies have been compensated with preferential treatment such as privileged loans and tax exemptions.

Table 1. ***Major Cases of State-led Industrial Coordination***

Case	Content
Company Rationalization (1969-1971)	112 insolvent firms in the PVC, automobile, steel, chemical and textile industries were liquidated or acquired by other chaebols
Industrial Rationalization (1972)	61 firms, including 30 in heavy industries, 8 in chemical industries, and 10 in light industries, undertook capacity adjustment, business specialization, subcontract system improvement, and M&As through state financial and tax support
Investment Readjustment of Heavy Industries (late 1970s-early 1980s)	The electricity generating, heavy construction equipment, automobile, and diesel engine industries were restructured by state-led M&As with bail-out financing and interest rate subsidies
Business Specialization (1990s)	Indirect inducement policy aimed at specializing two or three main core industries of the big 30 chaebols through easing bank credit limits and other preferential treatments

Source: J.W. Lee (1999, 254) and Jwa and Seo (2000, 330)

Kim Dae Jung's government also implemented the Big Deals program, which was based on familiar state-led ideology. The Big Deals program involves massive mergers and swaps of companies and business lines among the five largest chaebols including Hyundai, Samsung, Daewoo, LG and SK. Considering over-diversified business areas and excess productivity capacities as the major problem in the low profitability of the chaebol and in the less competitiveness of the nation's economy, the Kim government forced the five largest chaebols to focus on a few specialized businesses through mergers of their subsidiaries.

Table 2. ***Progress in the Bid Deals, as of the end of December 2000***

Type of industry	Targeted firms	Details	Status
Aerospace	Samsung Aerospace Industries, Daewoo Heavy Industries, Hyundai Space & Aircraft	Establishment of Korea Aerospace Industries through the merger among three companies	Completed- Delay of foreign capital attraction and difficulty in raising working capital
Automobile	Samsung Motors, Daewoo Motor	Daewoo Motor takes over Samsung Motors	Aborted- After the Daewoo bankrupt, Samsung Motors sold to a foreign auto-maker
Oil-refining	Hyundai Oilbank, Hanhwa Energy	Hyundai Oilbank takes over Hanhwa Energy's oil-refining business	Completed- Foreign capital attraction in the form of equity participation in progress
Petrochemical	Samsung General Chemical, Hyundai Petrochemical	Foreign investment in progress for the company by the merger between Samsung and Hyundai	Aborted- Failure of the merger deal due to the hesitation of the Mitsui concerning equity participation in the merged company
Power plant	Korea Heavy Industries, Samsung Heavy Industries, Hyundai Heavy Industries	Assets of Samsung Heavy Industries and Hyundai Heavy Industries transferred to Korea Heavy Industries	Completed
Railway vehicle	Hyundai Precision, Daewoo Heavy Industries, Hanjin Heavy Industries	Hyundai, Daewoo, and Hanjin invested on a 4:4:2 basis establishing the Korea Railway Vehicle Co.	Completed- Failure of additional investment by partners and delay of a debt reduction plan
Semiconductor	Hyundai Electronics, LG Semiconductors	Merger between Hyundai Electronics and LG Semiconductors	Completed- Hyundai takes over LG Semiconductors, but suffers from the low profitability
Ship engine	Korea Heavy Industries, Samsung Heavy Industries	Korea Heavy Industries takes over Samsung Heavy Industries' ship engines business	Completed- Privatization of Korea Heavy Industries earmarked

Source: SERI (2000), Chosun Ilbo (September 18, 2002)

On July 1998, there was an agreement on the Big Deals among the top five chaebols at a meeting between president and the chaebol's leaders (Y.R. Lee 1999, 91-97). Immediately after the meeting, the Federation of Korean Industries, an association of the chaebol, announced a sweeping business swap plan among 17 companies belonging to the 5 largest chaebols in the seven industrial sectors of aerospace, oil refining, petrochemicals, power plant equipment, railway vehicles, semiconductors, and ship engines. However, the Big Deals did not go forward due to disputes among those chaebols that were reluctant to give up their business or were not satisfied about the selling price of their business. On December 1998, again, an agreement between government and the top five chaebols was made for a speedier implementation plan for the Big Deals (Y.R. Lee 1999, 219-234). The final decision was composed of 16 companies belonging to the top five chaebols, excluding SK, and three non-top five chaebol companies, Korea Heavy Industries, Hanhwa Energy, and Hanjin Heavy Industries. The revenue size of those targeted companies under the Big Deals was 7.4 percent of the national GDP in 1998 (*Joongang Ilbo* February 20, 1999). Table 2 lists the major Big Deals proposed and the results to date.

The Kim government officially announced that the Big Deals in the private sector should be implemented based on market rules and mutual agreements between involved companies. For example, when he met the U.S. Trade Representative, the chairman of the Financial Supervisory Commission (FSC), Chun Yun Chul, said that "Big Deals in Korea have been done under market principles and government had not intervened in the process" (*Korea Economic Daily*, October 15, 1998). However, government exerted a strong influence toward the Big Deal since its early stage. For example, the Minister of Industry and Resources, Park Tae Young, determined that the semiconductor industry was an over-invested sector, which needed to be restructured (*Chosun Ilbo*, November 12, 1998). Rather than leaving the discipline of market mechanism, government identified a number of target industries.

Such a deep-rooted state-led ideology has two manifestations in Korea. First, the chaebol have only limited popular support. The average Korean citizen believes that the chaebol are too big and a source of corruption (Cho 1997, 217-224). Additionally, they believe that the chaebol are responsible for bringing on the current crisis. A 1999 Korean Gallup survey commissioned by *Monthly Joongang* (February 1999) revealed that 45.3 percent of the public approved the direct use of state intervention in the restructuring the chaebol while only 28.8 percent agreed with market-based reform and 22.4 percent with indirect control via financial institutions. Furthermore, the chaebol's owners and their family members tend to be ostracized by society, which takes it for granted that the state would intervene in the personal affairs of chaebol families, admonishing them for their extravagant life-style and mediating in conflicts between family members over the issue of inheritance. This kind of public attitude highly pressures the state directly intervening not only in the business but also corporate structure.

Next, the economic provisions of the Korean Constitution grant government virtually unlimited authority and control, to such an extent that all economic policies pursued by the state can be legally justified (*Weekly Donga* December 9, 1999). With the exception of Section 1 of Article 119, Articles 119 to 127 provide government with the power to guide and control the economy for specific national purposes. Particularly, Section 2 of Article 119 indicates "government may regulate and coordinate economic affairs for the balanced growth and stabilization of national economy, maintenance of fair distribution of income, prevention of market domination and abuse of economic power, and the democratization of economy through the coordination between economic bodies" (Yang 1994, p.962). Despite nine constitutional amendments, the underlying nature of the Korean Constitution in terms of advocating control of the economy has changed little since 1945. The nationalization of banks, preferential treatment through financial support and taxation, licensing and granting approval for market entry are all authorized and justified under the Constitution. The example of the Big Deals policy shows that Kim Dae Jung's government was also trapped with ideology of state-led industrial coordination, resulting from general public attitude and the Constitution. In the Big Deals, the government guided and forced swaps among the chaebol, determining the acquiring and acquired companies in advance and giving them the guidelines and deadlines to be met. Despite all the liberalization and deregulation slogans, the Korean state has not replaced its ideological orientation of state-led industrial structuring with a non-interventionist based on unfettered market force. The government retains the ideological manifestation in that over-competition can lead an economic harm.

Personalized Presidency

The next institutional constraint is the basic organization of the state—the executive branch. Impact of the nature and structure of political system (including the administrative division of responsibility government) on socioeconomic policies has been explored by a variety of scholars. Ideas or ideologies do not acquire political force independently of the constellation of formal institutions. The Korean political system is characterized by a highly personalized presidency.

The executive branch (and ultimately the president) exercises the most power in Korea. Policy arrangements are often recognized as being personality-driven in that the president determines the direction, priority, and objectives of economic or social policies by relying only on an inner circle of advisors around the presidential office (called the Blue House) who assist the president in planning and executing policy strategies. At the same time, government often uses autocratic force to impose its decisions. Presidents have been able to mobilize the power apparatus, such as the National Intelligence Service (NIS, previously the Agency for National Security Planning), the Attorney General (AG), the Chief of Police Bureau (CPB), and the Office of National Tax Administration (ONTA) at their discretion, to deal with his political opponents and to force through their economic agenda. Although the economic transformation and democratic transition since the late 1980s largely undermined presidential power by setting institutional constraints on the president and bringing the presidential office under democratic rules, the president himself has remained the single most important institution. Particularly, major policies around the chaebol still remain in the hands of the president. For instance, certain chaebols have been politically punished. Kukje, one of the 10 largest chaebols at that time, was destroyed in 1986, allegedly, for not supporting the president. Hyundai was punished in 1993 with freezes on financing when its founder ran for presidency. SK and Samsung were punished in a similar way for remarks made by their owner-chairmen.

In addition, Kim Dae Jung's government prefers informal arrangements in which the rule of law is compromised even if its measures are not legally biding. For examples, after the series of aircraft accidents of the Korean Air Line (KAL), the President Kim stated that the KAL, the subsidiary of Hanjin, should be managed by professional staff, not as a family run business and concentrate on providing an efficient and safe service for its customers (*Chosun Ilbo*, April 21, 1999). Some critics argue that the President's calling for a management reshuffling at KAL was inappropriate intervention in private business, overstepping the bounds of his authority, and that there is no relationship between ownership structure and 'an efficient and safe service.' However, President Kim's order was faithfully executed after the ONTA announced the imposition of 541.6 billion won penalty against subsidiaries of Hanjin, including KAL, and their management for evading taxes and amassing a number of secret slush funds (*Chosun Ilbo*, October 4, 1999). The owner-chairman of Hanjin, Cho Jung Hoon, resigned and the family management of KAL's daily operations ended.

Another example is Blue House talks between the President and the chaebol's owner-chairmen, which are often used to lay out reform programs with businesses at each phase and to verify progress on these programs. The President often used his supreme power at these meetings to dissolve deadlocks among the chaebol, banks and the government. The first meeting, in January 1998, laid out the five reform targets concerning the chaebol. The meeting in August 1998 put pressure on the foot-dragging chaebol. The meeting in December 1998 was used to settle the big deals among the five largest chaebols. The meeting in April 1999 was used to determine whether or not the reform agreements of state-business were proceeding as planned. The meeting in August 1999 was used to reach the contractual agreement of three new reform targets. The sequence of the Blue House meetings clearly shows that informal administrative guidance and the personalized presidential system in Korea.

Although there is no question that the Kim Dae Jung government is democratic, President Kim has maintained a commanding position in the process of chaebol policy implementation. Accordingly, some criticize the policy style of President Kim Dae Jung. In spite of democratization since the late 1980s, politics in Korea is still characterized by the personality-dominated system that articulates the interest of its top leader.

Centralized Bureaucracy

The bureaucratic system has played a powerful role in policy implementation organization. Career bureaucrats are not in a position to make strategic choices since they occupy a constitutionally subordinate position and lack the legitimacy of elective office holders. Even the bureaucracy, identified as a strong institutional presence by political analysts, has been structurally dependent on presidential prerogative while being vulnerable to presidential caprice (Chung 1989). Yet, the bureaucrats in Korea enjoy certain assets that allow them to influence economic policy. For one, they are often the source for technical information or information requiring a degree of expertise in a subject. Thus, the presidency cannot implement policy measures without the existence of an organizational capacity in the bureaucracy that not only commands a wide range of incentives through extensive control over production resources, but also possesses substantial information resources. As a regulating institution, the bureaucratic system remains intact both in terms of size and function. The only change in recent years is that the balance of power among the various ministries and officers has shifted slightly. The Economic and Planning Board (EPB, merged into the Ministry of Finance and Economy, MOFE), the Fair Trade Commission (FTC), the Office of Bank Supervision, and the Financial Supervisory Commission (FSC) are some ministries which exhibit the organizational capacity of the state vis-à-vis the chaebol. The existence of a stable and cohesive bureaucratic organization allows the executive branch to discipline the private business sector by taking advantage of a wide variety of policy tools such as credit, tax, regulation, and administrative guidance.

In particular, the Kim Dae Jung government empowered the FTC with new institutional provisions such as the right to look into bank accounts of the chaebol and the right to look into the internal financial transactions among a chaebol's member firms to take heavy punitive measures in the case of infringement. Thus the FTC launched investigation three times into illegal internal transactions among the five largest chaebols and imposed a total 100 billion won in surcharges (*Joongang Ilbo* August 12, 1999). The FTC is also charged with monitoring the swaps to prevent delays in restructuring. The chaebol consider as the serious pressure, statements made by high-ranking officials of FTC or FSC in which they said that government would take a knife to the chaebol, and administrative sudden decisions to investigate subsidiaries' internal dealings (*Chosun Ilbo*, 1998, May 8).

Financial Control

The final institutional feature is government-advised financial control. Whereas financial institutions are subject to a variety of regulations, not only in Korea, but also in most other countries, direct regulations such as the credit controls for financing specific industries and firms that prevailed in Korea in the 1970s are not a common practice in other countries (Amsden 1989, Fields 1995). Indeed, "government control of the banks is …the single most important economic factor explaining the distinctly subordinate position of the private sector" in Korea (Jones and Sakong 1980, 122). But, when commercial banks were privatized in the 1980s, the state acting as a financier seemed no longer possible. Moreover, the chaebol's increased investment in such non-banking financial institutions as insurance companies provided the capital that enabled the chaebol to become more financially independent from the state.

However, the financial system remains credit-based and subject to government-advisement. Liberalizing the financial sector was further complicated by the fact that the banking system had not adequately dealt with the losses it had suffered during the earlier periods of more pervasive state-directed lending. Despite their newly 'privatized' status in the 1990s, commercial banks had only limited discretion over lending policy. They could not survive without financial support from the central bank, the Bank of Korea, which is still controlled by government. Moreover, during the financial crisis of 1997, the government not only increased regulatory power over financial institutions but also gained influence as shareholders of the financial institutions that were bailed out with public funds. Kim Dae Jung's government used its control of banks to force the chaebol to improve their financial structure and streamline their business activities.

To improve the chaebol's financial structure, the Kim government recommended that a financial institution sign an agreement with its partner chaebol. The informal recommendation eventually developed into formal agreements, which were made between main creditor banks and 57 subsidiaries of the chaebol owing more than 250 billion won for capital structure restructuring. The main context of the agreement was the reduction of the chaebol's debt-to-equity ratio to 200 percent by the end of 1999, their business restructuring, and a clause for banks' overseeing of chaebol's new investment. Officially, the agreement between banks and the chaebol was voluntary, but it left no doubt that the state was deeply involved. The state set a deadline, namely the end of 1999, for the chaebol to lower their debt-to-equity ratios to below 200 percent, which applied to all chaebols without exception. To induce the chaebol to reduce outstanding debt, creditor banks directed them to either sell some of their member companies and assets or to attract foreign investment. In case of failure, the government and banks warned the chaebol that they would be punished with the withdrawals of existing loans or the refusal by their main banks to provide new loans. For example, President Kim himself directly threatened the chaebol that creditor banks would not stand by if the chaebol did not abide by the agreements; failure to do so would result in punitive action on the part of the banks (Chosun Ilbo December 14, 1998).

As main creditors, banks backed by government now have enormous power over the chaebol. They can virtually bankrupt firms by cutting off their creditors. We can see an explicit example in the case of Daewoo's collapse, which was dissolved into 12 major firms under the workout program in 1999 (Kawai 2000). On the other hand, although innumerable points of conflict occurred between the state and the chaebol, the government never allowed a complete breakdown of the big business structure. The Kim government followed a pragmatic approach toward any particular industry and chaebol, considering them as the backbone of the nation's economy. Current preferential loans for Hyundai are a good example of state support for a preferred chaebol.

While government officials have repeatedly stressed their willingness to allow creditor banks to determine the fate of terminally ailing companies by market principle, government-advised banks have continually extended preferential loans to keep Hyundai's subsidiaries afloat (*Chosun Ilbo* March 21, 2001, *Korea Herald* November 28, 2001). The government seemed to fear that Hyundai was simply too big to fail and its collapse could touch off a chain-reaction of economic havoc. The Ministry of Finance and Economy highlighted that "there would be no more bankruptcies of the chaebol like Daewoo's fall in 1999" and "the liquidity crunch of Hyundai was not serious" (*Chosun Ilbo* July 23, 2000). Another official of the Blue House said, "Hyundai is different from Daewoo. Its semiconductors and construction are Korea's backbone industries. These firms hold large market shares of their industries and these businesses are deeply linked with other domestic companies. Thus, these firms should not be sold off just to follow market principles" (*Joongang Ilbo* January 16, 2001). However, several editorials of various newspapers compared the government's repeated financial support to Hyundai to 'pouring water into a bottomless jar' (*Chosun Ilbo* March 11, 2001, *Hankuk Ilbo* March 12, 2001, and *Joongang Ilbo* March 12, 2001).

Furthermore, as the largest shareholder in many banks, the state participated in the personal decisions made by banks' top executives (Heo and Kim 2000, p.501). In a *New York Times* interview (November 10, 2001), Wilfred Horie, who is the first foreign national to run one of the largest commercial banks in Korea (the Korea First Bank), remarked that "the Korean governing establishment had indirectly influenced government-owned banks to extend loans to failing companies… There was quite a lot of pressure. There is probably indirect pressure." When a high-ranking official calls the bank's president several times requesting the resume of a particular person, the bank's president is actually being signaled to promote the person in question (*Shin Donga*, July 1999). This indirect pressure becomes more direct when government installs ex-bureaucrats in key executive positions of financial institutions. Kim Dae Jung regime consolidated the financial sectors in terms of "parachute appointments" or the career movement of ex-bureaucrats to high positions in various financial sectors upon retirement from the central bureaucracy. Between 2000 and May 2001, out of a total of 27 officials who retired from the MOFE, the FSC, and the FSS, 18 officials landed new jobs in financial institutions, such as banks, insurance companies, and brokerages (*Chosun Ilbo* June 25, 2001). For instance, Kim Sang-hoon, former assistant deputy chairman of the FSC, became president of Kukmin Bank in March 2001 (*Donga Ilbo* March 9, 2001).

In the wake of scandals involving officials of the financial watchdog agency, the state amended The Public Servants Ethics Law in May 31, 2001 in order to ban the practice of "parachute appointments." According to the revision, retired, high-ranking officials of the FSC and the FSS are prohibited from being re-employed in financial institutions for two years following the retirement (*Weekly Chosun* April 26, 2001). However, a top official in the FSS interviewed by the Korea Herald, said "it is still considered as 'heartless and disrespectful' to let go of 'honorable' top officials without securing them new jobs" (*Korea Herald* June 27, 2001). Even after the revision of the law, ex-bureaucrats became full-time inspection commissioners of 14 commercial banks, 12 securities companies, the Korea Securities Finance Corporation, and other specialized banks such as the Industrial Bank of Korea, and the Export and Import Bank of Korea (*Chosun Ilbo* July 29, 2001, November 9, 2001, February 11, 2002, and *Donga Ilbo* June 3, 2000). Finally, directors of commercial banks are not accustomed to autonomous decision-making on important issues and tend to rely on state officials (*Joongang Ilbo* February 29, 2000, and *Korea Herald* February 11, 2001). They often seek government intervention and ask the government to control the process of economic liberalization. Consequently, 20 years after their privatization, banks, in many respects, still function like state-owned institutions.

Conclusion

Institutions, once formed, are hard to change and tend to endure. Institutional change is "sticky" and episodic rather than continuous and incremental since the costs of uncertainty act as a countervailing force against institutional change. Institutions shape politics by conditioning preferences and options available to political actors and are considered to be a dominant factor in encouraging political and economic transition along a unique path. Viewed in these theoretical terms, state activism developed in Korea as a specific institutional design to control and guide the private business sector. Even when faced with the current trend towards globalization, the state activism (already traveling a path that provides positive returns in terms of economic growth in Korea) continues to rely on historically-developed institutions. At each point along the path of a nation's development, whether it be rebuilding after a war, or maintaining economic and social stability during external crisis, state activism generates a powerful cycle of self-reinforcing activity where continuing on a particular institutional path is more attractive than deviating from it.

This study argues that formal and informal institutional characteristics of the Korean state, such as state-led ideology, the centralized presidency, the consolidated bureaucratic system, and the state-advised financial sector, are interlocked. Such interlocking features are embedded in history, social, economic and political situations and, thus, cannot easily be detached from one another. During restructuring processes under the crisis era, the Kim Dae Jung regime desired to select only what was desirable from past practices and institutions. Nevertheless, parts of the institutional structure are so integrated that they cannot be easily divided into separate parts for the new regime in order to form efficient solutions to the economic crisis.

Under the Kim government, corporations' restructuring processes still have depended upon the government. With an ideology based on state-led industrialization, President Kim Dae Jung has negotiated directly with the chaebol over the restructuring plans, and the bureaucratic system such as FSC, FTC, and MOFE has pushed corporate governance reforms or debt restructuring through the control of financial institutions. When implementing chaebol reforms, the Kim government has often used informal administrative guidance with an implicit threat of sanctions.

This study argues that institutions are the key to understanding how and why state activism persists. The legacy of the developmental state has created regulatory administrative systems that do not bode well for the creation of Anglo-American market economies as opposed to the Franco-German models on the European continent. This study provides an analytic lens, which can be applied to other developing countries, which have been experiencing similar economic restructuring. Like many other countries of Asia, Korea has experienced political and economic changes. What role do domestic factors play in this process? If the determining factor in industrial reforms is domestic in nature even in such a small country as Korea, then domestic factors will most likely be the deciding consideration when other countries attempt to transform their economies. Moreover, this study helps in understanding similar interventionist tendencies elsewhere. These states, like Korea, profess a commitment to the free market, yet state involvement in the economy continues.

REFERENCES

Amsden, Alice H. 1989. *Asia's Next Giant: South Korea and Late Industrialization*. New York: Oxford University Press.

Biggart, Nicole Woolsey, and Mauro F. Guillen 1999. "Developing Difference: Social Organization and the Rise of the Auto Industries of South Korea, Taiwan, Spain, and Argentina," *American Sociological Review*, vol. 64, no.4, pp. 722-747.

Chung, Chun-Kil. 1989. "Presidential Decision Making and Bureaucratic Expertise in Korea," *Governance*, vol. 2, no. 3, pp. 22-49.

Fields, Karl J. 1995. *Enterprise and the State in Korean and Taiwan*. Ithaca: Cornell University Press.

Jwa, Sung-Hee, and Seo Jung-Hwan. 2000. "Industrial Policies in Korea: Evaluation and Redirection Based on New Asian Values," *Korea Journal*, vol. 40, no. 2, pp. 322- 364.

Korea Development Institute (KDI). 1998. *A Comprehensive Plan for Restructuring the Korean Economy and Overcoming in Crisis*. Seoul: KDI.

Lee, Young Ryul. 1999. *Big Deal Game: DJ vs. Chaebol*. Seoul: Joongang Ilbosa.

Ministry of Finance and Economy (MOFE). 1998. *Challenge and Chance: Korea's Response to the New Economic Reality*. Seoul: MOFE.

Moon, Chung-In. 2000. "In the Shadow of Broken Cheers: The Dynamics of Globalization in South Korea," In *Coping with Globalization*, ed. Prakash, Assem, and Jeffrey A. Hart. New York: Routledge.

Moon, Chung-In, and Sang-young Rhyu. 1999. "The State, Structural Rigidity, and the End of Asian Capitalism," In *Politics and Markets in the Wake of the Asian Crisis*, ed. Richard Robinson, Mark Beeson, Kanishka Jayasuriya, and Hyuk-Rae Kim. London: Routledge.

Samsung Economic Research Institute (SERI). 2000. *Two Years after the IMF Bailout: A Review of the Korean Economy's Transformation*. Seoul: SERI.

Woo, Jung-Eun. 1991. *Race to the Swift: State and Finance in Korean Industrialization*. New York: Columbia University Press.

Yang, Sung Chul. 1994. *The North and South Korean Political Systems: A Comparative Analysis*. Boulder: Westview Press.

Jiho Jang received his Ph. D. in Political Science from the University of Missouri - Columbia. He now teaches 'Government and Business' and 'Civil Society' at The Catholic University of Korea. His main research areas are institutions and policymaking, Government and Business, Industrial Policy and Civil Society.