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The South Korean Financial Crisis:

Debt-Leveraged Development, Liberalization, and a Loss of Sovereignty

by

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A thesis submitted to the Faculty of Graduate Studies and Research in partial fulfillment

of the requirements for the degree of Master of Arts

in

East Asian Interdisciplinary Studies

Department of East Asian Studies

Edmonton, Alberta

Fall 2000

0-612-59729-6

University of Alberta

Library Release Form

Name of Author: Jin Hwan Kim

Title of Thesis: the South Korean Financial Crisis: Debt-Leveraged Development, Liberalization, and a Loss of Sovereignty

Degree: Master of Arts

Year this Degree Granted: 2000

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October 2, 2000

Abstract

This research is motivated by the question why the South Korean financial crisis occurred in 1997. While recent US policy change toward South Korea turned out to be a critical aspect of the crisis, there existed long standing features of South Korean development that prepared the road to the crisis, e.g., the debt-dependent, Chaebol-centered, and worker-sacrificing strategy. The purpose of this thesis is first to examine what caused the South Korean financial crisis, secondly to attempt critical examination of the historical characteristics of South Korea development experience, and thirdly to seek the best way for the average Korean person to live a quality life. Also, this research will detect what kinds of social problems have arisen as a result of the financial crisis. The research historically examined those aspects of the crisis caused by US policy change, using an interdisciplinary approach that incorporates studies in history, sociology, international relations, political science, and economics.

University of Alberta

Faculty of Graduate Studies and Research

The undersigned certify that they have read, and recommend to the Faculty of Graduate Studies and Research for acceptance, a thesis entitled South Korean Financial Crisis: Debt-Leveraged Development, Liberalization, and a Loss of Sovereignty submitted by Jin Hwan Kim in partial fulfillment of the requirements for the degree of Master of Arts in East Asian Interdisciplinary Studies.

Satoshi Ikeda, Ph.D.

Susanne Soederberg, Ph.D.

Gord Laxer, Ph.D.

September 29, 2000

To my wife Jeonga,

my parents-in-law,

and my parents in heaven

Acknowledgement

I am indebted to the many people who helped me conduct this research successfully and kept me studying at the University of Alberta. I was blessed to have Satoshi as my supervisor; he gave me insightful comments, scholastic suggestions, and most of all courage. I cannot forget all of his efforts toward my work. I would like to express my gratitude towards my colleagues in East Asian Studies. Without the support of my family, I could not have pursued this second MA. Finally, I would like to thank all of the people who helped my wife and me during our wonderful stay in Edmonton.

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I. Introduction

The South Korean economy was irrefutably the most successful model of state-led economic development. This 11th largest in the world, however, had collapsed following the South Korean financial crisis in late 1997[1]. Since the crisis, South Koreans have suffered from economic and social hardships such as declining living standards, a sharp increase in unemployment and suicide, deepening wealth polarization, and so forth. According to Watts (1998), suicide had increased by 35 percent since late 1997 till the fall of 1998. In other words, 36 people killed themselves every day in the year following the financial crisis. Suspected causes of suicide include the loss of jobs, financial difficulties, and economic difficulties in everyday lives.

In addition, insolvent banks, financial institutions, and big businesses have been sold to foreign, mostly US, investors. Big businesses have been the vehicle and symbol of South Korean economic development since former president Park Jung Hee launched economic development in 1962. South Koreans worked very hard for these companies, believing that they were the means to transcend the vicious circle of poverty that had prevailed among ordinary people since the end of the Korean War. Eventually the Korean economy grew large enough not only to live without foreign aid but also to join the Organization for Economic Cooperation and Development (OECD) in 1996. Therefore, South Koreans feel as if a part of their own bodies is being taken away when those companies are taken over by foreign investors and global companies. At the same

[1] People call the 1997 crisis a financial crisis or an economic crisis. If the crisis was caused by the real economy, it would be proper to call it an economic crisis. However, the 1997 South Korean crisis occurred mainly owing to financial problems (Chang, 1997). That is why the crisis will be hereafter called the "financial crisis" rather than the "economic crisis."

time, this business-purchasing trend by foreign investors, which has sharply accelerated since the financial crisis, alarms South Koreans and signals that state-led economic development, the model that brought remarkable economic growth, is over.

The crisis brought a lot of changes in the average person's lifestyle. Koreans have to work very hard day and night to pay off debts in order to regain their sovereignty over economic matters. Some of them developed mental and physical illnesses due to job stress and depression mainly caused by the financial crisis and its aftermath. On the other hand, Americanization has deepened especially among teenagers and the rich. Teenagers tend to copy American fashion and like to eat Western food more than Korean food. They simply want to follow American trends without thinking because they are exposed to American culture through Hollywood movies, television dramas, and various forms of business presence. When people walk along any busy street in Seoul, they can easily see commercial signs that are written in English, as well as have something to eat at fast food restaurants such as Burger King, McDonald's, KFC, Starbucks, etc. The more the financial crisis brings liberalization, deregulation, and globalization, the more people lose their Korean identity and become Americanized.

When the crisis occurred, the IMF prepared the largest ever loans to rescue the Korean economy, supposedly to pull it out of the crisis. However, in actuality, the IMF's true intention was to bail out foreign investors such as banks, financial lenders, investors, and the like. South Korea gave up its economic sovereignty in exchange for the loans although it was once a development model. The IMF and World Bank seem to want South Korea to once again become a model economy, one that overcomes this time the financial crisis and resulting economic hardships, just as the country once before served as the state-led model economy for other developing and developed countries in the 1970's and 1980's. However, almost three years after the crisis, the Korean economy does not seem to be doing well; at best it is still struggling to recover. The Korea Composite Stock Price Index (KOSPI), which gives us a good indication of the performance of the current South Korean economy, has fallen from close to 1,000 points in May 1996 to below 700 in September 2000.[2] Although the South Korean economy was fueled by the biggest ever IMF rescue loans in the history of the IMF during the crisis period, it is still stumbling.

There were plenty of studies and reports that applauded South Korea as one of the most successful development models before the crisis, but since then the South Korean economy has been greatly criticized. One well known study that complimented South Korea together with other Asian countries was a 1993 World Bank publication entitled "The East Asian Miracle: Economic Growth and Public Policy." This publication researched the public policies of eight East Asian countries: Hong Kong, Indonesia, Japan, Malaysia, Singapore, Taiwan, Thailand, and the Republic of Korea from 1965 to 1990. It praised these state-led development policies not only for dramatic economic growth, but also for improved human welfare and more equitable income distribution. It praised South Korea as one of the most successful developmental models with "a combination of sound development policies", "tailored interventions", and "an unusually rapid accumulation of physical and human capital" (World Bank, 1993; Aseniero, 1996: 174-175).

[2] KOSPI recorded 653.68 points on September 9, 2000, according to the stock market news section of the Maeil Business Newspaper. Internet Edition, September 9, 2000.

On the other hand, Paul Krugman insisted that there is no miracle in the Asian economy in an article published just before the South Korean financial crisis happened. "Nobody can or should try to deny that Asian economies have achieved remarkable growth. However, that achievement is no miracle, if by a miracle we mean something inexplicable according to the usual law of nature" (Krugman, September 29, 1997). He continually argued that Asian growth resulted from high volume of investment, high level of education, and the transferring of a large number of the unemployed in the agricultural sector into the industrial or modern sector. In short his argument is that Asian economic growth is not "miracle", although he agrees that growth was rapid and significant. Other economists argue that "the key to the development is a high level of investment – the willingness to sacrifice current consumption for the sake of future production" (Haggard & Kim, 1997).

As such, many economists and officials of international organizations including the IMF and the World Bank complimented Asian economic performance. Even those who deny 'miracles' agree that the Asian economic performance, including that of South Korea, was magnificent. Before the financial crisis, South Korea was regarded as a model economy and a country that attracted compliments from other nations, economists, and the officials of international development institutions. Therefore, many people wonder what caused this troublesome crisis in what was once a successful state-led economic development model, and furthermore want to know if there is any way out of the resultant social and economic hardships. The existing explanations of the crisis can be broadly divided into two categories: the "internal" cause and the "external" cause schools.

A majority of scholars and economists, including the officials of the IMF and World Bank, attribute the crisis to the factors "internal" to South Korea, such as crony capitalism, a corrupt government, and high rates of corporate debt (e.g., World Bank, 1998; Goldstein, 1998). Although the World Bank once highly praised the South Korean economy as a model, it now blames the country for all its problems. Also, the IMF insists that South Korean banks and Chaebols[3] borrowed an overwhelming amount of foreign capital, especially in the form of short-term debt, after the liberalization of the financial sector in 1993. As a result, they could not keep up with payment obligations for such large loans, and could not avoid the financial crisis (Saito, 1998; IMF, September 1998; Sachs, 1999).

According to a conference report that was presented by a World Bank regional manager of East Asia and the Pacific, the origin of the crisis was "public policy failure, fundamentals that contained important weaknesses, and loss of confidence" (Shirazi, 1998). Another belief belonging to the same "internal" cause school ascribes the crisis to internal causes, specifically policy failure. From this point of view, the government failed to properly regulate, a failure due to under-regulation rather than to over-regulation. "In the name of financial liberalization, the government also failed to monitor properly foreign borrowing activities" (Chang, 1997).

However, the "internal cause school" fails to explain why the crisis did not occur in the 1970's or 1980's when the level of debt was higher than that in the late 1990's. In the case of South Korea the high debt ratios of corporations have coexisted throughout the history of economic development. The ratio reached almost 350 percent in 1985, but

[3] "Chaebol" is the Korean term for the big conglomerates which account for a great proportion of the gross national product.

the South Korean economy recorded a current account surplus for the first time in 1986 and again in 1987, 1988, 1989, and 1993. The current account deficit in other years implies capital account surplus, or foreign capital inflow, and this means that the debt flowing into the country from overseas played a vital role as an engine of economic development in South Korea. Actually, external debt, even if it was of significance, did not become a threat that could destroy the national economy until 1997. As a matter of fact, the government either helped the corporations to borrow from overseas or else more or less overlooked it.

This "external" cause school put the blame on the lenders. The lenders to be blamed include the Japanese and other foreign lenders who acted irresponsibly and the international financial speculators who took advantage of foreign reserve shortages (e.g., Woo-Cumings, 1997; Cho, 1998; Singh, 1999). This group of people argues that the crisis took place because of the external cause such as the international speculators' attack on local currencies using hedge funds, mutual funds, pension funds, and other financial instruments. Another says that the crisis was caused by US corporate-led financial globalization utilizing the WTO, IMF, APEC, GATT Uruguay Round agreements, etc. (Bello, 1998). From this point of view, "the roots of the crisis lie in the deliberate policies of the World Bank, the IMF, and the WTO to remove barriers to corporate flows of trade and investment and to codify corporate "intellectual property rights" (Cavanagh, 1998). By eliminating the barriers to the inflow of foreign capital, international speculators' games start, and also transnational corporations invest in more profitable countries such as South Korea rather than in their own countries.

On the other hand, the "external" causes, such as irresponsible lenders and greedy speculators, are in fact quite relevant in understanding the contemporary features of global capitalism. When these "internal" and "external" causes are put together, it becomes clear that the crisis occurred when the South Korean borrowers and international lenders met in the arena of the South Korean liberalized financial market which is freely connected to the global financial market. The process of financial liberalization was forced by the American government and business interest, although it was also welcomed by the South Korean businesses. This draws our attention to the issue of the bilateral relationship between South Korea and the USA because it was the US government that pressured the South Korean government to take liberalization measures.

This research is motivated by the question why the crisis occurred. Through the examination of historical processes leading to the crisis, it became clear that US-South Korea bilateral relationship should be focused. While recent US policy change toward South Korea turned out to be a critical aspect of the crisis, there existed long standing features of South Korean development that prepared the road to the crisis, e.g., the debt-dependent, Chaebol-centered, and worker-sacrificing strategy. Thus, the purpose of this thesis is first to examine what caused the South Korean financial crisis, secondly to attempt critical examination of the historical characteristics of South Korea development experience, and thirdly to examine policy implication, or to seek the best way for the average Korean person to live a quality life. Furthermore, this research will detect what kinds of social problems have arisen as a result of the financial crisis, an issue which had received relatively little study thus far. This research will historically examine those aspects of the crisis caused by US policy change, using an interdisciplinary approach that incorporates studies in history, sociology, international relations, political science, and economics.

In the next three chapters, South Korean experience is examined in the pre-liberalization period (the Korean War to 1984), the liberalization period (1985 to 1997) and the post-crisis period (from 1998 to the present). This periodization is based on the characteristics of South Korean development and the changes in US policy toward South Korea. South Korea developed under the auspices of the US who provided aids and loans in the first period. Success of debt-leveraged development and export-oriented industrialization prepared the marked expansion of South Korean export to the US in the liberalization period. With an increasing bilateral trade deficit, the US pressured South Korea to open markets, and when the Cold War was over, the US pressured South Korea for liberalization in finance. The third period, the post-crisis period, is currently proving to be the harshest time for Koreans with even more pressure being brought to bear by the US. The US government uses the IMF to implement measures that make South Korea an international debt-slave and deprive South Koreans of their sovereignty and enterprises. The concluding chapter summarizes the South Korean development experience and proposes new direction for a more equitable and independent development.

II. Pre-Liberalization Period: Debt-Leveraged Development (the Korean War to 1984)

The history of South Korean economic development from the birth of the country until today cannot be told without the involvement of the United States of America. Under the tutelage of the US, South Korea achieved remarkable 'success' in becoming one of the major economies. However, it is necessary to identify the underlying processes whereby South Korea deepened its dependency on US aid and loans, while promoting big businesses at the expense of the ordinary people.

The Republic of Korea (South Korea) has had a long-standing economic and political relationship with the US since its birth.[4] The US supported the establishment of the Republic of Korea after the Korean people achieved independence from Japan in 1945. In the years following independence, American diplomats, aid officials, and workers in private sectors got involved in providing necessities for Koreans. Also, many American soldiers fought and died in Korea during the Korean War from 1950 to 1953 in an effort to protect South Korea whose existence was threatened by the invading North Korean communist force. After the Korean War, the US provided South Korea with substantial assistance both economically and politically, and the US was deeply involved in successful South Korean development. Thus, Americans "have helped to keep South Korea safe from a North Korean renewal of the war stalemated more than thirty years ago and to achieve prosperity. In the decades since the Korean War truce was signed, the US

[4] In fact, the Korea's official relationship with the US started with the signing of a treaty agreed on May 22, 1882. But the relationship saw a period of vacancy during the Japanese rule (Ku, 1983: 8-11).

has played crucial governmental and commercial roles in assisting South Korean economic development" (Olsen, 1988: XV).

<Table II-1> US Aid to Korea

Year	Free Aid	Compensation Aid (Loan)	Total
1945	4,934	-	4,934
1946	49,496	-	49,496
1947	175,371	-	175,371
1948	175,593	-	171,593
1949	116,509	-	116,509
1950	58,706	-	58,706
1951	106,542	-	106,542
1952	161,327	-	161,327
1953	194,170	-	194,170
1954	153,925	-	153,925
1955	236,707	-	236,707
1956	326,705	-	326,705
1957	382,892	-	382,892
1958	321,272	-	321,272
1959	222,204	12,740	234,944
1960	245,393	6,100	251,493
1961	199,145	3,100	202,345

Million Dollars[5]
Source: Bank of Korea, "Tonggye Nyunbo" (translated into "Annual Report of Statistics"). Recited from Ku. ed. Hankookkoa Mikook: Kwageo, Hyunjae, Mirae (translated into "Korea and America: Past, Present, Future"), Parkyongsa, 1984: 219.

South Korean economic development emerged from the utter devastation of the Korean War (1950-1953) that followed a 36 year period of colonial exploitation by the

[5] Dollar or $ indicates US currency hereafter, unless otherwise indicated.

Japanese (1910-1945). Without natural resources and with little food to feed people, overseas aid, mainly from the US, was the only means of survival until the national economic development project was launched in 1962. Even though Korea did not ask for official aid, the US started to provide aid for South Korea after the Korean War for the purpose of promoting US security interest in the region (Ku, 1984: 221). A large inflow of US aid helped Korea as shown in Table II-1 achieve a moderate rate of economic growth between 1953 and 1958. However, economic growth was blocked during 1959 – 1962 and the growth rate of GNP per capita fell close to zero in the early 1960's (Islam, 1997), due to vast corruption among politicians resulting in widespread chaos in every aspect of society.

In addition, US aid started declining after it reached the peak of $383 million in 1957. Free US aid dropped to $321 million in 1958 and to $245 million in 1960 (see Table II-1). The reason why the US reduced the amount of aid to South Korea was the dollar crisis and the aggravation of the US balance of payments. Eventually, this reduction in US aid hit the aid-dependent economy hard, and companies that received aid in the form of foodstuffs and wares could not operate fully. As a result, the unemployment rate soared and prices dropped. As a matter of fact, the Korean economy encountered severe recession for the first time. The GNP growth rate recorded 8.1 percent in 1957 but fell to 2.5 percent in 1960. The decrease in US aid also affected the revenue of the South Korean government. In response, the government increased taxes to offset the revenue loss. Taxes as a percentage of GNP were raised from 10.0 percent in 1957 to 16.5 percent in 1960. Such an unpopular government policy under the condition of economic difficulty for the public, together with corruption among politicians and power brokers, led to the "4.19 (April 19) Democratic Revolution" in 1960 (Lee, 1987: 135-137).

Even though the amount of US aid declined from 1958, US aid was continuously infused into the South Korean economy. Indeed, South Korea remained one of the largest US aid recipients from 1946 to 1962. The total amount of the aid, composed of both military and economic assistance, was $5.434 billion during this period, and this ranked South Korea first among the US aid recipient countries (see Table II-2). From the 1960's until 1978, total US economic aid given to South Korea was equal to that received by all the African nations combined (Aseniero, 1996: 179; Cumings, 1987).

Why did the US provide the largest amount of aid to South Korea among all aid-receiving countries? Was it simply for South Korean economic development or out of compassion for the ailing country? The answer is unquestionably no. Even though aid itself costs the aid provider, it helps a provider export private sector capital and exploit resources from aid receiving countries. Moreover, it helps strengthen the political and military linkages with receivers, and affects the policy making process of the aid recipients. Through this channel, it helps an aid provider pursue commercial profit. In this regard, aid should not be understood based on provider's sympathy over the recipient, but as an endeavor of the provider in the pursuit of profit making opportunity. Former US president John F. Kennedy once expressed that foreign aid was provided so that the US could take control over or influence aid recipients, and that US support is given to those countries that would perish or become communist if no aid was provided (Lee, 1987: 113-116). This US policy stance needs to be kept in mind, when we try to understand the US policy toward South Korea in the post Korean War period. The US had keen interest in military, political, and international relations in East Asia, and South Korea was and has been positioned geo-politically in the most critical location for the US to achieve its strategic goals in the region.

<Table II-2> US Aid by country (1946-1962)

Country	Total	Military Aid	Economic Aid	Ratio of Overseas Debt	Rank
Total	97,695	31,060	66,615	35.9	
South Korea	5,434	2,002	3,431	2.3	1
Taiwan	4,428	2,377	2,052	17.3	2
India	3,952	-	3,952	69.6	3
Turkey	3,869	2,288	1,581	36.6	4
Japan	3,694	1,033	2,661	14.6	5
Greece	3,388	1,603	1,785	14.7	6
Vietnam	2,442	742	1,699	5.8	7
Brazil	1,953	116	1,739	91.9	8
Pakistan	1,890	-	1,890	42.5	9
Philippines	1,753	419	1,334	29.2	10

Million Dollars
Source: Charles J.V. Murphy, Foreign aid: billions in search of a good in fortune, Mar. 1963; Recited from Lee Nae Young, "Hankook Kyongjeui Kwanjum" (translated into "A View of Korean Economy"), 1987: 143.

With this background, South Korean national economic development started when General Park Jung Hee, who became president in 1963, launched the First Five Year Plan for economic development in 1962, one year after his successful military coup d'etat. The Plan was intended to break the vicious circle of poverty and to build a foundation for self-sustaining growth. From this economic development plan, a series of plans with different objectives were initiated and most were successfully completed. The Second Plan (1967–1971) aimed mainly to vitalize the microeconomic functions of the government, and to promote efficient allocation of resources through agricultural, industrial, trade, and social infrastructure policies (Song, 1990).

The Third Plan (1972–1976) was designed to shift the structure of the industrial sector from labor-intensive industries to chemical and heavy industries. The promotion of heavy and chemical industries was initiated by the South Korean government for security reasons but was also promoted by the US government. "Since 1961, the developmental state in South Korea has justified its regime in terms of the urgent need to rescue the nation from the brink of starvation as well as defend it from the North (Korea) threat. The state's commitment to heavy industrialization in Korea during the early 1970's was security driven, partly motivated by a U.S. decision to place clearer limits on its military commitments in East Asia" (Suh, 1998: 44). The objective of the Fourth Plan (1977–1981) was to upgrade the heavy and chemical industries to skill and technology intensive industries (Islam, 1997). Because the Five Year Plans were designed by President Park, who was assassinated during his office period, they were not well maintained nor developed by the succeeding Presidents. The Fifth Plan (1982 – 1986) was designed for more liberalization of the economy, and the Sixth Plan (1987 – 1991) was focused on the balance of regional development. The Seventh Plan (1992 – 1996) was initiated by President Roh Tae Woo, but it was replaced with a new Five Year Plan (1993 – 1997) by President Kim Young-Sam. He gave more emphasis on the development of the private sector and the reliance on the market system (Islam, 1997).

In order to achieve the goals of national economic development, the military regime led by President Park Jung Hee not only mobilized old Chaebols that were already formed during the Japanese colonial rule but also promoted new companies that later joined the rank of Chaebols. In particular, the government promoted the Chaebol companies in the heavy and chemical industries not only for military strategy purposes with US encouragement but also for economic development purposes in the 1970's. The government supported the Chaebols both through cheap credit allocation and with protective economic policies. For instance, the government tried to keep wages low by impeding collective bargaining as well as by interfering in all types of industrial relations. The companies were becoming more dependent on the government when they were in disputes with their employees. Between the government and the big corporations, workers and ordinary people gave up their freedom of speech and the right to protest and even negotiate (Lee, 1997: 407-409). As a result, the Korean Chaebols could accumulate their wealth at the expense of workers and ordinary people.

<Table II-3> The GNP per capita trend of South Korea

Year	1970	1975	1980	1985	1990	1995	1998
GNP per capita ($US)	253	594	1,598	2,229	5,886	10,823	6,823

Sources: "Juyo Kyungje Jipyo" (translated into "Major Economic Indicators"), Major Indicator 2, Statistics Ebook Service, National Statistical Office of the Republic of Korea. http://www.nso.go.kr

As a result of the aggressive economic development planed and led by the government, South Koreans' GNP per capita had increased greatly from $ 253 in 1970 to $1,598 in 1980 to $5,886 in 1990. For the first time in 1995 South Korean GNP per capita exceeded $10,000 at $10,823 (see Table II-3). Throughout the 1970's and 1980's the annual GDP growth rate was between seven and nine percent.

<Table II-4> Rate of private savings

Year	1960	1965	1970	1975	1980	1985	1990	1995
%	2.9	5.7	12.2	15.5	18.0	23.7	27.4	26.0

Source: Song Byung-Nak, "The Rise of the Korean Economy", Hong Kong: Oxford University Press, 1997: 60-61.

As for the financing of the rapid economic development, South Korea used the funds for economic development from two sources: domestic savings and overseas loans. Domestic savings in the 1960's, however, were not sufficient as the rate of private savings remained single digit (see Table II-4). Although the percentage of the private savings increased in the 1970's, they were far from enough to achieve the goals of the economic development plans, especially in the phase of heavy and chemical industry development.[6]

<Table II-5> Foreign loans in the 1960's and 1970's

	67-71	1972	1973	1974	1975	1976	72-76
Public Loan	733.5	324.4	368.5	316.6	575.6	694.7	2,279.8
Commercial Loan	1,512.9	326.4	344.4	616.0	829.5	852.3	2,968.6
Total	2,246.4	650.8	712.9	712.6	1,405.1	1,547.0	5,248.4

Unit: $ million

Source: Lee Nae Young, Evaluation Report of the Third 5 Year Plan, "Hankook Kyongjeui Kwanjum" (translated into "A View of Korean Economy"), 1987: 162.

As the US aid was drying up by the early 1960's, the public and commercial loans replaced official aid as the major source of development finance. As Table II-5 shows,

[6] From 1962 to 1981 more than 50 percent out of the total source of economic development plans fund was provide from overseas in the form of loans. In fact, contribution of foreign loans to economic growth was 4.1% (real growth rate: 7.9%) during the First Plan; 4.8% (real growth rate: 9.72%) during the Second Plan; and 3.3% (real growth rate: 10.2%) during the Third Plan of GNP growth (Lee, 1987: 181).

the Korean government borrowed a huge amount of foreign loans in the form of commercial and public loans, particularly in the 1970's. The source of such loans was mainly the US, and Japan became an important source after the normalization of diplomatic relation between South Korea and Japan in the 1970's.

The total foreign debt had grown steadily since 1963, but it increased rapidly especially in the 1970's. Such a large amount of foreign finance was needed in order to develop heavy and chemical industry sectors in the 1970's. This kind of borrowing had lasted throughout the period of economic development plans, and rendered the Korean economy heavily dependent on loans (Deyo, 1989: 15-18) from the US and Japan. In a sense, what South Korea achieved in the pre-liberalization period was "debt-leveraged" economic development. South Korean economic development was prompted by external debt, and even though the amount of debt reached a high level, the South Korean economy was not threatened by repayment or debt-servicing obligations.

As Figure II-1 points out, the ratio of total foreign debt to GNP in the 1970's and the 1980's was very high when compared to that of the 1990's. For example, the ratio reached almost 50 percent in 1980 and went over 50 percent from 1981 to 1985 (see Figure II-1 and II-2). These figures demonstrate that the theory, which had been propagated by officials from the IMF and World Bank as well as a majority of scholars and researchers to explain the 1997 crisis, did not work. The theory that the high debt ratio of the country would lead to the financial crisis did not apply to South Korea in the 1980's.[7] Indeed, the ratio of debt to GNP was higher in the 1980's than that in the 1990's.

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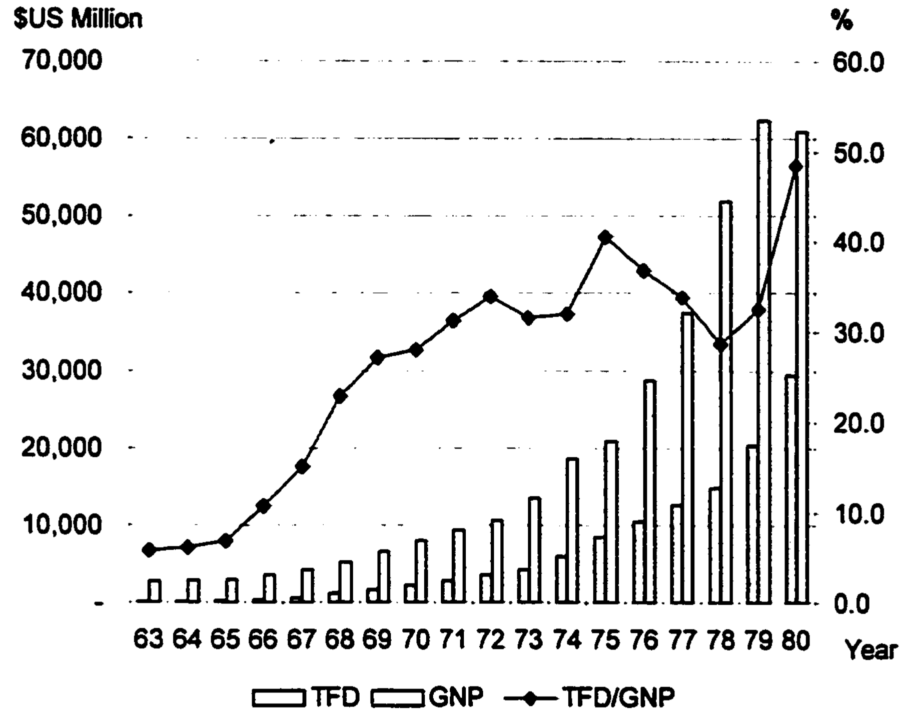
[7] The ratio of short-term to long and mid-term loans in the 1970's and 1980's did not exceed 50 percent (Lee, 1987: 178).

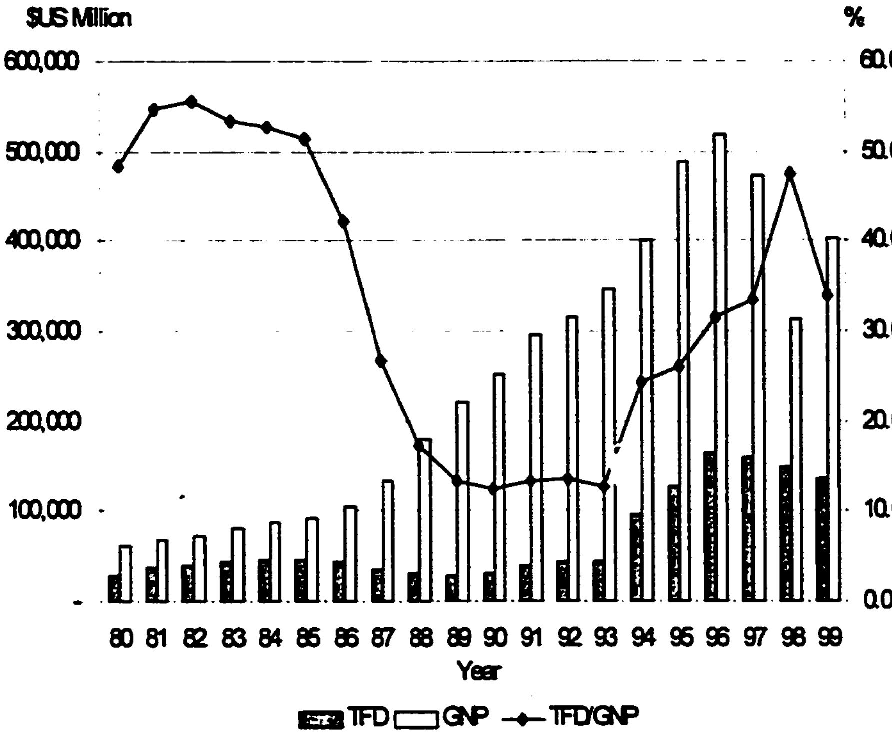
<Figure II-1> Total foreign debt to GNP ratio (1963 to 1980)



TFD stands for Total Foreign Debt.
Source: Song Byung-Nak, The Rise of the Korean Economy, Hong Kong: Oxford University Press, 1997: 60-61.

Aside from its role as the supplier of official aid and public loans, the US government and its policies played a critical role in the successful South Korean economic development. The US official attitude toward South Korea was that of "tolerance" (Cumings, 1997: 67-68). Success in export-oriented industrialization was not possible without easy access to US finance, technology, and markets. One of the reasons why the US government encouraged South Korea to become an export-led economy was that export earnings were critical to pay back South Korean debt (Cumings, 1997: 68-70 and 80). In other words, the US turned South Korea into an absorber of US financial surplus.

<Figure II-2> Total foreign debt to GNP ratio (1980 to 1999)



TFD stands for Total Foreign Debt.
Source: "Juyo Kyungje Jipyo" (translated into "Major Economic Indicators"), Major Indicator 2 and International Trade Balance and Foreign Debt, Statistics Ebook Service, National Statistical Office of the Republic of Korea. http://www.nso.go.kr

Behind such US "tolerance" and "generosity" existed the motive derived from its military and economic strategy. First, South Korea was on the front-line to prevent the spread of communism/socialism. In order to use South Korea as the shield against communism, the US needed to station its troops and to mobilize a "friendly" South Korean military. Secondly, the US could make profits not only from loans but also from official aid. US official aid was a way of dumping surplus agriculture and manufactured goods, and at the same time, an instrument to create and protect a monopoly of US products in South Korea. Thirdly, the US benefited from importing inexpensive but quality goods from South Korea in addition to earning interests on loans.

Steady economic development since the beginning of the national economic development lifted the status of South Korea from that of a 'basket case' country to that of the 'successful model economy.' Under the surface of such success lied fundamental characteristics of South Korean development: politico-military dependence on the US, financial dependence on aid and loans, excessive promotion of the Chaebols, and the sacrifice of ordinary people. All of these characteristics play important roles in the unfolding of the South Korean 'miracle' in the liberalization period from 1985.

III. Liberalization Period: Accumulation of Short-Term Loans (from 1985 to 1997)

Debt-dependent, yet successful South Korean economic development in the period leading to the 1980's was simultaneously a period that prepared US policy change. This chapter reviews the path that led the South Korean economy to 'liberalization' and 'intensified debt-dependency,' which ultimately brought the financial crisis. This chapter is organized as follows.. First, there will be a review of bilateral South Korean trade surplus vis-à-vis the US. This trade imbalance led the US to threaten South Korea for market opening. Secondly, there will be an examination of the process the US prepared for Super 301 as a weapon to open foreign markets. Thirdly, this paper will examine the process of liberalization in trade and finance. Lastly, the immediate process that led to the financial crisis will be examined.

1. Increase in South Korean Trade Surplus

Table III-1 and Figure III-1 summarize bilateral trade balance between South Korea and the US. US imports from Korea markedly increased from 1986 to 1988, much faster than the growth of US export to Korea. The bilateral balance was favoring South Korea only marginally in the first half of the 1980's, but the size of imbalance jumped to a quite high level between 1985 and 1988. The US bilateral trade deficit with South Korea hit its peak at close to 10 billion dollars in 1987 and 1988. Such South Korean trade performance pushed Korea in the eyes of American policy makers as one of the biggest economic problems.

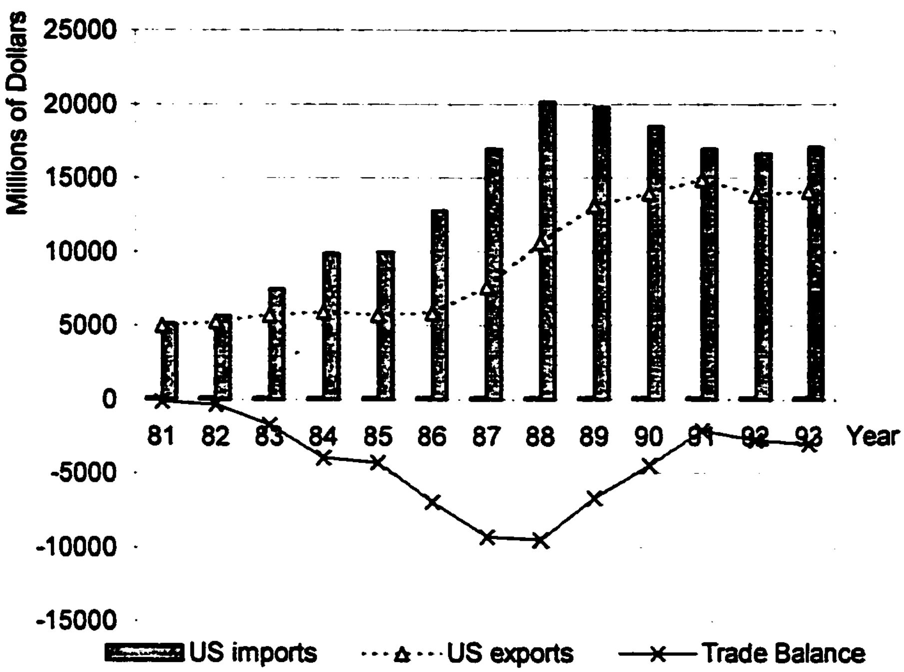
<Table III-1> Trade with Korea, 1981-93

Year	US imports from Korea (millions of dollars)	US exports to Korea (millions of dollars)	Bilateral trade Balance (millions of dollars)	Korean imports from the US as a percent of total imports	Korean exports to the US as a percent of total exports
1981	5,141	4,998	-143	23.1	26.8
1982	5,667	5,286	-381	24.6	28.8
1983	7,475	5,732	-1,743	24.0	33.8
1984	9,857	5,887	-3,970	22.5	36.0
1985	9,980	5,728	-4,252	21.0	35.6
1986	12,805	5,862	-6,943	20.7	40.1
1987	16,964	7,646	-9,318	21.4	38.9
1988	20,160	10,637	-9,523	24.5	35.4
1989	19,803	13,082	-6,721	25.1	32.4
1990	18,437	13,961	-4,476	24.3	29.9
1991	16,983	14,876	-2,107	23.5	25.5
1992	16,649	13,839	-2,810	17.0	22.3
1993	17,089	14,073	-3,016	n.a.	n.a.

n.a. = not available
Source: US Department of Commerce, "Survey of Current Business", various issues; IMF, Direction of Trade Statistics yearbooks, various issues, recited from "Reciprocity and Retaliation in U.S. Trade Policy" (Bayard & Elliot, 1994: 174).

In the process of increasing bilateral trade surplus with the US, the Korean economy deepened its dependence on the US market as the absorber of Korean products. The share of export to the US out of total Korean export reached 40.1 percent in 1986 (Table III-1). Thanks to this success of Korean export to the US market, the South Korean economy, for the first time in its history, recorded current account surplus in 1986. In the remaining of the 1980's, South Korea recorded current account surplus (Figure III-2).

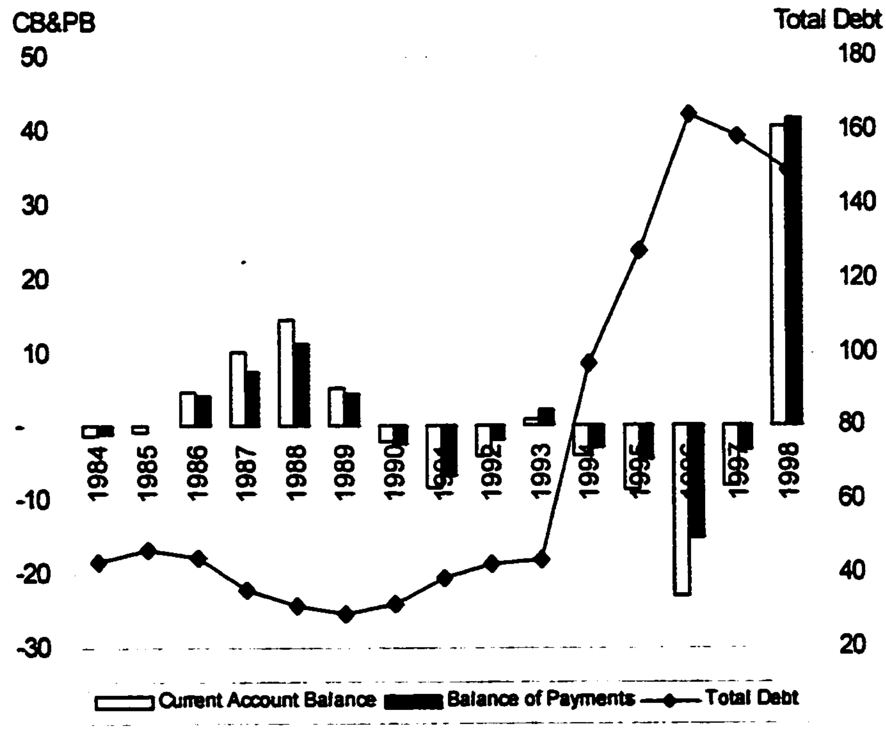
<Figure III-1> The US trade with South Korea



US imports from Korea and exports to Korea
Trade Balance: Bilateral Trade Balance
Source: US Department of Commerce, "Survey of Current Business", various issues; IMF, Direction of Trade Statistics yearbooks, various issues, recited from "Reciprocity and Retaliation in U.S. Trade Policy" (Bayard & Elliot, 1994).

Successful South Korean exports to the US market was partly a result of US dollar appreciation vis-à-vis the Japanese yen. "Because both South Korea...pegged to the US dollar, the value of their currencies followed the dollar down in 1986 and 1987, and their exports gained significant price competitiveness vis-à-vis Japan and other countries whose currencies appreciated in the period" (Bayard & Elliot, 1994: 176). This yen appreciation was a result of the Plaza Accord of 1985 among the G5 countries to lower the value of US dollar vis-à-vis other major currencies. This measure was an indication of the changes in the policies of the Reagan Administration in the early 1980's regarding a strong dollar. Together with the policy of free trade, deregulation (including financial markets), and tax cuts (Bayard & Iliot, 1994: 13), the so-called Reaganomics created twin deficits of US balance of payments and government budget. Balance of trade deficit, especially with Japan, alarmed the US policy makers to change its foreign exchange policy.

<Figure III-2> South Korean Current Account Balance, Balance of Payments, and Total Debt



Note: $US billion
CB stands for Current Account Balance; PB Balance of Payments
Source: "Juyo Kyungje Jipyo" (translated into "Major Economic Indicators"), Ministry of Finance and Economy, The Republic of Korea, September 1999.

The result of the Plaza Accord, however, did not alter the US trade balance in the desired direction. Instead of reducing the bilateral trade deficit with Japan, Japanese exports kept expanding. With mounting complaints from the negatively affected industrial sectors, the US government prepared tougher trade negotiation measures including the so-called Super 301, which is discussed shortly. One of the side effects of dollar depreciation against Japanese yen, however, was an increase in South Korean export to the US as shown in Table III-1 and Figure III-1. This increase in the bilateral trade deficit in the end caused the US policy makers to impose a tougher trade policy on South Korea.

2. Super 301 and the Loss of Favored Status

The US had maintained two principles in the US trade policy: multilateralism and nondiscrimination based on unconditional most-favored nation (MFN) treatment, which was embodied in the General Agreement on Tariffs and Trade (GATT). However, these principles and the GATT system itself were weakened in the 1980's (Bayard & Elliot, 1994: 9) as the US trade deficits were getting bigger not only with Japan but also with the Newly Industrialized Economies (NIEs) including South Korea.

What the US adopted for the trade policy from 1985 was unilateralism in that "first the United States frequently, but not always, unilaterally decides a foreign trade practice is unfair. Second, the United States typically requires that its partners unilaterally liberalize without any reciprocal concessions from the United States" (Bayard & Elliott 1994: 1). The US became more aggressive in pushing other countries to liberalize their economies and to reduce the barriers that hindered the US free trade. "The United States became more assertive in demanding that its trading partners reduce real and imagined barriers to US exports and investment and protect intellectual property rights" (Bayard & Elliott 1994: 1).

<Table III-2> Evolution of Section 301

Law	Change from previous law
Trade Expansion Act of 1962 (section 252)	
Trade Act of 1974 (Sections 301-302)	Replaced Section 22; extended coverage to services "associated with international trade"; authorized action against foreign export subsidies; required USTR to submit report to congress every six months
Trade Agreement Act of 1979 (Sections 301-306)	Clarified applicability of statute to services "whether or not associated with specific products"
Trade and Tariff Act of 1984 (Sections 301-307)	Explicitly authorized retaliation in the services sector; explicitly included for the first time in coverage of intellectual property and direct foreign investment; Section 181 requred submission of the National Trade Estimate Report to the Congress
Omnibus Trade and Competitiveness Act of 1988 (Sections 301-310).	Established Super 301, requiring USTR in 1989 and 1990 to identify trade priorities, including designating 'priority countries and practices' to be investigated under Section 301; established 'special' 301 to promote more aggressive assertion of intellectual property rights; established new deadlines for action in cases involving GATT dispute settlement or intellectual property

Source: selected from Bayard & Elliott, 1994: 24.

Eventually the US minted Super 301 to push Japan and South Korea, as well as other newly industrialized economies, to open up their markets and reduce barriers against US exports. The Super 301 was originally designed to take care of the trade deficit with Japan that reached alarming levels in the 1980's, especially in 1987 and 1988. The US Congress "wanted the administration to make deals that led to increased US exports; they wanted tangible results" (Bayard & Elliot, 1994: 23 and 171). Even though Super 301 was born in 1988, its origin dates back to the Trade Expansion Act of 1962 (Section 252), which developed to the Trade Act of 1974 (Sections 301-302) to

Trade and Tariff Act of 1984 (Sections 301-307), and eventually to the Super 301 in 1988 (see Table III-2).

Whereas Super 301 targeted the Japanese market and trade practice initially, it later became a major weapon to open the South Korean market after South Korea graduated from preferential tariff treatment. This treatment once helped South Korea to shift the export-led development strategy from the import substitution strategy (Cumings, 1987), but "(t)he Reagan administration tackled the issue of special and differential treatment for the NIEs in January 1988, when it announced that a year hence, South Korea and Taiwan (along with Singapore and Hong Kong) would be 'graduated from preferential tariff treatment under the Generalized System of Preferences (GSP)" (Bayard & Elliot, 1994: 171). According to a bilateral agreement with the US, the South Korean government had no choice but to adopt some liberalization and deregulation measures: liberalization of "restrictions on foreign investment", "removal of 'special law' in favor of import substitution strategy", and "enhancement of transparency of its customs procedures" (Bayard & Elliot, 1994: 171).

Super 301 was nót a big threat to South Korea until 1989 in spite of the fact that Korea was on the Super 301 list. There are several reasons for the US to acknowledge South Korea as "preemptive" although the county was listed atop in the list. "A former trade negotiator, Kim Chulsu, offered four reasons: (1) fear that designation would trigger an outbreak of anti-Americanism in Korea; (2) concern that it would provide ammunition to obstructionists who opposed Korea's already announced plans for liberalization; (3) commercial uncertainty resulting from the mere possibility of retaliation; and (4) [a genuine belief that] the branding of Korea as an 'unfair trader' would be unfair" (Bayard & Elliot, 1994: 178).

<Table III-3> Super 301 results (Korea and Taiwan)

Case	Outcome of negotiations	Estimated annual increase in exports	Assessment	Comments
Korea	Agreement reached preemptively	Little or none	Nominal success only	Although commitments carried out on paper, continuing bureaucratic red tape prevented significant liberalization
Taiwan	Taiwanese plan accepted, no formal agreement	\$100 million to \$500 million[a]	Some objectives largely achieved	Tariff reductions mostly implemented as promised; reduction of trade surplus targets met; however, adjustment more likely due to appreciation of the new Taiwan dollar and political manipulation than to liberalization

a. Based on USTR's estimate of benefits of promised tariff reduction (National Trade Estimate Report 1993, 247)
Source: selected from Bayard & Elliott, 1994: 43.

Until the end of the 1980's, South Korea could invoke security concern as the reason for its exempt status for trade liberalization. In the spring of 1989, Korean negotiators, with Han Seung-Soo, the Trade and Industry Minister, visited the US in order to defuse the pressure or to avoid the designation. During their visit, Minister Han argued that designation of South Korea as a Super 301 target country "would have a symbolic significance whether or not it resulted in retaliation" (cited in Bayard & Elliot, 1994: 178). However, he warned the US that the US policy "would strengthen the hand of protectionists in our country and would be tantamount to giving certain economic matters greater priority than security issues. It would not be wise to destabilize [Korea's] democratization program" (cited in Bayard & Elliot, 1994: 178). These South Korean visits and their demand based on security concerns worked anyway to slow down the radical market opening (see III-3).

It is noteworthy that the US acknowledged the security reason raised by the South Korean government and that security concern was winning over economic reasons until 1989. However, international political environment had totally changed in the late 1980's and in the early 1990's when Soviet Union was dismantled and the Berlin Wall was torn down. This phenomenon sent a signal to the world that the Cold War was over. The US did not need to be so gentle or generous toward its allies such as South Korea and Taiwan. The US shifted its priority from security to trade, and started to pressure South Korea to liberalize the financial sector. Then, Super 301 emerged as the weapon of choice to make markets of other countries open for US products.

One of the US policies was to support such countries as South Korea and Taiwan in order to keep in check such socialist countries as the USSR and China, but the US came to have no reason to protect or support South Korea any more in this regard. The US did not pay much attention to China's threat since China changed their policy toward a more pragmatic one in 1979 by Deng Xiaoping. China started to be more focused on developing their economy than strengthening its military. This is why the USSR was the one that the US had to watch for and the US was comparatively in favor of South Korean economic expansion until the end of the 1980's. The US wanted to use South Korea as a front-line restrainer against North Korean expansion with support from the USSR. In doing so, the US maintained its hegemonic power over the USSR and China.

The change of US policy to demand liberalization was not just applied to South Korea. Since the 1980's, the US actively pressured Japan and Germany to liberalize financial sectors and to eliminate those restrictions that prevented the US corporations to operate freely. This was a part of US strategy to dismantle "national" economic development (Reifer and Sudler, 1996: 32), but the most seriously affected "victim" of US policy change was not rich Japan or Germany, but South Korea and other Newly Industrializing Countries.

3. Liberalization of the South Korean Economy

With the economic, international, and political background provided by the US, the domestic environment that prepared the financial crisis was formed. In the 1980's, as mentioned above, South Korea faced tougher US demands to liberalize trade and deregulate domestic markets. Although the South Korean government attempted to take some financial liberalization measures, the financial system of South Korea changed little. However, the door was opened toward financial sector liberalization in the late 1980's, and this led to a fundamental transformation of the nature of the South Korean financial structure. The most visible change of the structure would be an increase in the presence of non-bank financial institutions (NBFIs) from the mid 1980's. Because these financial institutions were not regulated as much as the banks, Chaebols were extremely interested in using the NBFI to channel low cost finance (Chang and Yoo, 2000).

The US and domestic companies alike started demanding liberalization already in the late 1980's. The domestic companies, mostly Chaebols, began regarding the regulation and intervention in the exchange transaction system as a burden because they already had a free access to international financial market without government support. On the other hand, the government could not keep the regulation on the exchange system because of excessive liquidity flowed in as a result of the trade surplus in the late 1980's. Although trade surplus was over in the 1990's, the continuing relaxation of the regulation was justified by a large capital inflow (Chang and Yoo, 2000). With this development as background, the government of South Korea started taking measures for financial liberalization. In the exchange market, South Korea adopted its market average rate system in 1990 that determines exchange rates in market. "The shift from the fixed exchange rate system to the floating exchange rate system" means "the financial strength of capitalist enterprises exceeded that of the states" (Ikeda, 1996: 64-65).

> South Korea adopted its present market average rate (MAR) system in 1990. Under the MAR system, the Bank of Korea (BOK) – the country's central bank – has given market forces a greater role in the determination of exchange rates. The BOK implements monetary policy in conjunction with the government and sets the daily basic rate based on the MAR system. The basic rate is computed as the weighted average rate of the interbank spot transactions of the previous day. The won is now allowed to move within a 2.25 % band around the basic rate. The central bank often intervenes in the capital market through open market operations to affect market liquidity. It also regulates the foreign exchange position of the authorized banks, to stabilize the movement of won and to adjust domestic liquidity (Euromoney, June 1996).

Under US pressure to liberalize foreign exchange market with endorsement by the South Korean government, the BOK widened the band many times after 1991. In addition, a swap market was opened in October 1995 for the purpose of attracting foreign exchange transactions, but the activities in the market were not particularly strong in the first half of the 1990's (Euromoney, June 1996). The South Korean government favorably adopted liberalization because it was seeking a membership in the OECD.

"The gradual liberalization of the economy has attracted continued foreign capital inflows. As the government attempts to enter the Organization for Economic Co-operation and Development in 1996, more gradual economic deregulation will be planned. For example, the foreign equity participation ceiling on the local bourse was raised to 18% from 15% in April and will likely be lifted to 20% later this year" (Euromoney, June 1996).

Pressure to liberalize financial markets came from the foreign investors as well as domestic companies. They demanded further opening of Korean markets to exploit the wide interest differential with overseas markets. Thus, "(t)o meet their demands to a certain degree, a capital account liberalization plan was finally announced in 1993. This plan was superseded by the Foreign Exchange Reform Plan in 1994, which in turn was revived in late 1995. Further liberalization was recently announced in April, 1996" (Cho, 1998: 82).

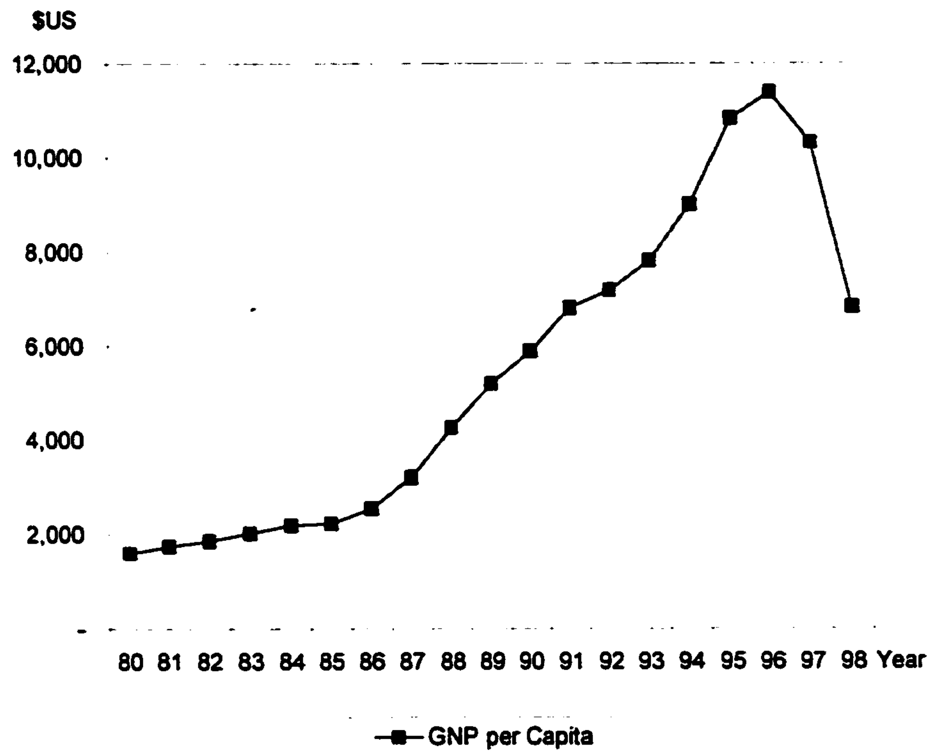
In the early 1990's, the macroeconomic situation of South Korea seemed to be getting better just after starting the liberalization of the financial sector. Economic foundation, as declared by experts in the IMF, WB, and OECD, was sound thanks to a large amount of foreign capital inflow that kept interest rates from rising, exchange rates from depreciating, stock prices and growth rate from falling (Black, 1996: 2). This rise in foreign capital inflow was a result of the three-step financial sector liberalization that was initiated by the President Kim Young-Sam's government in 1993. "The major factors include gradual deregulation of all interest rates except deposit rates by 1997, eliminating government influence over bank lending operations, encouraging the development of composition and new financial instruments, and promoting liberalization of the foreign exchange market and of capital flows" (Black, 1996: 12-13).

Figure III-2 traces a process leading to the crisis in a longer time frame than that in Figure III-5. It is clear from the figure that total Korean external debt had been stable around $40 billion and the balance of payments was more or less stable until 1993. In fact South Korean current account recorded surpluses in the late 1980's. In contrast to such "stability", the trend from 1993 is quite disturbing. Since the start of three-step financial liberalization, the total foreign debt had skyrocketed from around $40 billion to over $160 billion in 1996. Current account and the balance of payments turned to deficit from 1994, reflecting an increase in South Korean imports for facility investment and so forth without generating immediate export earnings in the process.

4. Effect of Liberalization

Between the start of full-fledged liberalization started in 1993 and 1996, a year before the crisis, the South Korean economy recorded enormous economic growth as shown in Figure III-3. This period is the time when the President Kim Young-Sam replaced the Seventh Plan (1992-1996) with a new Five Year Plan (1993-1997) that emphasized private sector development and increased reliance on the market system (Islam and Chowdhury, 1997: 161-162). Korean GNP per capita grew markedly from $253 in 1970 to $2,229 in 1985 to $10,823 in 1995 (see Table II-3). Roughly speaking, the figure increased almost more than forty folds in 25 years between 1970 and 1995. With the annual growth rate of GDP between seven and nine percent in the 1970's and 1980's, the Korean economy certainly became a model economy among the developing countries.

<Figure III-3> GNP per capita trend of South Korea



Sources: "Juyo Kyungje Jipyo" (translated into "Major Economic Indicators"), Major Indicator 2, Statistics Ebook Service at National Statistical Office of the Republic of Korea. http://www.nso.go.kr.

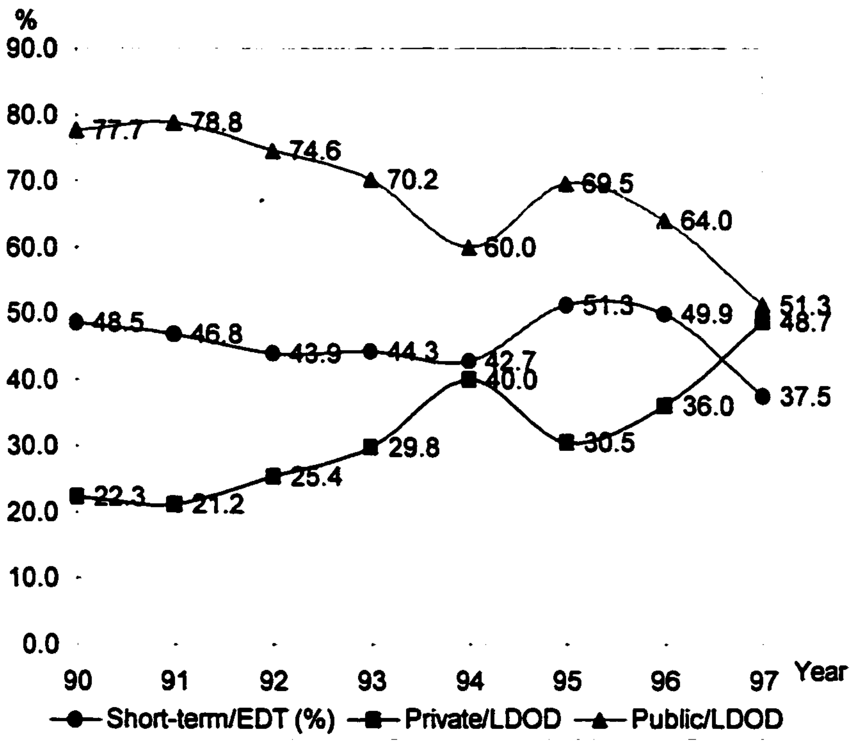
The financial liberalization resulted in the rapid accumulation of foreign debt that directly led to the 1997 financial crisis. Most scholars and officials have insisted that the crisis was a result of the accumulation of the short-term debt. However, the ratio of the short-term debt to Total Debt Stocks (EDT) seems not to be so serious compared to that of the early 1990's even though the ratio jumped slightly over 50 percent in 1995 (see Figure III-4). In fact the level of the ratio remained stable between around 40 and 50 percent in the first half of the 1990's, but it reached 58.3 percent by the end of 1996. As a matter of fact, the level increased to around 10 percent compared to the first half of the 1990's. Could it make South Koreans unsustainable? Actually not. The problem started from the dollar panic as a result of the chock of dollar circulation.

These measures of financial liberalization, with the positive outlook of the Korean economy, encouraged foreign banks and investors to lend a large amount of capital, mostly short-term, to Korean banks and major financial institutions and corporations. The amount of external liabilities owed by Korean private banks, as indicated by the Korean balance of payment figures, has increased steadily from $720 million in 1993 to $7.6 billion in 1994, $11.4 billion in 1995, and $9.9 billion in 1996 (IMF, 1999: 438-443). Such infusion of foreign capital made the Korean currency won appreciate against the US dollar for a short time, while deteriorating the current account balance and making difficult to control currency fluctuations for the government and eventually raising the amount of foreign debt to a dangerous level (Nam, 1998).

As regulations regarding international monetary transaction were lifted, Chaebols and banks started borrowing a huge amount of short-term loans from overseas (Crotty & Dymski, 1998). Short-term loans were encouraged partly because restrictions were attached to long-term capital inflows (Sachs, 1999). Those who borrowed short-term loans invested the capital into 'productive' projects that expanded production base in the semiconductor and shipbuilding sectors, etc., as well as in 'non-productive' projects such as real estate and stock market speculation (World Bank, 1998). Either way, these are the investments that would not generate instant return or that would be wiped out in the event of market collapse. To make matters worse, the overall world economy was stagnating and an "unexpected" Japanese yen depreciation from 1995 vis-à-vis US dollar weakened

South Korean price competitiveness. When exports did not generate sufficient income, Chaebols and financial institutions were not able to pay back debt and interests.

<Figure III-4> Structure of Short-term debt and Long-term debt



EDT stands for Total Debt Stocks, and LDOD Long-term Debt.
Private means Private nonguaranteed and Public means Public and Publicly guaranteed.
Source: The World Bank, Global Development Finance: Country Table, 1999: 308.

Figure III-4 reveals the most significant change is the ratio of the private nonguaranteed debt and the long-term debt. This graph shows more changes than that of short-term debt and total debt stocks. The amount of private non-guaranteed debt as a percentage of long-term debt increased from 21.2 percent in 1991 to 48.7 percent in 1997. In short six years, the percentage more than doubled. It means that private sector debt was getting out of control and needed careful monitoring. However, the government not only failed to watch the private sector debt but also did not play a critical role in the domestic financial system because of the financial globalization and the US pressure.

The borrowers of foreign capital were mostly Chaebols, banks, and other financial institutions. Financial liberalization in the early 1990's allowed the Chaebols to borrow foreign capital, most of which was in the form of short-term loan. Unlike in Mexico where huge foreign borrowing was simply used to finance consumption (Singh, 1999: 45-62), South Koreans used a good portion of foreign borrowing to continue their aggressive investment strategy from the 1980's. The "target" industrial areas included semiconductors, steel, shipbuilding, and automobiles (IMF, 1998: 9). Table III-4 points out that the South Korean manufacturing companies maintained higher debt-equity ratio than those companies in other countries such as Taiwan, Japan, and the U.S.A.

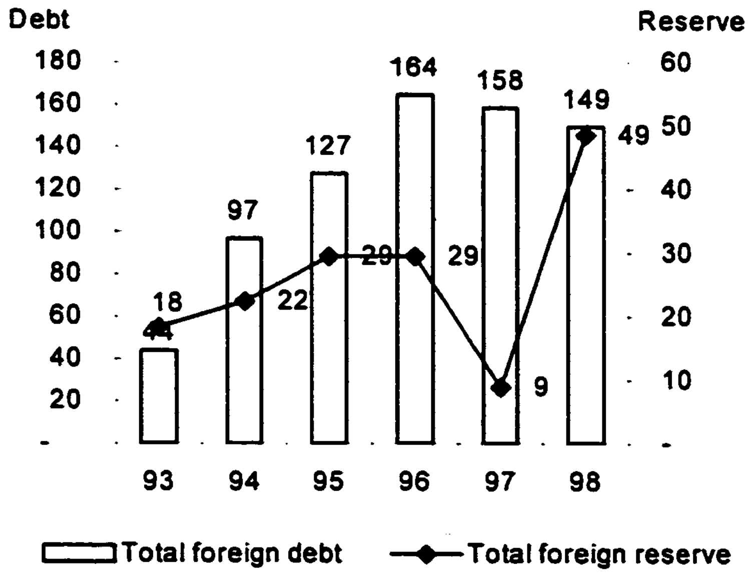
<Table III-4> Debt-Equity Ratios of Manufacturing Corporations (percent)

	1985	1990	1991	1992	1993	1994	1995
Korea	348	285	306	318	294	302	286
Taiwan	114	83	98	93	88	87	86
Japan	252	226	221	216	213	209	206
U.S.A.	121	149	147	168	174	166	159

Source: Sung Kwack, "The Financial Crisis in Korea: Causes and Cure", IMF Seminar Series, No. 1998-19 (Washington, June 1998). Recited from "World Economic Outlook", October 1998. IMF, Washington.

In 1996, one year before the financial crisis started, total foreign debt reached the highest level in the Korean history: $164 billion, while total foreign reserves were mere $29.4 billion (see Figure III-5). This imbalance between South Korean external liability and a meager amount of reserves signaled the short-term lenders that currency depreciation was imminent. Moreover "(a) drastic increase in the demand for the dollar was a result of a massive disintermediation by foreign lenders, who had suddenly become very much concerned about the business prospects in Korea. Korean foreign debt at the end of 1997 was very large, standing at $153 billion, (of which $82 billion were short-term debts due within a year)" (Choi, 1999).

<Figure III-5> Total foreign debt and reserve after 1993 three step liberalization



Note: $US billion
Debt: Total Foreign Debt; Reserve: Total Foreign Reserve
Source: "Juyo Kyungje Jipyo" (translated into "Major Economic Indicators"), Ministry of Finance and Economy, September 1999.

This development, on the other hand, was accompanied by financial market problems in other Southeast Asian countries. There was a spillover effect from countries such as Thailand, the Philippines, Indonesia, and Malaysia. The Thai baht was attacked by speculators in early 1997 due to "a large current account deficit", "high short-term foreign debt", "the collapse of a property price bubble", and "an erosion of external competitiveness." Equity price continued to downturn in the face of gluts in the property sector, especially in Malaysia and the Philippines. Thailand gave up its exchange rate peg against the dollar, letting the baht float because there were huge capital outflows. This process amplified doubts about exchange rate regimes in other Asian countries. The Philippines, Malaysia, and then Indonesia allowed their currencies to float on July 11, July 21, and August 14, 1997, respectively (IMF, December 1997: 15-22). In this process, foreign investors lost confidence in Southeast and East Asian markets, and they withdraw their investment. This spillover effect spread to the South Korean financial market.

Evidence suggests that since March 1997, soon after the bankruptcy of the Hanbo group in January, new medium to long-term loans coming from abroad had not been provided (Chosun Ilbo, January 30, 1998). To make things worse, the declaration of the bankruptcy of Kia Motor Company in August 1997 led to a complete drying-up of short-term loans. Moreover, Korean borrowers needed approximately $11.5 billion dollars by September 1997 to payback the loans that were approaching maturation. Banks and other financial institutions struggled to purchase dollars to repay the loans because the foreign lenders refused refinancing (Choi, 1999). Furthermore, "the building up of the expectation for currency devaluation induced many Koreans to substitute US dollar for won. For example, many Korean firms stopped converting their export earnings into local currency, preferring to hold them in dollars in anticipation of devaluation, further reducing the supply of dollars" (Choi, 1999).

As a result, foreign investors were alarmed by the sudden and massive dollar demand. The Bank of Korea (BOK) tried to calm down foreign investor anxiety, providing 32 trillion won for private Korean banks for the prevention of serial bank failures (Choi, 1999). Nevertheless, the South Korean government could not maintain confidence among foreign investors. Thus, they withdrew their lending from South Korean borrowers all of a sudden. The South Korean government vainly spent two-thirds of their foreign reserve in order to defend the won against assassin-like currency speculators, and the level of total foreign reserve had dropped to $8.9 billion in 1997 (see Figure III-5). Figure III-6 summarizes the process leading to the financial crisis and the result of the crisis.

<Figure III-6> Flow of the process leading to the financial crisis

Little foreign loans provided after Hanbo and Kia bankruptcies
⇓
Debt due approached
⇓
Skyrocketing demand for dollars but little dollars supplied
⇓
Dollar panic
⇓
Stock market crash and local currency won depreciation
⇓
Debt burden doubled
⇓
Koreans should work twice as hard as they did before
in order to repay the debt

This process led to the transformation of South Korea from a country with economic sovereignty to a country without. As Goldsmith portrays, this is a process experienced by many other developing countries in the 1980's and 1990's. "Lending large sum of money to the compliant elite of a non-industrial countries is the most effective method of confronting it and thereby obtaining access to it market and natural resources. ... A country that borrows large sums of money must fall into unrepayable debt ... once in debt, the country inevitably become hooked on further and further borrowing rather than cutting down on expenditure and thus fall under the power of the lending countries" (Goldsmith, 1996: 261-262).

Had Koreans known such a possibility, would they have borrowed so massively in such a short time? In a sense, the path toward liberalization was prepared by the debt-leveraged development strategy, and South Korean success undermined the very condition that favored its development. If it had not been for the South Korean miracle, the US would not have imposed liberalization so earnestly. And if the Chaebols had not been promoted as the engine of South Korean development, they might not have grown so large that they demanded liberalization. The end result of South Korean success was the financial crisis, and the analysis of post-crisis process in the next chapter should reveal true costs and benefits of the South Korean development experience.

IV. Post-Crisis Period: Losing Sovereignty (from 1998 to the present)

The South Korean economy collapsed in late 1997, and South Koreans lost their sovereignty in making decision regarding socio-economic policies. Although remarkable economic growth once impressed officials from the IMF and World Bank, who had even labeled South Korea as a model economy, their compliment stayed just for a short time. After the financial crisis, GNP per capita dropped to under $7,000 from over $10,000. The IMF loaned South Korea the biggest ever rescue package. However, almost three years after the crisis, South Koreans are still struggling to overcome all the problems resulted from the crisis. In this chapter, the process where South Korea lost economic sovereignty is reviewed first. The impact of the financial crisis, of course, is not limited to economic aspects. The cost of the crisis is mostly bore by the ordinary people of South Korea. In order to provide the basis of evaluating South Korean development experience, the second half of the chapter examines social cost of the crisis.

1. Structural Adjustment and Losing Sovereignty

Aftermath of financial crisis in the third world countries has been the loss of economic sovereignty. There are three major expressions of this humiliating experience. First is the loss of monetary sovereignty where the country loses capacity to control interest rates, create and allocate credit, and regulate flows of funds across the border. Second is the loss of fiscal autonomy where fiscal spending becomes subject to outsider supervision and permission. Third is the loss of controlling policies affecting trade, industry, investment, and even consumption. For those developing countries like South Korea where the government employed industrial policies, imposition of "free trade" doctrine, or forced convergence to neo-liberal global order, means a loss of control over powerful instruments for development. How did these happen to South Korea after the crisis?

The first job of president-elect Mr. Kim Dae-Jung before even taking the seat in the Blue House was to beg the IMF for an emergency loan. With US endorsement, the IMF prepared a bailout program where the IMF and major industrial countries took over insolvent private loans from the lenders and forced South Korea to keep its debt. The amount of the IMF rescue package (loans from the IMF and the major countries) was the biggest ever in the amount of $57 billion, surpassing the IMF 'rescue' package of $48 billion for Mexico in 1995[8] (Yonhap News, December 24, 1997; IMF Survey, December 15, 1997: 385).

Such a "rescue" package always involves "conditionality" over interest rates, government expenditure, and trade policy, and such IMF intervention is known as Structural Adjustment Programs (SAPs). The goal of the SAPs is to force "adjusted" countries to open their markets to global corporations. Thus, the IMF has become the prime enforcer of corporate globalism (Sanders, 1998). Such IMF policy, however, was to enforce what is called "Washington consensus", an ideology which advocates free-trade and free-enterprise activities as the panacea for prosperity. Materially, the US controls IMF mandates together with other major countries through the control of voting power within the IMF (Buckley, 1999: 16).

[8] South Korea received loans in the amount of $21 billion from the IMF and the rest of it from other member countries while Mexico received loans $17.8 billion from the IMF and the rest of it from other

In fact, the South Korea's initial agreement with the IMF made in December, 1997 for the rescue package affected almost all aspects of Korean economy including macroeconomic policy, financial sector restructuring, and other structural measures as summarized in Table IV-1. The basic idea of the agreement is to accelerate and foster liberalization, free trade, globalization, market openings, free investment, free acquisition of companies, and so on.

Clearly, the IMF rescue package was not good medicine for a financially troubled country. Instead, it intended to introduce US-type capitalism and its institutions so as to pave the way for major transnational corporations to enter the South Korean economy. For example the IMF Arrangement set a provision of labor market reform: "the capacity of the new Employment Insurance system will be strengthened to facilitate the redeployment of labor, in parallel with further steps to improve labor market flexibility" (Table IV-1). This provision attempts to apply the same criteria as in the US to South Korea. However, the characteristic of the South Korean labor market is significantly different from that of the US in that layoffs are unusual. This issue about the labor market will be discussed shortly. Another example is the arrangement regarding corporate governance and corporate structure. "No government subsidized support of tax privileges maintained to bail out individual corporations" (Table IV-1). This means that the government can not help insolvent companies like before. This is why so many South Korean companies went bankrupt and then sold out to US investors. Moreover, the IMF wants South Korea to make corporations prepare an "international" or US standard account system, that is, "for the transparency of corporate balance sheets, independent external audits, full disclosure, and provision of consolidated statement for business

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member countries.

conglomerates needed" (Table IV-1). All of these requirements indicate that the US (and therefore global) standards are to be introduced for an easy access of global corporations, international lenders, and speculators to the South Korean economy.

<Table IV-1> IMF Stand-By Arrangement December 5, 1997

Fields	Items	Arrangement
Macroeconomic Policies	Objectives	– Real GDP growth in 1998: below 3 percent – Inflation in 1998: below 5 percent – External current account deficit in 1998 and 1999: below 1 percent
	Monetary and Exchange rate Policy	– Tightened – Call rate: 12.5 percent December 1, 1997 → 21 percent December 5, 1997 – Money growth during 1998: 5 percent or less – Flexible exchange rate policy maintained
	Fiscal Policy	– Tight fiscal policy maintained in 1998 – Cyclical slowdown projected to worsen the 1998 budget balance of the consolidated central government by about 0.8 percent of GDP – Increasing VAT coverage and removing exemptions – Widening the corporate tax base – Widening the income tax base – Increasing excises, luxury, and transportation taxes – Reducing current expenditures supporting the corporate sector – Reducing low priority capital expenditures
Financial Sector Restructuring	Reform Bills by the National Assembly	– Will be passed before the end of the year as below: – A revised Bank of Korea Act, which provides for central bank independence – A bill to consolidate supervision of all banks (all financial institutions) – A bill requiring that corporate financial statements be prepared on a consolidated basis and be certified by external auditors

Financial Sector Restructuring	Restructuring and Reform Measures	– Troubled financial institutions will be closed. – A credible and clearly defined exit strategy will include closures as well as mergers and acquisitions by domestic and foreign institutions. – The disposal of nonperforming loans will be accelerated. – Any support to financial institutions will be given on strict conditions. – The schedule for allowing foreign entry into the domestic financial sector will be accelerated, including allowing foreigners to establish bank subsidiaries and brokerage houses by mid-1998. – Borrowing and lending activities of overseas' branches of Korean banks will be closely monitored.
Other Structural Measures	Trade Liberalization	– Timetables will be set in accordance with WTO commitments at the time of the first review, to: – Eliminate trade-related subsidies. – Eliminate restrictive import licensing. – Eliminate the import diversification program. – Eliminate and improve the transparency of the import certification procedures.
	Capital Account Liberalization	– Liberalize foreign investment in the Korean equity market by increasing the ceiling on aggregate ownership from 26 % to 50 % the end-1997 and to 55 % by end-1998. The ceiling on individual foreign ownership will be increased from 7 % to 50 % by end-1997. – The supervisory authority will allow such purchases provided that the acquisitions of foreign banks contribute to the efficiency and soundness to the banking sector. – Allow foreign investors to purchase, without restriction, domestic money market instruments – Allow foreign investment, without restriction, in the domestic corporate bond market. – Further reduce restrictions on foreign direct investment through simplification of procedures. – Eliminate restrictions on foreign borrowings by corporations.

Other Structural Measures	Corporate Governance and Corporate Structure	– For the transparency of corporate balance sheets, independent external audits, full disclosure, and provision of consolidated statements for business conglomerates needed. – The commercial orientation of bank lending respected. – No government subsidized support or tax privileges maintained to bail out individual corporations. – The real name system in financial transactions maintained.
	Labor Market Reform	– The capacity of the new Employment Insurance system will be strengthened to facilitate the redeployment of labor, in parallel with further steps to improve labor market flexibility
	Information Provision	– There will be regular publication of data on foreign exchange reserves, including the composition of reserves and net forward position with a two weeks delay initially. Data on financial institutions, including nonperforming loans, capital adequacy, and ownership structures and affiliations will be published twice a year. Data on short-term external debt will be published quarterly.

IMF Stand-By Arrangement Summary of the Economic Program December 5, 1997. IMF
Taken from http://www.imf.org/external/np/oth/korea.htm

This IMF Stand-By Arrangement initially made on December 5, 1997 has been changed several times based on the progress of economic recovery. However, the IMF basic package to Korea, especially the second version of the Arrangement introduced at the end of December 1997, created serious problems. After the second bailout, in fact, a large number of companies went bankrupt because "the IMF's percent inflation target was already too deflationary, given that the economy has to deal with a big rise in import prices due to devaluation; with the excess liquidity released by financial sector bailouts and the further fall of the currency since the signing of the agreement, this target now seems indefensible" (Chang, 1997).

The IMF also imposed further financial liberalization onto the weakened and fragile South Korean banking sector. Without an instrument to protect its banks or even gain time for the banks to recover, the South Korean government was forced to open the way for foreign takeover of South Korean private banks (Chang, 1997). The loss of financial sovereignty is near completion since the South Korean government is left with no "South Korean" bank to protect.

The IMF also demanded South Korea to maintain high interest rates, although high real interest rates in heavily indebted economies were obviously dangerous (Khor, 1998). The IMF insisted that if South Korea kept interest rates high, foreign capital would flow in. This may be true as long as investors do not take risk into consideration. However, high interest rates did not help South Koreans with their external credit crunch and simply forced many corporations to go under. Later, the IMF agreed to lower interest rates to protect the real-sector economy from further collapsing in May 1998 (Chun, May 7, 1998). But criticism toward IMF policy is rising as SAPs keep piling up "success" after "success" of crushing developing country economies. The IMF administered the SAPs to 89 countries from 1965 to 1995. One research argues that 48 out of 89 countries have not improved, and 32 countries had gotten even poorer after receiving the help of the IMF (Kim, September 24, 1998).

In the process of post-crisis "structural adjustment", the IMF instructed the South Korean government to raise interest rates. While some economists criticized the wisdom of such interest rate policy after the crisis deepened (e.g., Krugman, 1998; Zhang, 1998), the immediate consequence was a score of bankruptcies among South Korean companies. Under the high interest rates, 20,000 firms went bankrupt in the first half of 1998 (The

Economist, 1998). These companies went under due to bank refusal to provide credit, and most of them were medium to small sized enterprises. Such difficulty, faced among the medium to small sized companies, in fact, was not only created by the large sized corporations but also used by the same large sized corporations to strengthen their domination. Such a development had a grave implication in the distribution of income. In short, the crisis worsened income distribution in South Korea. A detailed discussion of the changes in income distribution is given in the next section.

After the financial crisis, most officials and scholars have insisted that the South Korean economy needs more opening and liberalization along with the policy administered by the IMF and World Bank. Even South Korean high official, Lee Hong-koo, a member of the South Korean National Assembly and a former prime minister, says that "(t)he model is now clear. It's not Japan. It's the West. The current crisis has convinced almost all people that the old style doesn't work. We will adjust ourselves rapidly to the new requirements, which means we will fashion ourselves more like the West, like the US and European model" (Kristof, 1998). "If we faithfully implement the reforms we agreed on with the IMF, we will emerge with a stronger economic foundation, and we will be poised to overtake Japan", said You Jong-keun, a top economic adviser to President-elect Kim Dae-jung (Kristof, 1998). They believe that the Korean economy will be getting better or become more like that of the western countries if South Korea follows IMF suggestion and liberalizes the economy completely.

However, the reality is that the IMF presses South Korean firms to lay off their workers just like in the U.S. without considering South Korean tradition of avoiding employee lay-off. Another long-standing South Korean tradition includes honoring seniority, patriarchal benevolence of the manager to his workers, lifetime employment, and family-like atmosphere maintained in numerous firms. This tradition helped South Koreans pull their economy out of the miserable life just after the Korean War since the Korean workers worked day and night without taking many holidays and sacrificing time to be spent with families. However the IMF pressed South Korea to abandon this tradition and to adopt the American standard where companies can lay off their employees freely. The basic problem of the lay-off system that follows employment practice in the US is that South Korea had not well prepared an employment insurance program and re-training schemes (Chang: 1998). It means that those laid-off cannot rely on unemployment insurance to acquire new skills needed to find new jobs, and they cannot support their families if they have little savings. Furthermore, there is age discrimination in the labor market which gives rigidity to the labor market. This environment prevents the newly fired older workers from finding and getting good jobs. In fact, partial application of the US-style labor practice, i.e., easy lay-off but little insurance or no provision to prevent age discrimination, does not work in South Korea. Therefore, the application of the IMF standards only adds to frustration among South Koreans and it became the cause of numerous incidences of suicide.

This development in the labor market can be interpreted as an extension of the phenomenon of American cultural globalization which is already taking deeper roots among the people. For example, many South Korean teens wear American designed clothes, eat McDonald's or Burger King hamburgers instead of Korean Kimchi, enjoy American sports such as baseball or football, and watch Hollywood movies. Walking along the streets in Seoul, people can see a lot of neon signs that are written in English and numerous stores that sell American beers, whiskies, and cigarettes all over the city. "All this will make Asia's labor markets, finance and industry resemble America's a bit more, but Americans do not become more group-oriented or respectful of their parents when they put on a Sony Walkman" (Kristof, January 17, 1998). Although these cultural phenomena cannot be reduced the policies imposed by the IMF and World Bank, they constitute an integral part of South Korean social transformation in the post-crisis period.

2. The Costs of the Financial Crisis

Most of the research on the Asian financial crisis is focused on the financial and economic difficulties in the region. In comparison, social impacts resulting from the financial crisis have not been studied much. However, the social cost of the crisis and its aftermath should be an integral part of the understanding of South Korean experience. In the following, various impacts of the crisis and post-crisis 'management' are examined starting with economic cost. After a brief discussion on political consequences of the crisis, the chapter examines various aspects of social cost based on newspaper and magazine articles.

1) Economic Cost

• Losing "national" enterprises

While many South Korean people suffered from economic hardship, the financial crisis offered a good opportunity for foreign companies to acquire Korean companies at a low price. After the debts of Korean companies hit the peak in 1996, several big conglomerates as well as a list of small and mid sized firms started going bankrupt. With the devaluation of the won to a half of its pre-crisis value, this development provided a good opportunity for major foreign companies to take over the bankrupt South Korean companies. In other words, the foreign companies could take over those insolvent companies at a half price or lower as compared to the pre-crisis cost.

Deutsche Bank, which has total assets of $732.5 billion and it ranks first in the world in terms of assets with the 1,566 subsidiaries in Germany and 744 overseas, took over KorAm Bank by purchasing DRs (Depositary Receipts) in the amount of 500 billion won ($437 million) in the spring of 2000. This purchase gives Deutsche Bank a control of 36 percent stake in KorAm Bank. Deutsche Bank will be managing the KorAm Bank hereafter (Kim, January 8, 2000; Kwak, January 10, 2000). This takeover signals only the beginning of the further actions. Banking industry analysts argue, the "Deutsche Bank' move is also likely to speed up the second-round restructuring of the banking industry by prompting domestic banks to merge in order to survive,... Deutsche's advance into the Korean banking scene is likely to increase the momentum for another wave of bank restructuring since many domestic banks will see it as a threat to their existence" (Korea Herald, January 10, 2000)

Another foreign acquisition of a Korean bank indicates a structural shift in Korean economy since it involved Korea First Bank (KFB). This state-sponsored bank has been providing capital needed for national economic development. Most of its clients were Chaebols, but it also provided credits to small and mid sized firms, and even to ordinary people. Also it once was a big employer that absorbed a large number of employees in the country. KFB operated "336 branches across the nation, three overseas offices, two international joint venture firms. It has 4,809 employees, down from over 8,000 before the financial crisis and has a total of 4.5 trillion won in paid-in capital. The total assets of the bank at the end of Oct(ober, 1999) were 32.809 trillion won" (Kim, December 23, 1999).

Korea First Bank was taken over by Newbridge Capital, a US financial institution, in December 1999. KFB received financial infusion and lost management control in the exchange. The South Korean government has to cover the non-performing loans of the bank. In other words, South Korean tax payers take over the non-performing loans which were created by Chaebol's and the rich people. "Newbridge Capital of the United States and the South Korean government closed their deal on the takeover of Korea First Bank (KFB) yesterday, signing a 'definite agreement' for a transfer of the bank's majority 51 percent stake. The deal was priced at 500 billion won (US $420 million) with the bank's capital adequacy ratio expected to improve to 10 percent. The US investors agreed to provide another 200 billion won (US $177 million) over the next two years as bank earnings improve....The Korean government in return committed to offer a two-year guarantee to cover KFB's non-performing loans" (Kim, December 23, 1999).

Another case of the foreign takeover of a prominent South Korean company involves Daewoo Motor which is the largest company belonging the Daewoo Group. While this group was once the second largest Chaebol, its debt level has reached $75 billion in the beginning of 2000 (Lee, February 11, 2000). "Daewoo Motor can produce a total of 1.07 million cars a year at home and has established a wide production network overseas with plants in India, Vietnam, Poland, Romania, Iran, and Egypt, which together make 784,000 vehicles" (USA Today Bloomberg December 5, 1999). Daewoo Motor is about to be sold to one of the biggest carmakers in the world: General Motors, Ford Motor, Daimler-Chrysler, Fiat, or Hyundai. Those five companies submitted the letter of intent to take part in the auction for Daewoo Motor, two of whom will be the final candidates (Burton, March 03, 2000). There are two U.S. companies with strongest intention: General Motors and Ford Motor. Auto-analysts say, "(f)or the US automaker, the acquisition of cash-strapped Daewoo Motor is an easier and less costly way to enter one of the world's 10 biggest auto markets....GM announced its plan to invest in Daewoo Motor in October 1999 as part of its broader strategy in Asia, where it aims to capture 10 percent of the vehicle market by 2005, up from 4.6 percent" (USA Today Bloomberg December 5, 1999). Also, Ford Motor has a strong intention to purchase the bankrupt Daewoo Motor. It is expected that one of the two U.S. automakers can acquire the insolvent Daewoo Motor.

According to a recent report, Hyundai Motor is about to sell 10 percent of its shares to a foreign automobile company. A board member of DaimlerChrysler and a head of Mercedes-Benz announced that "the programme would define the advantages that DaimlerChrysler could gain from its brand portfolio, which has increased this year following the acquisition of 34 per cent of Japan's Mitsubishi Motors and a 10 per cent holding in South Korea's Hyundai Motors" (Burt, 2000). DaimlerChrysler considers expanding its business to not only South Korea but also other Asian markets. This share-taking process of DaimlerChrysler will be the first step to participate in the South Korean auto market without domestic resistance, and then eventually could take over the local automobile company.

In short, the financial crisis led to a number of bankruptcies of not only small and medium-sized firms but also financially troubled Chaebols in South Korea. Insolvent manufacturing companies are being purchased by major foreign, mostly US, companies.

Those businesses once were the symbol of South Korean economic development and industrialization, and they successfully boosted their presence on the world stage with various support rendered by the government. Those companies contributed to South Korean economic development when it took off from an agriculture, fisheries, and forestry centered economy to a heavy and chemical industry based one, to a high technology based economy. However, their contributions and presence become diminished when they are taken over by transnational companies propelled by the objective of global profit making. The financial crisis has offered very good opportunities to these overseas profit-seeking companies to acquire insolvent South Korean companies at a low price. Therefore, this feature explains that state-led, national economic development is over, and signals a start of economic development led by global companies, or development of global companies at the expense of national economies.

- **Currency depreciation and external payment requirement**

Currency depreciation means that a local currency loses its value against the US dollar. As demand for the US dollar increases, the US dollar increases its value and becomes strong, and in turn, local currency gets weaker and loses its value vis-à-vis US dollar (Chossudovsky, 1998). Therefore, people who borrowed foreign capital in US dollars have to repay the amount that they borrowed plus the amount that was added by local currency devaluation. In other words, South Korea came to owe twice the amount of original debt measured in local currency since there was a 200 percent devaluation of the Korean won.

South Korea had over $160 billion debt when the financial crisis occurred. Three months later, the exchange rate jumped up to 200 percent; the Korean won lost half of its value vis-à-vis US dollar. The 1997 currency depreciation devastated the Korean economy because the economy was heavily dependent on imported material and capital whose price was doubled as a result of weakened won. In addition, South Korea had to repay the external debts that amounted over 160 billion dollars. South Korea encountered the most difficult situation when foreign creditors refused to roll over the debts. This led to a severe credit crunch and serial bankruptcies of heavily indebted companies, endangering the Korean national economy. This credit crunch "resulted in mounting bankruptcies – 123 bankruptcies per day in December 1997 and 151 per day in January 1998 – as well as cancellation of investment projects, factory closures, layoffs and wage-cuts, etc. The crisis has had truly devastating effects" (Choi, 1999).

Most Chaebols borrowed too much from overseas before the financial crisis, and then they became unable to pay back. The government of South Korea took over such insolvent debts that should be repaid by the Chaebols. This means that South Korean tax payers became responsible for the debt, although the Chaebols took benefits from the foreign loans that they initially borrowed.

2) Political Consequence

• Union Movements

What makes South Korean union movements unique is that they always protest against the government even when issues do not involve the government directly. It is because the South Korean government had oppressed union movements until the 1980's, providing national security reasons. In fact "the Korean Central Intelligence Agency played a prominent role in selecting leaders in the Federation of Korean Trade Unions" (Deyo, 1987: 189). This is a long-standing tradition because throughout the economic development the government had supported the interest of big businesses, which in turn kept the wages low and exploited their employees. After the financial crisis, union members in the banking and financial industry have protested against the government, demanding that the government stop intervening in their banking affairs. Also they have insisted that the government should not allow the formation of financial holding companies to deal with insolvent banks (Korea Herald, July 11, 2000).

The major issue that union members were concerned about was the possibility of massive lay-offs in the banking and financial industry. The banks and financial institutions have been, in fact, preparing large scale restructuring and downsizing in order to survive, which will immediately affect the life of their employees. Already these sectors eliminated more than 45,000 employees after the crisis (Korea Herald, July 11, 2000). According to the IMF bailout program (see Table IV-1), the banking and other financial sectors should be reformed. Nonviable banks are scheduled to be merged or taken over by domestic or foreign institutions.

- **Criticism on the former government**

As a matter of fact, the financial crisis led to a severe criticism of the former Kim Young Sam government. People believe that the government could have prevented the crisis if it had prepared well or if at least it had managed the crisis well. People suspected that the government and the ruling party were not able to deal with economic matters well. This suspicion aroused among most South Koreans, and changed South Korean voters' perception about the ruling party. At the end of 1997 just after the financial crisis broke out, there was a presidential election in South Korea. People eagerly wanted to elect an able person who would solve the complicated economic and financial problems. As a result, people voted for the head of the other major party who is now president Kim Dae Jung.

It was a long tradition that Koreans usually cast votes for the ruling party. It is well explained from the fact that the ruling party has never been changed since the establishment of the Republic of Korea. However, in the 1997 presidential election, people set their minds on the head of the other major party, who showed possible solutions regarding the financial crisis. His major strength that appealed to people came from not only his liberal economic policies, as opposed to traditional state-led management, but also his platform concerning the unification of the two Koreas. In short, the financial crisis led South Koreans to place more importance on economic and practical issues rather than political issues as before. Eventually, the ruling party failed to keep the presidency.

3) Social Cost

• Increase in suicide rate

The most telling indicator of the severity of the situation in South Korea following the financial crisis and IMF intervention is the statistics on suicide. According to a Lancet (Watts, 1998) article issued in the fall of 1998, 36 South Koreans killed themselves every day after the crisis. It can be inferred from the statistics that more than 13,000 people committed suicide in one year after the crisis. After the crisis began, the suicide rate increased by 41.1% in 1998 from the year before (National Statistics Office, Republic of Korea, "98 Nyun Samang Wonin Tonggye": translated into "Statistics of Causes of Death in 1998").

In addition to those who committed suicide, it is not difficult to imagine that numerous people have suffered from physical and emotional difficulties as a result of the crisis. The potential causes of death that could have been inflicted by the crisis include septicemia or blood poisoning, heart attack, and diabetes (National Statistics Office, Republic of Korea, "98 Nyun Samang Wonin Tonggye": translated into "Statistics of Causes of Death in 1998"). It is because the pattern of people's life has changed in the struggle for their everyday lives. They were more exposed to the dangerous work environment that they would not have had had it not been for the crisis. In addition, people became more stressed to keep their jobs under increased risk of losing their jobs. In short, the crisis not only caused economic hardships to people but also brought death and deterioration of health among the general public. The crisis has changed the circumstances of the lives of ordinary people because they need to work longer and harder in order to sustain their everyday lives.

• **Wealth polarization**

The financial crisis of South Korea expanded the income gap between the rich and the poor. The income gap between the households with 550,000 won[9] or less monthly income (about 3.7 percent of all households) and the households with 4,950,000 won or more monthly income (2.4 percent) sharply increased from 6,200,000 won in 1997 to 9,880,000 won in 1998. In other words, the gap has increased by more than 50 percent

(Lim, November 19, 1998). In a conference called "Poverty Forum" held in Seoul in November 1999 (Jun, November 11, 1999), a professor argued that the household income at the bottom 60 percent of population had declined in 1998, while the household income at the top 20 percent had increased after the 1997 financial crisis.

The salary or wage of the workers in all the industries shrank by 1.9 percent by the end of August 1998 from the same period of 1997. In the same period, the salary for high-income earners jumped up by 4.8 percent while the wage of low-income workers dropped by 16.9 percent. It means that blue-collar workers' income greatly diminished even though that of white-collar workers' went up in the same period. Since generally blue-collar workers in Korea do not have better education than white-collar counterpart, those educated get better chances for secure jobs, higher income and privileges despite the financial crisis.

Furthermore, the founders and/or heads of the top 10 Chaebol groups became much more powerful after the crisis as they strengthened their control over affiliates, subsidiaries, and suppliers. Their stock shares over their companies increased from 19.95 percent before the crisis to 28.73 percent after the crisis according to a report of the Korea Stock Exchange (Yonhap News, September 13, 1999; Ye & Han, September 13, 1999).

In spite of the fact that the financial crisis hit all aspects of Korean society hard, the heads or owners of Chaebols have rather strengthened their controlling power over their businesses. It is evident that the crisis helped the owners of Chaebols increase their shareholdings in order to control their businesses effectively during the crisis period without public criticism. The Korea Stock Exchange (KSE) revealed its research results for the shift of the shareholdings regarding 91 listed companies, comparing two points of

[9] 550,000 won of Korean Currency values approximately $733 CAD, when 750 won is exchanged to $1.

time: January 1, 1998 and August 31, 1998. The individual ownerships of the owners of the top ten Chaebols, that is, Hyundai, Daewoo, Samsung, LG, SK, Hanjin, Ssangyong, Hanwha, Kumho, and Lotte, have increased although the average shareholding of the controlling owners fell to 2.82 percent as of the end of August from 3.22 percent at the beginning of 1998. When the individual shareholdings, including family and cross subsidiary members, are all put together, the ratio sharply jumps up to 34.60 percent, which is remarkable growth as compared to the January ratio of 27.23 (Yonhap News, September 13, 1999).

Income and wealth inequality worsened partly due to unequal distribution of interest income. When interest rates soared up to around 30 percent at the end of March 1998, there were about 18,000 or so individual bank accounts in South Korea which had over $400,000, totaling $21.7 billion (Lim, November 19, 1998). It can be inferred from that statistics that the owners of those accounts, a handful of wealthy Korean households, made $4.3 billion[10] of return from the interest in a single year.

Moreover the government has experienced a decrease in tax collected since the financial crisis. This situation stimulated the government to change its tax policy to increase indirect tax such as transportation tax in order to compensate for revenue loss. The income gap between the rich and the poor has been widened (SERI, 1998) because the government has practiced policies such as the exemption of value-added tax for professionals, decrease in real estate tax, and long-term bond issues without indication of owner's name (Kim, July 20, 1999). According to the same newspaper mentioned above, the burden of income and consumption taxes for the top ten percent of the urban

[10] The exchange rate reflects that US 1 dollar is exchanged to Korean 1,150 Won in this thesis hereafter.

households stayed about the same, but that of the bottom ten percent increased by 200 percent, in 1998 from the previous year.

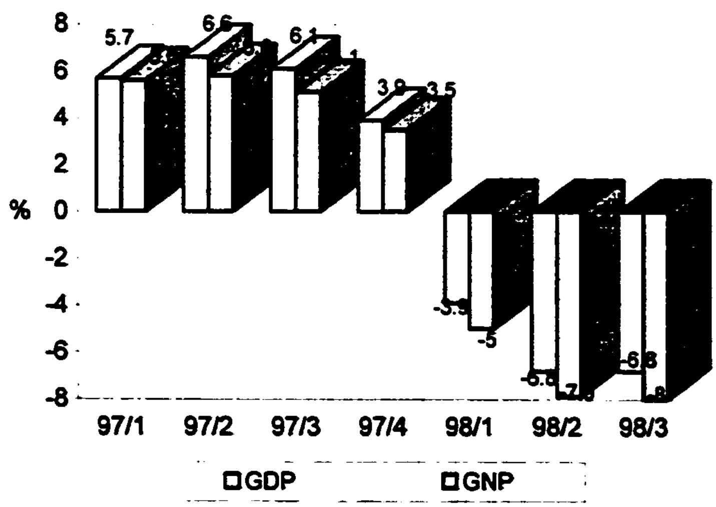
Import statistics also showed that wealth polarization is intensifying. According to the Korea Customs Office, imports of 20 luxury, non-productive goods increased by 65.7 million dollars during January 1999, a 38.2 percent increase from the year before. Those items include golf gears, cars, cigarettes, perfume, ski gears, health food, and so forth. In contrast, retail goods such as food and drink that are more likely to be consumed by common people shrank by 22.0 percent in January 1999. Furthermore, the sales of home electronics and appliances decreased by 19.0 percent in January 1999, compared to the month before (Hankyoreh Newspaper, February 14, 1999).

The rich have had a very good opportunity to accumulate their wealth during the financial crisis. The high interest rates in 1998 and the soaring stock prices in 1999 brought them an astounding opportunity for wealth accumulation. In short, the wealthy made more fortunes even in the middle of the financial crisis while the poor suffered from income reduction, job loss, tax increase, and resulting financial difficulties.

• Deterioration in living standard

After two years of hardship since the crisis, many economists and scholars, including those at the IMF, insisted that the South Korean economy was recovering. They even go on to praise South Korea as being the most successful case among the crisis-hit countries, saying that the South Korean GDP is showing signs of recovery (Park, March 13, 1999). Figure IV-1 summarizes the growth rates of GDP, an indicator of national production, and GNP, an indicator of national income (quarterly figure converted to annual equivalent) in the crisis and post-crisis periods. In fact, the negative GDP growth rate shows a sign of leveling off around –6.6%. However, the growth rate of GNP continued to fall to –8% in the third quarter of 1998. The gap between GDP and GNP corresponds to what the foreigners earned from South Korea, or the profits and interest earned by the foreign investors. With the huge burden of external debt, even when GDP shows the sign of recovery and growth, the living standards of South Korean people as measured by GNP keeps deteriorating. Therefore, the "recovery" under the IMF policy of heavy external debt and austere domestic structural adjustment needs to be reexamined carefully before interpreting it to be a positive development.

<Figure IV-1> GDP and GNP Growth Rates, First Quarter 1997-Third Quarter 1998



Note: The horizontal axis indicates years and quarters.
Source: Ministry of Finance and Economy, Republic of Korea.

• **Broken families**

One of the results of the financial crisis has been the rising number of broken families in South Korea. According to a report on September 22, 1998, by the Ministry of Health and Welfare of South Korea, there were 6,353 children of the age of 17 or less who needed public care throughout the country. Some 884 of them were abandoned in the first half of the year, an increase of 203 from 681 a year before. In particular, 2,045 children were sent to care facilities during the first half of 1998 by single mothers and broken families as compared to 826 in the first half of 1997 before the financial crisis occurred (Lee, September 22, 1998).

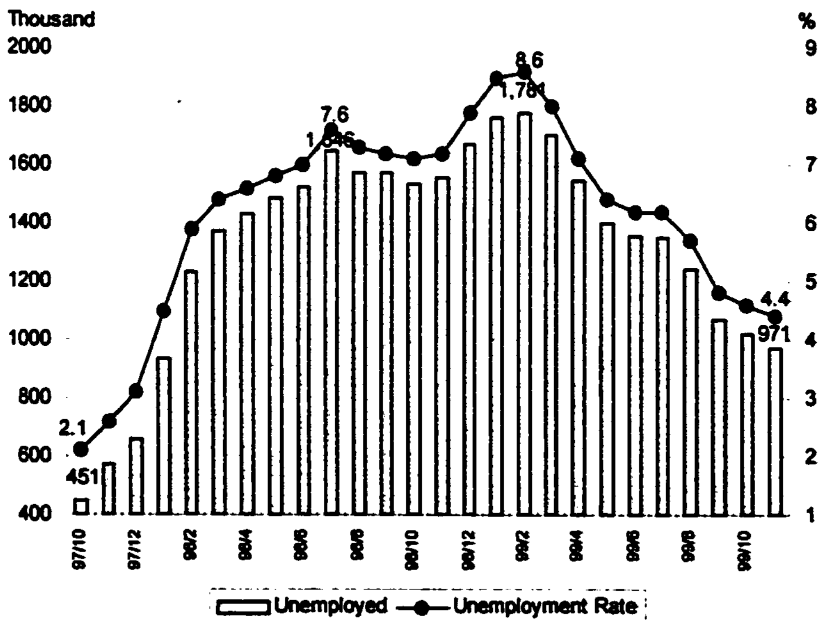
According to another report (Lee, October 8, 1998), women with low income in particular have suffered. Welfare facilities for women had housed 3,353 women by the end of June 1998. This figure is alarming when compared to 3, 000 at the end of 1996 and 3,137 at the end of 1997. 137 people increased for one year from the end of 1996 to that of 1997, but the number jumped to 216 for the only 6 months from the end of 1997 to June 1998. This number increased especially at the end of 1997 and in 1998 as a result of the financial crisis. The newspaper report explains that women alone who do not have enough income for living are sent to the facilities.

In short, the weakest people in South Korea, mostly women and children, from homes with insufficient income for living have suffered more as a result of the crisis, even though the rich have enjoyed making more income in the same process. In the long run, this phenomenon will make income distribution more unequal, produce more broken families, and weaken the national economy.

• **Increase in unemployment**

Another important indicator of the severity of the South Korean crisis is the unemployment rate. Figure IV-2 summarizes month-to-month movement in the number of unemployed and the unemployment rate. From November of 1997 there occurred a sharp rise in the number and rate of unemployment until July of 1998, and after six months of "stability" at a high rate and number, they soared again until February 1999. In that month, the unemployment rate reached 8.7 percent, and 1,785,000 people were unemployed.

<Figure IV-2> Number of the Unemployed and the Rate of Unemployment



Source: 1) Juyo Kyongje Jipyo (Major Economic Index), September 1999. Ministry of Finance and Economy
2) Korea Economic Update, October 2, 1999. Ministry of Finance and Economy

As compared to the pre-crisis levels in October of 1997, the unemployment rate tripled and the number of unemployed increased more than four fold in a short 14 months period. Since February of 1999, the rate and number of unemployment dropped to 5.7% and 1,220,000 in August, but the unemployment problem is far from being solved. The rate and number of unemployed are still nearly three times as high as those in the pre-crisis period.

The rate of unemployment at the level of 9% may not sound such an alarming figure in many Western countries. However, social consequences of unemployment in South Korea create quite a serious problem. This is due to the absence of an open labor market, the practice of recruiting mostly those who are freshly entering the job market, and serious discrimination based on age, schooling, and gender. For instance, major corporations recruit mainly the male university graduate of age 27 or 28 who has already completed compulsory military service. In addition, mid-career job-hopping is severely penalized because of limited job openings and significant decline in personal earnings, social standing, and prestige. Such rigidity in the labor market magnifies the negative implication of being unemployed. In a sense, unemployment means "death" to the Korean people, and this is not simply a metaphor as indicated by the jump in suicide rate mentioned earlier. Losing a job brings shame not only to the worker but also to his family, and therefore a good number of unemployed people do not even tell their family the fact that they are being laid off. Therefore, a 6 or 9 percent unemployment rate indicates a graver social problem in Korea than the same rate would bring in countries like Canada or the USA.

In addition, it is necessary to take into account how the unemployed are composed. Out of those unemployed at the end of August 1998, full time workers accounted for 21.9 percent while temporary and daily employed workers accounted for

63 percent (Lim, November 19, 1998). The temporary and daily workers in Korea have low income, and their lives are quite unstable. Therefore, a high unemployment rate among these people indicates a grave social problem. Also, the economic hardship of such people widened the true income gap between the poor and the rich.

As the above analysis indicates, the people of South Korea suffered from various problems in economic, political, and social life. As a result of the crisis, many ordinary people lost their jobs, livelihood, health, and even lives. The government of South Korea and the working people of South Korea became heavily indebted, South Korean corporations were bought up by the major Western corporations, and South Korea is left with little sovereignty in economic affairs.

In short, the South Korean financial crisis has brought a lot of social, economic, and political consequences. In particular, ordinary people have suffered from social and economic hardships. The biggest victim of the financial crisis must be weak people such as single mothers without enough income to live, children from broken families, and the unemployed (Lee and Rhee, 1998). They were not involved in the big money making process directly but are obvious victims of the crisis. Those problems that were brought about by the financial crisis make people more difficult to resolve because the government has pursued the growth-first strategy and globalization. The government did not take much care of its own people but of Chaebols and the overseas markets. The government did not pay much attention to its people, and forced people to pay for its policy failure. Now is the time for the government and the people to reevaluate a possible strategy that benefits the entire population.

V. Conclusion and Policy Implication

The South Korean financial crisis in 1997 brought the people of South Korea incalculable amount of suffering. Many people committed suicide due to economic hardship, shame of job loss, absence of hope, and the like. Nowadays even a university degree does not guarantee a decent job, unlike in the pre-crisis period when such a degree meant enormous prestige. The lifestyle of the "average" person has changed completely. They work harder and longer for much less reward. Their fate is in stark contrast to that of the rich who accumulated wealth before, during, and after the crisis. The living standard of ordinary people dropped to the same level as that of the early 1990's. Every social problem in Korea today appears to be the result of the 1997 financial crisis. However, the roots of the present day situation were sown in earlier periods of economic development. After characterizing South Korean experience in the past, this chapter concludes with a suggestion of alternative images of the future of Korea.

Presently South Koreans are suffering from the fallout of the crisis, and their economic performance is not improving even after the implementation of the IMF bailout program. The KOSPI (Korea Composite Stock Price Index) indicator of economic performance is running far below the desirable level. Furthermore, the South Korean economy is extremely vulnerable to external shocks because it heavily depends on primary materials from which final products can be produced as well as on exports to other economies. This means that the Korean economy will experience trouble if there are price turbulences or trade barriers in overseas markets. The Korean economy is woven complexly into the global market system without a suitable buffer that can absorb external shocks. Moreover, the market system in South Korea is not working properly because the economy is forced to transform into US-like capitalism when in fact its background is so different from that of the US.

In the current era of globalization, most countries are forced to take the path of a corporate-led, market-oriented economy. If they do not follow the path of liberalization and deregulation, they will be left behind. This is precisely why almost all the countries of the world are opening their markets, using the degree of deregulation and liberalization as the gauge of openness. This trend has been initiated and accelerated mostly by the governments of major developed countries, especially the US. The US government is pushed by major global corporations that are eager to make more overseas profit to overcome the limit of profit-making opportunities within the boundary of their own countries.

As with other countries, South Korea itself has pursued liberalization, deregulation, the opening of their economy, and especially the opening of the financial market since the 1980's, with the most rapid activity having been concentrated in the 1990's. This globalization effort and the US policy changes that are directly related to the crisis have taken place since the early 1990's when the Kim Young Sam government decided to give up state-led economic development and the protected domestic economic system in favor of the strategy of globalization, or opening the heretofore protected domestic market. The financial crisis was caused by the financial liberalization that was forced by the US but welcomed by the South Korean government and big business. It becomes clear that there have been three major parties which have played a critical role in opening the South Korean financial market and pursuing globalization: the US, the South

Korean government, and Chaebols. Ordinary South Koreans have not benefited from those processes but suffered from the results of the crisis.

During the crisis, the Korean government asked the IMF for a rescue package, which was the largest in the history of the IMF. The IMF has pressured South Korea to open its domestic markets to foreign competition, partly using the liberalization schedule imposed by the WTO and the GATT Uruguay Round. South Korea partially lost its sovereignty to make its own decisions on national budget, economic and social policies, and political activities. To make decisions on those activities, the government must obtain approval from the IMF. In other words, South Korea was dominated by the US neocolonial capitalism that raids foreign economies to make more profit and to boost its hegemony worldwide. The South Korean national economy that was once highly praised by the World Bank as well as by other economists and scholars is now lifeless, and there is no hope to revive it to the level it was at previously. Indeed the state-led and export-oriented national economic development, which was called "an Asian miracle", died in South Korea (Arrighi, at. all, 1993). After the crisis, the government became weaker; the average person has suffered and the Chaebols have been absorbed into global corporate networks. No longer would there be the glory of the miracle of a state-led economic development in South Korea, but rather that of globally surviving Chaebols that are now free from government control.

South Korea now faces many social, economic, political, and cultural problems, all stemming from the structural problems of society. Those problems have existed even before the crisis. There have been many accidents that indicate the weakness of the South Korean infrastructure such as the breakdown of the Sungsoo Dae Kyo (a bridge) in

1994, the collapse of the Sampoong Department Store in 1995, the gas explosion of a Taekoo Subway construction area in 1996, and the conflagration of Hwasung camp ground in 1999. Each of these accidents claimed the lives of many people. These accidents may signify the crisis in all aspects of South Korean society. The 1997 South Korean financial crisis is just one example of many problems. Those problems have resulted from the export-led economic development strategy that was pursued by sacrificing the living standard of ordinary people. Construction companies took greater care in constructing buildings and bridges overseas in order to win a global reputation at the expense of local infrastructure construction. Manufacturing and service companies did the same thing. Their interest lay in overseas markets for export earnings, even when it required sacrificing domestic consumers. The more they sold overseas, the more they earned the government's confidence, and the more support they received from the government. As a result, the major Korean companies had easy access to cheap financing and had more opportunities to make a profit from their business not only in the country but also overseas. The government also helped these companies by keeping wages low.

Now South Korea stands at a crossroad between the road to national economic development and the road to full globalization led by global companies. Judging from the trend that South Korea has followed so far, it will go further toward full globalization. What kind of benefits does the average person get from globalization? The lesson learned from the 1997 South Korean financial crisis was that full globalization does not bring a higher standard of living to ordinary South Koreans, only to the rich, Chaebols, and global companies. Therefore, it is the time for people to carefully reevaluate the Korean economy, society, and globalization. Is South Korea on the right track to help the majority of its population in the improvement of their living standard and to be happy with hope for the future? South Korea cannot stand alone against globalization because it is a trend strongly pursued not only by the US but also by other developed countries. However, there are some ways to cope with the powerful force of globalization. What South Korea can do to prepare for globalization can be categorized into several areas.

Firstly, South Korea should not depend on external markets too much in order to buffer shocks from overseas markets. In other words, South Korea should make the local market larger through developing the domestic demand that is not affected much by the overseas market. Domestic or local market development seems to stand in opposition to globalization. However, over a long period of time, globalization may not be worthwhile since it does not guarantee a quality life for local people, but rather serves the interests of Chaebols and global corporations. When local people attain a high standard of living, globalization becomes worthwhile. Contemporary globalization gives Chaebols and transnational corporations good opportunities to have free access to overseas financial markets and to further accumulate their wealth in the domestic and overseas markets. If they eventually run into trouble, the government will bail them out because of their critical role in the national economy. Nevertheless, their output would not go to the people who struggled to bail them out but in turn would go back to the owners of Chaebols, when they finally do recover and make profit.

Secondly, the reunification of the two Koreas is very important for ordinary Koreans in both South and North Korea, although reunification would be very costly. When the two countries reunify, the combined market size will be larger, and there will be an inexpensive labor force available in the North. The population of South Korea is

45 million people, and 25 million people live in North Korea. If the domestic market becomes larger, the dependence on overseas markets will be reduced. It will help Korea buffer external shocks and it will not be as vulnerable as it was previously. Also, both Koreas can produce products in the North and export them to countries such as China or elsewhere after satisfying the domestic demand. Most of all, reunification will prompt the local economic development that ordinary Koreans can take part in, and this would become one of the mechanisms that stand against corporate-led globalization. Moreover, North Koreans will have access to South Korean high technology to increase agricultural output. As a result, North Koreans would be able to survive the famine that has prevailed throughout the 1990's. Reunification will give both countries a chance to share their strong points; that is, economic strength in South Korea and strong national identity in North Korea. Thus, reunification may offer a chance to regain the sovereignty that South Korea has lost for the last half century.

Furthermore, reunification allows the people of the Korean peninsula a freedom from any foreign power for the first time in more than one hundred years. Just as the US could change its policy toward South Korea after the fall of communism, the Koreans may be able to abandon their policy of US dependency. The US has reasons why it stations its troops in South Korea in that it prevents the spread of North Korean communism and socialism. The US insists that it is concerned about the defense matter of South Korea, which is kind of a military deterrence system. Therefore, reunification could make the US have no reason to poise their troops in South Korea, and give up the military globalization policy. In the long run, people of the two Koreas will obtain true independence.

Most of all, reunification is only natural because the countries were divided not by Koreans themselves but by overseas powers. Many families and relatives have not seen each other for 50 years, and they do not even know if their relatives are still alive. This must be one of the greatest tragedies in human history. In order to end this hardship reunification should be brought about as soon as possible. In the long run, the living standard of ordinary people will increase in both regions. As the first step toward reunification, a confederation[11] of the two governments would be formed. It is practical and reasonable since it serves the interests of both countries, but does not require huge sacrifice on either part.

Thirdly, the South Korean government should invest in education, health care, and social development in order to help the entire population become strong both mentally and economically. These factors are of fundamental importance if the whole population is to have a quality of life. If the government ignores investment in these areas, there can be no improvement in the living standard. After the financial crisis, every aspect of society has been infected with disease, and the government has not to date produced comprehensive treatment. These factors are "invisible" infrastructures that may help people establish a solid foundation to improve their living standard and to cope with greater globalization and liberalization.

In addition, the government should support small and medium-sized firms rather than Chaebols. This will change the structure of the South Korean economy that has thus far been composed mostly of a few Chaebols[12] to a system that can support local

[11] Both heads of state of the two Koreas agreed in principle to this first step toward reunification during the June 2000 summit although the details have yet to be worked out.

[12] More than 82 percent of GNP of South Korea was produced by the top 30 chaebols in 1994 and 54 percent by the top 5 chaebols (Samsung, Daewoo, Hyundae, LG, and Hanjin) in the same year (Jang

businesses which are founded for the local people. This system will improve the living standard of most local people. It will make the local economy stronger to protect people against an event such as the 1997 financial crisis. Another important issue in South Korea is the distribution of wealth. If the government keeps collectively supporting big businesses or Chaebols as it did, there will be more distortion of income distribution and an extreme wealth polarization. These policies would mark a departure from the Chaebol-centered, rich people-oriented development policy for the first time.

The IMF has been working hard to root out crony capitalism, corruption of the government, and the high volume of debt of Chaebols in South Korea since the financial crisis. The IMF seems to be making South Korea another American capital market in East Asia that will be favorable for their global companies in seeking profit overseas. However, the more the IMF tries to drive South Korea along the path of American standardization, which they think is good, the more the South Korean economy will run into trouble and the South Korean people will lose their dignity, self-confidence, and pride in their national identity. If the IMF really wants to help financially troubled countries such as South Korea, it should not exert such brutal power over these countries and should not treat all countries with the same measures. It should reexamine the philosophies upon which it was founded. If the IMF truly wants to help South Korea recover, it should stop imposing such harsh mechanisms to open up the market, and should help South Korea restore its sovereignty.

The primary characteristic of South Korean economic development over the last half century could be described as a "dependence-prone economy", which means that the

Myung Kook's column in Naeilshinmoon, #76, April 12, 1995).

Korean economy tends to be dependent on other big economies such as the US and Japan. This dependency is not clearly recognized however, because it is obscured by the large volume of exports and the dynamic overseas activities of Chaebols. Further, the term "dependence-prone economy" implies that Korean economic development was based on foreign debt. From a long-term perspective, the 20th century was a lost century for South Korea since the country was colonized and deprived of sovereignty in the first half of the century, and it lost economic sovereignty at the end of the century to the US and global institutions. It is time for South Koreans to regain their sovereignty and become truly independent. Now is the time when the US and other powers as well as the IMF should endeavor to assist South Korea in achieving this goal.

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