HEGEMONIC IDEAS VERSUS INSTITUTIONAL ETHOS IN KOREA'S NEOLIBERAL REFORM DURING THE LATE 1990S ECONOMIC CRISIS

by

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A Dissertation submitted to the

Graduate School-New Brunswick

Rutgers, The State University of New Jersey

In partial fulfillment of the requirements

For the degree of

Doctor of Philosophy

Graduate Program in Sociology

Written under the direction of

Tom Rudel

And approved by

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New Brunswick, New Jersey

OCTOBER, 2013

ABSTRACT OF THE DISSERTATION

Hegemonic Ideas versus Institutional Ethos in Korea's Neoliberal Reform during the Late 1990s Economic Crisis

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This study uses the historical case of the late 1990s economic crisis in Korea to explore the encounter between exogenous neoliberal doctrines and the endogenous "developmental" policy ethos. It investigates to what extent the neoliberal policy frame was institutionalized to change the developmental regulatory structure. The discourse of "moral hazard" mediated the acceptance of the harsh International Monetary Fund programs in such a way that neoliberal norms were espoused as the legitimate tools to cure "inefficient" developmental policy arrangements. The far-reaching restructuring aimed to make the system conform to the Western market economy model and was guided by major reform agendas such as small government, fiscal austerity, bank autonomy, strict capital adequacy, corporate transparency, capital liberalization, and labor flexibility.

Tracing the implementation of these agendas revealed two primary contexts for incomplete neoliberal transition under the developmental institutional legacies. First, pragmatic policy orientation framed market adjustment as a national project, empowering the government to achieve immediate economic and political stability. Financial reform to build market discipline led to more integrated authority and expanded the domains of supervision by the government. Pursuing small-government reform failed due to the organizational culture and strong policy leadership of the closed, rank-based bureaucracy. Second, the political and economic incentives to protect major large conglomerates (*chaebols*) and organized labor compromised the market adjustments. Reforming the structures and practices of the *chaebols* was limited because they were still the core players in the Korean economy. The initiative to promote labor flexibility deepened labor market segmentation, widening the gap among workers by firm size and unionization. The agenda of capital liberalization led to the successful implementation by making financial institutions more susceptible to the growing influence of foreign shareholders and investors. The Korean experience shows that highly legitimate neoliberal values in the policy discourse were rearticulated, compromised, or abandoned within the local policy institutions. The post-crisis reform entailed excessive government intrusion and the mobilization of passive private sectors with the persistence of the enduring developmental ethos to guide the government-market relationship.

Acknowledgements

I have been thinking about writing a dissertation about the gap between ideas and practices for years. I recently took the first step in my intellectual journey, which would not have been possible without the support and friendship of numerous people. My biggest debt is to my advisor, Tom Rudel. He has been my attentive listener, enthusiastic reader, and generous mentor, guiding my work in a graceful and efficient manner. Catherine Lee showed her trust in my work at critical moments when I felt intellectually vulnerable. Patricia Roos offered constructive and valuable feedback and constant encouragement. I would like to thank Yoon-Kyung Lee at Binghamton University. She has been a model scholar and I want to emulate her in my future career.

I thank Paul McLean and Sarah Rosenfield for their reading of and advising on my first published article. I have also learnt tremendously from my teaching experiences with Elizabeth Mitchell, Eleanor LaPointe, and Jeff Wilhelms. I would like to express my gratitude to Dianne Yarnell for her excellent service and warm support.

My life at Rutgers has been enriched by friendships with fellow graduate students. I would like to thank Chigusa Yamaura, Eiko Saeki, Eun-Kyung Song, Kirsten Song, Na-Mi Shin, Shruti Devgan, Neha Gondal, Benny Nuriel, Vikash Sing, Shin-Cha Park, Yusheng Lin, and Ghassan Moussawi. My gratitude goes to my close friends, Sheena, Shang-Eung, John, and Taeun; their friendship helped me survive living away from home for years.

I especially want to thank my family in Korea. I've always counted on the big hearts of my siblings, Eun-Jung and Oh-Sung. Hae-June, the coolest and sweetest person I know, has energized my days in magical ways. Finally, I would like to thank my parents,

Young-Jae Kwon and Young-Hee Kim, who taught me the values of optimism and patience. It is to them that this work is dedicated.

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CHAPTER 1

HEGEMONIC IDEAS AND INSTITUTIONAL ETHOS IN REFORM POLITICS

This study examines the dynamics of post-crisis reform in Korea after the late 1990s financial crisis to better understand the interaction between neoliberal ideas and "the developmental state" institutions. I analyze the processes of financial, corporate, and labor reforms, focusing on a tension between externally imposed neoliberal ideas and Korea's enduring developmental policy ethos. The latter had cultivated a set of policy arrangements and tools geared for high economic growth that contradict neoliberal doctrines. When the crisis hit the country, the preexisting policy framework was severely problematized and the neoliberal policy prescriptions from the IMF became the hegemonic policy framework. In the midst of ideological and political momentum for change, what made neoliberal ideas hegemonic during the crisis? How did neoliberal doctrines challenge the developmental policy ethos and to what extent did they replace them? In what ways did the developmental inertia compromise the newly imposed policy goals? Answering these questions should clarify our understanding of "neoliberal transitions" as the processes in which ideational hegemony and institutional inertia constantly interact to generate unique policy outcomes across countries.

1. The Crisis and the Hegemony of Neoliberal Ideas

1.1 The crisis, social dislocations and the IMF programs

The 1997 economic crisis is seen as the greatest disaster since the Korean War in terms of the scale of damages inflicted on people's lives. Until the financial crisis, Korea's macroeconomic performance had been favorable. As of 1996, the annual economic growth rate was 7%, unemployment rate was 3% and the central government debt amounted only 6.8% of GDP, much lower than other OECD countries: U.S. 69.7%, U.K. 50.4%, Germany 20.7% (Lee, K.S. 2011). The crisis came when Korea was a new OECD member with $11,235 of GDP per capita in 1997. After a long and constant record of successful economic performances, the massive and sudden collapse shocked the public and puzzled observers. What exposed the economy to such a collapse? Even top policy makers didn't expect the spectacular crisis and hardly imagined that they would have to ask for an IMF bail-out. The International Monetary Fund (IMF) organized rescue funds of $57 billion, the largest bailout program, to date, in IMF history.

In return, the IMF imposed policy prescriptions that were seen as almost "insulting" and "overkill" for an economy that had sound economic conditions just months earlier (Sachs 1997). Korea had to pursue a modest growth rate with hard controls on inflation. The most destructive requirement was a high interest rate policy. The money market rate, which was about 12% before the crisis, more than doubled to about 27-30 % during December 1997 (IMF 1998a). Even financially sound firms could not cope with such drastic increases in costs. This severe credit crunch generated endless corporate bankruptcies. One and a half million people lost their jobs during one single year of 1998 and about three-fourth of households experienced income reduction by an average of 44.2%. The divorce rate right after the crisis, January to September 1998, increased by 34.5 percent over the previous year (Choi and Chung 2002). Increasing inequality was the most critical long-term effect of the IMF regime. Korea's relatively sound income distribution deteriorated, with the Gini index increasing from 0.29 in 1997 to 0.31 in 1999 (Lim and Jang 2006). These negative consequences were not surprising given that the IMF conditionality imposed on Korea was much stricter than the conditionalities imposed on other countries (Feldstein 1998). The contents and intensity of the IMF programs were decoupled from the local context and caused Korea to carry out unnecessary and costly policy changes (Sachs 1997).

The crisis blame game had no winner but clear losers. Top policy makers, including President Kim Young Sam, were bashed for their poor crisis management (NA: Special Committee, January 27,1999). The U.S. and foreign investors were accused of profiting from high interest rates from the devastated Asian financial market. However, it was the developmental nexus among government, bank, and big conglomerates (*chaebols*) that became the main target of criticism. To be specific, the government guaranteed the liabilities of financial intermediaries which encouraged risky over-investment. This practice revealed a serious moral hazard problem in the economy (Krugman 1998).[1] The Korean economy began to be framed as a defective system that deviates from universal market discipline, not as a mere local idiosyncrasy. In particular, the developmental strategy to favor key industries and firms began to be problematized as discouraging fair competition and strict risk management in market. This attack on domestic institutions was the official stance of the IMF and widely shared by opinion leaders in Korea. Michel Camdessus, the then IMF managing director, envisioned the Korean crisis as a "blessing in disguise" in that only crisis could make a fundamental

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[1] The concept of *moral hazard* was derived from finance. It refers to over-borrowing or excessive risk-taking activities motivated by an insured position. Concerning government bailouts, troubled firms are seen as rewarded for their bad behavior.

restructuring happen. That would eventually strengthen the economy after painful adjustments (IMF 1998b). The IMF insisted that its mission for Korea should aim for far-reaching institutional changes to make the entire system conform more closely to the Western model.

Massive structural reforms aimed at replacing the excessive government control with a market mechanism. The IMF set the guidelines to make the financial and corporate sectors more profit-oriented, streamlined in operations and staffs, and open to foreign investors. The newly launched Kim Dae-Jung administration planned even more intensive restructuring plans than those suggested by the IMF. Banks consolidated branches to shed their staffs, and foreign participation in banking almost tripled since 1996. The government enforced strict capital adequacy on banks and firms to make them financially accountable. It also closed down or suspended a total of 171 financial institutions by 1999 during the massive restructuring (Jwa and Yi 2001). The government granted exclusive advantages to foreign investors expecting that their participation would upgrade the economy by bringing global standards with them.

The IMF and the creditor countries explicitly demanded that the government dismantle labor rigidity. Labor flexibility was required for facilitating the mergers, acquisitions, downsizing, and bankruptcies associated with the IMF restructuring. The neoliberal rationale assumed that flexible labor would promote the efficient use of labor force and maximize production and employment. The labor reform in 1998 legalized collective layoffs and the use of dispatched workers and substitute labor during strikes.[2] The government tried to send creditors and investors a message that Korea was fully committed to restructuring, repaying its debts, and building a favorable environment for investors. However, its ambitious reform plans did not directly lead to improving the national credit rating. The rating moved upward twice only when two major Korean banks were to be acquired by foreign banks for fire sale prices with the aid of government's public funds.

1.2 Hegemonic ideas of neoliberalism and institutional ethos of developmentalism

The power of ideas in policy shifts has been an important subject for discussion about neoliberal transitions. This ideational approach differentiates periods of exceptional policy making from those of normal policy making. During normal times, policy paradigm remains largely unchallenged and only incremental changes occur. But in times of crisis, the existing policy paradigms are disapproved and possible policy options are reconfigured. A crisis not only destabilizes policy field but also promotes collective action to resolve uncertainty. Policy actors are desperately seeking an authoritative diagnosis of what constitutes the crisis and “road maps” to guide which policy change should occur to secure their political legitimacy (Goldstein 1993; Hay 2001; Blyth 2002). Accordingly, in periods of transformation, highly articulated, explicit, and organized ideological systems emerge with new strategies of action (Swidler 1986).

[2] "Dispatched worker" is employed by an employer and engaged in work for another person under the instruction of the latter, while his or her employment relationship is maintained with the former.

During the last decades of the 20th century, a set of economic ideas called "neoliberalism" came to be seen as the most legitimate frameworks for perceiving an economy. Neoliberalism has its roots in the *doux commerce* thesis in the eighteenth century that sees market as a civilizing force: market relations make people more gracious and less hostile to each other (Hirschman 1977). Based on Adam Smith's doctrine of invisible hand, liberalism assumes that competitive markets yield the best possible arrangements for satisfying individual needs and achieving efficient resources allocation. Thus, government interventions to favor particular players distort efficient market operations. Originally incubated in Europe during the interwar period, neoliberalism was more refined as a philosophy of free markets by the Chicago school in the United States. Its contemporary political and economic formulations were set under the regimes of Reagan and Thatcher during the 1980s. In its most abstract form, neoliberalism advocates fiscal austerity by public spending reduction, deregulation of currency and investment for deeper integration into world trading, privatization to insure government retreat from market, and arrangement of compensatory social safety nets to counteract increasing inequality from market adjustments (Fourcade and Healy 2007; Unger 1988).

Clear and coherent neoliberal ideas become more appealing during times of high economic uncertainty (Fourcade-Gourinchas and Babb 2002; Campbell and Peterson 2001). The adoption of neoliberal policy prescriptions were often precipitated by an acute economic crises that created a sudden enthusiasm for a realization of a new policy paradigm. In the 1980s, a neoliberal view emerged as hegemonic ideas in Britain. It became a dominant *policy paradigm* that suggests “the hierarchy of goals and set of instruments employed to guide policy" (Hall 1993, 284). The neoliberal policy paradigm was articulated in response to the Keynesian institutional legacies such as rising government spending and inflation. Its capacity to problematize the pre-existing policy paradigm constitutes the critical strength of hegemonic ideas. Prime Minister Thatcher used Monetarism as a policy weapon in her battle against Keynesian politics.

The IMF has played a critical role in diffusing neoliberal policy prescriptions. The countries in economic crisis had to appease the IMF, U.S. and global investors. To domestic policymakers, the IMF's diagnoses and prescriptions based on the *Washington Consensus*[3] provided the optimistic vision that only the short-term pain of adjustment is required for recovery and sustainable growth (Woods 1995). The IMF approached economic crises as the symptom of the problems whose fundamental cause lies in high absorption of resources by excessive consumption and investment relative to the growth of real gross national product (Polak 1997). Therefore, the IMF usually imposes stabilizing programs that promote high interest rates and cut public expenditure. All of these measures should restore the balance between production and consumption.

Domestic political factors are critical in determining the legitimacy of the IMF programs imposed. The dominance of neoliberal elites and technocrats who shared the IMF mindset facilitated neoliberal reforms in the Latin American countries. The public and politicians in the post-communist European countries accepted the IMF policies as a

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[3] This term was coined by an economist John Williamson in 1989 to address a set of policies that Washington D.C. based institutions such as the International Monetary Fund (IMF), World Bank, and the U.S. Treasury Department believed were necessary elements of first stage policy reform to increase economic growth. They emphasized macroeconomic stability and integration into the global market.

way to dismantle the communist legacy and to move toward Western liberalism. The plural ideological orientations in a country tend to generate diverse interpretations of economic reality so that more people would question the necessity of the IMF's radical structural reforms (Jorge 1985).

New hegemonic ideas are imposed in a context structured by a prevailing *institutional ethos*, a governing way of action that persists in local context for the long-term. Institutionalized culture, logic, or customs of economic organization in a given country are not made instantly but built over decades (Dyson & Wilks 1983). Persistent policy culture or strategies should not be the idiosyncratic ideologies and beliefs of sub-political or interest groups but should be shared and understood within the larger numbers of people in a society. They are not easily changed by power shifts or the demands of particular social groups.[4]

Among the enduring logic of economic institutions, the key assumption about government-market relationship is the most critical basis for long-term policy ethos in a given country. In his comparative study of railway development in the late 19th century, Dobbin used the concept of "political culture," defining it as “shared conceptions of reality, institutionalized meaning systems, and collective understandings” that are taken for granted (Dobbin 1993, 9-19). He argued that key assumptions about government and market relationship affected railroad policy more than material interests of business and

[4] Sewell emphasized the link between ideology and institutional structure. Ideology is neither a set of ideas held by intellectuals about society nor a reflection of material class relations. Rather, it influences the structure of institutions, the nature of social conflict and cooperation, and predispositions of the population (Sewell 1985).

political elites. French "political culture" sees centralized state authority as key to the political order and this rationale shapes rules, procedures, routines, and habits for policy making. The administrators in Paris orchestrated a railway project with a heavy hand to ensure that private firms would not disrupt the development of a centrally-coordinated national rail system. In contrast, the political culture in the United States endorsed entrepreneurial autonomy during the 1930s. The policy makers perceived market or local autonomy as central to the political order. Accordingly, the U.S. rail policy was developed around market competition and enforcement of anti-trust law.

The state's coordination capacity based on institutionalized pattern of government-market relationship determined the nature of neoliberal transitions. Intensely coordinated policy institutions in France or Mexico created the pragmatic perception of neoliberalism as a necessary step for the country to adapt to the new global economy. In contrast, poorly mediated conflicts regarding the burdens of market adjustments as seen in Britain or Chile led to the highly political and ideological approach to their transitions (Fourcade-Gourinchas and Babb 2002).

1.3 Neoliberal transition: ideas and institutions

The post-crisis reform under the IMF guidance in Korea shows a local experience of the discursive hegemony of neoliberalism that came with an economic crisis. The discussions of the Korean crisis have focused on its causes and consequences. They primarily attempted to identify domestic and global dynamics leading to the crisis and addressed the scope and pattern of dislocations after the crisis. Relatively less attention has been paid to the ideational dynamics of the transition. This study aims to fill a void in the discussion by exploring the interaction between exogenous neoliberal ideas and the endogenous developmental ethos. The studies of neoliberal transition have been conducted in diverse theoretical paradigms. This dissertation counts on both discursive and historical institutionalisms that are not contradictory but complementary approaches.

Discursive institutionalism takes interpretative strategy and asks how institutions are framed and transformed through discourse (Campbell and Petersen 2001). Policy makers tend to be guided by dominant interpretative framework in which they are trying to make sense of reality, identifying problems and depicting legitimate solutions (Hay 2001). This interpretive approach use the concept of "translation," instead of "diffusion" to delineate the process in which actors in a particular national context selectively use neoliberal concepts and replace pre-existing interpretative orders and desirable policy models. Ideas or paradigms are to be altered by the particular discursive and institutional conditions. In other words, discursive approach assumes an ongoing creation of "meaning" in a particular local context and examines how discourse mediates the impact of neoliberalism on economic adjustment (Kjaer & Ove 2001).

Historical institutionalism is another process-centered approach which counts on historically and empirically specific descriptions. It asks how domestic institutions constitute policy capacities in responding to external shock like economic crisis and the pressure of contradictory institutional logic. Accordingly, its analysis tends to emphasize path-dependent institutional change: different political-economic systems created uneven institutionalization of neoliberalism across countries and cases. The complexity of neoliberal transition began to be discussed in the context of collision between diverse regulatory landscapes. There exists no prototypical form of "neoliberalization" across divergent local contexts but articulation and institutionalization are inevitably heterogeneous. Therefore, market-disciplinary regulatory restructuring reveals "historically specific, unevenly developed, and hybrid tendency" (Brenner et al. 2010, 330).

Neither discursive nor historical institutionalism is sufficient in itself but their respective emphases can be combined to suggest an analytical framework that more adequately explains what happened in the post-crisis reform in Korea. This study suggests a frame that discerns two different stages of a "neoliberal transition": the adoption of new policy references (agendas) and the institutionalization of those policy prescriptions. These two stages are placed under different influences of *hegemonic ideas* versus *institutional ethos*. Explaining the hegemony of neoliberal policy paradigm requires a discursive approach to delineate the local context in which neoliberal ideas provided an interpretative frame to define problems and suggest remedies. On the other hand, the dominant policy paradigm were rearticulated and modified under inherited politic-institutional arrangements. The focus on local institutions in historical institutionalism is effective in capturing the processes leading to uneven and incomplete neoliberal projects.

2. Research Questions

This study aims to estimate the nature and scope of the post-crisis transition by asking to what extent neoliberal policy frames were institutionalized to change the "developmental" regulatory structure. It approaches "neoliberal transitions" as processes in which ideational hegemony and institutional inertia constantly interact to generate unique policy outcomes across countries. The study highlights how domestic factors counteracted the pressure of neoliberal realignment. To delineate key contexts for incomplete neoliberal transition, the study constructs the post-crisis reform following three sub-questions.

2.1 The emergence of neoliberalism as hegemonic ideas

The first question asks how neoliberal policy doctrines became main ideological force behind the reform initiatives. With the crisis and the IMF reform in Korea, neoliberal norms dictated quick and large-scale realignment in the policy landscape. Deregulation, competition, and accountability emerged as primary agendas of almost every government department and agency. They were widely pictured as remedy for a "developmental," "backward," and "state interventionist" economy like Korea. Neoliberal doctrine was not vain rhetoric, but actualized through specific rules and sanctions through the IMF programs. Policy makers are all prisoners of the economic orthodoxy of their time and have to demonstrate their adherence to legitimate norms and values. The majority of the policy makers began to espouse the Anglo-American institutions as the advanced model that every country would eventually converge to.

The post-crisis endorsement of neoliberal values was different from Korea's previous liberalization initiatives that centered on how to make the economy competitive. Their legitimizing source was the goal of building a strong national economy, not the virtue of neoliberal ideology itself. Thus, neoliberal doctrines were selectively advocated: the rigid labor market and excessive government regulations were problematized but *chaebols*' over-investment by high debts was rarely framed as a key danger to the economy. Attacking *chaebols* seemed to represent an anti-capitalist political view, rather than a neutral economic perspective. *Chaebols*' performances, especially market expansions, were often seen as the indicator of the power of the national economy. As far as they contributed to economic competitiveness, "less" liberal practices could be tolerated. In contrast, anti-chaebol sentiment was the significant part of moral hazard discourse that came with the crisis. *Chaebols'* ownership structures, corporate governance, and the means of capitalization were reconsidered under the norms of the Anglo-American business model. New policy goals to discipline *chaebols* received support even from left-oriented intellectuals and activists who had long opposed the *chaebol*-centered Korean economy.

The acceptance of the neoliberal rationale was mediated by a moral hazard view that highlights the defects of the developmental institutions. The IMF prescriptions were accepted as painful but inevitable tools for upgrading the economy. During one year leading to the crisis, a series of bankruptcies among highly leveraged *chaebols* created an awareness among the public about structural and moral problems in the Korean economy. Finance with state guarantees, risky over-investments and excessive debts had been typical business practices during the high growth era. They suddenly became the signs of economic dysfunction and immorality.

The story of moral hazard about the Korean crisis highlights that major banks, financial institutions, and *chaebols* took advantage of their insured position by the government and engaged in risky investments. It was the official opinion of the IMF that moral hazard practices induced by the government-banks-*chaebols* alliances were the main culprit for the economic catastrophe (IMF 1997). It is worth discussing how moral panic and disillusionment with the pre-existing system shaped policymakers' interpretation and usage of neoliberal creeds in Korea.

2.2 Contradictions between neoliberal agendas and the developmental policy ethos

The second question of the study asks how newly espoused neoliberal agendas contradicted the developmental policy ethos or rationales, specifying the areas of conflict between two different policy paradigms. The post-crisis reforms aimed to "upgrade" the Korean economy by following the Anglo-American model of market economy. While neoliberal doctrines denounce its effectiveness, active and strategic government interventions had been perceived as key to the economic success of the East Asian countries including Korea. Even neoclassical economic view admitted in the well-known work *The East Asian Miracle*, that government interventions in East Asian economies were not harmful. This was because their interventions (i.e. government subsidies) were basically market friendly and price distortions were minimal, relying primarily on market mechanism (World Bank 1993). Whether it be praise or criticism depending on their economic philosophy, most theoretical discussions can't explain the success of the Korean economy without factoring in the government's active industrial policy. It had never been fundamentally denied in its central role to economic growth.

Then, the 1997 crisis and the IMF regime placed the developmental paradigm in new context, highlighting its deviance from the Anglo-American model of market economy. The government's active industrial policy, once highly praised, began to be seen as inevitably distorting, inefficient, and immoral. The government's implicit guarantees that favored strategic projects and particular players, allowed key businesses to take excessive risks in their investment (*The Economist*, November. 15, 1997). Moreover, that type of intervention discouraged financial institutions from managing risks in their investment and lending. The IMF estimated that "the legacy of intervention has left an inefficient financial sector which has led to a highly leveraged corporate sector that lacks effective market discipline" (IMF 1997). In sum, a lack of commercial orientation, limited expertise in pricing and managing risks, and lax supervision constituted the weaknesses of the financial system. This new highlight on the weakness of the Korean economy caused downgrading of the credit ratings in the global market.

Neoliberal denouncement of active government interventionism was well represented in the IMF reform agendas. The centerpiece of the IMF reforms was to change the financial system to be more market-oriented, competitive, transparent and accountable. The programs were supposed to replace the government's control with market discipline, which had always been a challenging goal in Korea. Pre-crisis efforts to empower banks were largely futile because the government's industrial policy counted on policy-financing by controlling the banking sector (Woo 1991). Banks had been under the full control of government with little authority in disciplining corporate management. As a consequence, they were incapable of making lending decisions through their own estimation of business credibility, profitability, and risks (Park, K.S. 2003). The agenda of small government had been inevitably cosmetic. The support of cohesive bureaucrats was essential for securing the leadership of any regime. The attempts to contain their size and functions had always been incomplete.

Neoliberal agendas were accompanied by new standards and rules. For example, a set of capital adequacy requirements aimed to secure financial accountability in banks and firms. The Bank for International Settlements (BIS) measures the banks' financial soundness using the index of the ratio between risk-bearing capital and risk-weighted assets.[5] The higher BIS ratio indicates the lower risk of potential bankruptcy. Following the IMF guidelines, the government required all banks to stay above 8% of the BIS ratio. This means that banks should maintain enough capital at least 8% of its risk-weighted assets. This rule aimed to drive banks to be more prudent in their corporate lending whose risk is more weighted. Failure to meet this task made banks deemed "unaccountable" and forced them to be closed or merged with other banks. Another capital adequacy measure was the rule of 200 % debt to equity ratio for firms. It was enormously challenging rule to the majority of *chaebols* given that the average liability ratio of the top 30 *chaebols* was almost 600 percent as of July 1997 (Lee, P.S. 2000). The reform introduced a set of "global standards" concerning accounting and disclosure. They aimed to prohibit firms from moral hazard behaviors by binding them to stringent rules and standards.

Corporations' high debts and risky investments had been a business paradigm in Korea for decades. In a credit-based economy like Korea, high debts were inevitable for spurring high growth and promoting ‘patient’ long-term investments (Joh 2004; Wade & Veneroso 1998). These paradigms had been compatible with the avowed policy goal of economic growth and market expansion. However, they would be less compatible with

[5] Founded in 1930 in Basel, Switzerland, the BIS is an international bank headquarters for monetary cooperation among European central banks, the Bank of Japan, and the U.S. Federal Reserve System. Its main goal is to monitor and collect data on international banking activities and set the rules concerning international bank regulations.

stricter loan qualifications and foreign capital's priority on short-term interest. In the Korean context, neoliberal ideas in contradiction to the "developmental" policy rationales became powerful as reform agendas. However, they had to be rearticulated and compromised in their implementations.

2.3 The operation of the developmental policy ethos in the reform

The third question of the study, the most central one, asks how *the developmental policy ethos* compromised the institutionalization of hegemonic neoliberal doctrines. Unlike a coherent and explicit set of ideas such as monetarist doctrines, policy ethos is embedded in implicitly shared understanding and norms that operate in the interactions among policy actors. It is associated with particular recurring policy preferences, strategies and capacities. I focus on government interventions characterized by particular capacities: a cohesive group of goal-oriented bureaucrats actively supervise and coordinate private sector to solve problems. The ethos entails weak ideological commitment to state-market boundary and strategic policy support to key economic sectors.

Neoliberal doctrines certainly acted as a dominant reference to guide the post-crisis reform. They successfully framed the crisis as the result of institutional failures and set the reform master plans. Neoliberal policies advocated fair, competitive and autonomous market force, which contradict many of the developmental policy preferences. Although pre-existing paradigm was de-legitimated, endorsement of a new paradigm does not guarantee the permanent replacement of old ones. Celebration of market discipline tends to lose its momentum as the economy gets back to its normal status and resilient institutional inertia began to operate. How did the pre-existing policy rationales persist to influence the path of reform?

In the study, I identify key domestic contexts for how the developmental policy inertia limited the neoliberal reform in Korea. The radical market adjustments were legitimated and pursued as a project of overcoming the national adversity and "upgrading" the economy. Accepting the disciplining programs imposed by the global market came to be understood as the only way to survive. While perceiving the external enforcement as exogenous and uncontrollable forces, top bureaucrats used the IMF programs in regaining their initiatives in the domestic reforms. Another key compromising factor was the political inertia to protect core sectors. The market adjustment aimed to rationalize the core sectors that include intrusive government, expansive chaebols, and rigid labor. To make the markets more fair and efficient, the ambitious administrative, corporate, and labor reforms aimed to remove the protection for them. Before the crisis, the policy preferences to protect core sectors were so consistent that the attempts to discipline them were selective, cautious, and largely cosmetic. Did a series of radical reform initiatives sacrifice the core sectors' interests? Overall, did neoliberal doctrines, articulated by the IMF policy prescriptions, substantially recast the developmental policy arrangements in neoliberal terms?

3. Perspectives, Conceptualization, and Data

This study explores the encounter and tension between hegemonic neoliberal ideas and the developmental policy ethos in the post-crisis transition. The term of "neoliberalism" has been perceived and used differently by liberal minded public and market-oriented reformists, often with opposite political connotations. Likewise, what "neoliberal transition" actually signifies in a local context is confusing: the term can mean different things to different groups. Does a "transition" signify a conversion in values, a change in policy priorities, or technical enforcement of a particular set of programs? Analytically, I define neoliberal transition or neoliberalization as the process of implementing neoliberal agendas.

Ideational perspective assumes a coherent set of new ideas that dominate the policy making processes. In contrast, path dependency perspective focuses on constant national peculiarities to highlight how they generate particular policy outcomes. Neither of these perspectives is sufficient in itself but their respective emphases can be combined to suggest an analytical framework that more adequately explains what happened in the Korean post-crisis reform. I suggest a frame that discerns two different stages of a "neoliberal transition": the adoption of new policy references (agendas) and the institutionalization of policy prescriptions. These two stages are placed under different influences of *hegemonic ideas* versus *institutional ethos*.

I define *hegemonic ideas in policy domain* as exogenous and short-term influence that operates more rhetorically than practically. Policy actors are subject to the prevailing ideas that offer the main references to reconsider the pre-existing institutions and practices and suggest legitimate models to follow. In general, participants in policy discourse most safely refer to this dominant frame in interpreting reality and suggesting solutions. Neoliberal view emerged to dominate the discussions about the crisis in the form of crisis diagnosis. Its policy prescriptions provided coherent action plans. The neoliberal policy paradigm had rarely been experienced or empirically tested in the local setting. Nevertheless, the narratives of the crisis discourse and the official reform agendas indicated a paradigmatic change in the policy landscape.

To capture the hegemonic status of neoliberal frames, I primarily review the crisis discourse and official reform agendas. Policy elites' interpretations of the crisis and their attitudes toward market adjustments were heavily influenced by a dominant policy frames to which policy actors could safely refer. I draw on the texts that describe the narratives concerning the crisis and delineate how policy elites counted on neoliberal policy frames to identify the causes and remedies of the crisis. Focusing on the major reform agendas, I discuss the policy goals set by the specific programs to highlight the impact of neoliberal ideas and the source of their legitimacy. Periodization of an ideational dominance may differ from that of its institutional effects (Hay 2001).

In contrast, I define *institutional ethos* as endogenous and long-held orientations that have more direct influence on practical actions. The stage of implementing reform agenda are affected more by these local influences. As institutional ethos operating in policy domains, I attend to a set of recurring policy strategies, preferences and capacities employed by the government in managing the crisis and guiding the reform projects.

For this process-oriented analysis, I use a variety of archival data. First, I refer to public archives which include legislative records, government publications, and IMF/OECD reports. The transcripts of the regular meetings and inspections of the standing committees in the National Assembly are the written records of verbal conversations between the congressmen and the administrative bureaucrats regarding policy issues of each standing committee. These documents offer reliable accounts of the practical concerns and conflicts of major policy makers. The transcripts were accessed through "Knowledge Management System" which is online archival data base (http://likms.assembly.go.kr/record/index.html).[6] I particularly examine the committees of the Civil Service Commission, the Ministry of Environment and Labor, and the Special Inspection on the Economic Crisis (see Appendix). The special inspection committee was held from January 25 to February 11 in 1999 and the top economic policy makers were investigated by a group of congressmen regarding their policy decisions and the crisis management. These interrogation records revealed practical pressures they faced and personal policy orientations. These legislative manuscripts provide a realistic glimpse into the government's policy rationales; the government's communications with other policy groups; the conflicts and negotiations occurring during the reform processes. The OECD/IMF regular reports give relatively unbiased policy data provided by each government. I also use interview transcripts published in media and autobiographies of the significant policy actors to get the micro-level contexts for critical policy decisions.

Second, to map out major perspectives regarding the crisis and the IMF intervention, I rely on major daily newspapers which are the most significant spaces for opinion leaders to voice their views on current issues in Korea. I use two online archives: *Naver News Library* (http://newslibrary.naver.com) and *Korean Integrated News Database System* (KINDS: http://www.mediagaon.or.kr). *Naver News Library* stored the articles of four newspapers from 1920 to1999 in their original images and text files. These four newspapers (Dong-A, Jung, Hankyurae, and MK Business News) have

[6] I indicate the legislative transcript sources in the following format: (NA: committee name, date of meeting). The special investigation committee will be indicated as (NA: Special Committee, date, year).

different political orientations from progressive (Hankyurae), center-left or center-right (Kyunghyang, Dong-A) to conservative (MK business News). This archive effectively visualizes the frequency of relevant articles for key words in each year to show how much each agenda or issue were debated. The KINDS has been the most comprehensive web-based archives to store the articles and editorials of both major and minor (regional and professional) newspapers and magazines.

By using keywords, I review editorials and opinion columns concerning the causes of and solutions to the crisis. In tracking each article or editorial, I check their reference sources (best practices, academic theories, new concepts) and policy orientations to capture the ideational influences in policy discourse. Then, I discuss the discrepancy between the ideological force of neoliberalism and its actual institutionalization by asking how original agendas or values were ensured by formal rules and enacted to create intended changes. The analysis is confined to the whole period of the Kim Dae-Jung administration (1998-2002) and the early period of Roh Moo-Hyun administration (2002-2004) since the time span is a reasonable time frame to include both exceptional and normal policy making.

4. An Outline of the Arguments by Chapters

Chapter 2 discusses key pre-crisis policy ethos and liberalization initiatives during the 1980s and the 1990s. As the developmental policy ethos, I address pragmatic policy orientations, public-private mix in mobilization, and strategic support of key economic sectors. A pragmatic policy orientation allowed the government to employ a variety of hybrid policy tools geared toward economic growth. Weak ideological commitment to drawing a boundary between government and market granted the government the greater maneuver in mobilizing the private sectors. It supervised banking sectors, guided businesses, and controlled labor for long-term economic projects. The government strategically supported key economic sectors by offering credit loans to *chaebols* and keeping employment security for the workers of key industries. Then, I discuss how liberalization initiatives during the 1980s and 1990s affected these developmental policy rationales. I identify the main political drives and limited achievement in financial, corporate, and labor sectors. The reform efforts were largely cosmetic, neither curtailing government control nor disciplining chaebols' dominance. Finally, I address major reform issues right before the crisis and describe how the reform initiatives were stuck in political gridlock because of growing veto powers of the opponents until the outbreak of the crisis.

Chapter 3 explains the rise of neoliberal doctrines as a dominant policy paradigm under the IMF regime. I highlight how the "moral hazard" perspective shaped the interpretation of the crisis and legitimized neoliberal prescriptions. I describe the Hanbo scandal and the Kia crisis as critical events to invoke the moral hazard view in the Korean politics. Then, I address the general logic of IMF program and its major reform agendas such as small government, bank autonomy, strict capital adequacy, priority of shareholders' benefits, corporate transparency, labor flexibility, and capital liberalization. I describe how the crisis-driven reform dynamics provided favorable reform-making institutions. Finally, I discuss the incomplete ideological conversion to market discipline found in the top economic bureaucrats and limited power of neoliberal doctrines as enduring policy rationales.

Chapter 4 highlights how the developmental ethos persisted to compromise the main reform agendas. The "small government" doctrine was a huge failure: the government restructuring did not yield any substantial change and the government spending and debts increased. The project of building stringent market discipline led to more integrated government control over financial institutions. The political and economic incentives to protect cohesive bureaucrats, *chaebols*, and organized labor compromised the agendas of limited government and market autonomy. The most successful implementation was seen in the policies related to the interests of foreign capital. With rapid capital liberalization and promotion for foreign investment, the financial institutions became more susceptible to the growing influence of foreign shareholders and investors.

Chapter 5 discusses the changes and continuities in the labor market. Promoting labor flexibility was an integral part of the market adjustments. The legalizations of collective layoffs and dispatched workers critically weakened employment security. Increasing labor market insecurities facilitated the expansion of state welfare and social insurance programs. These improvements did not effectively deal with the increasing risks inflicted on unorganized non-regular workers. The strong corporate unionism centered on big enterprises maintained employment security for regular worker members, but excluded non-regular workers from collective bargaining. In sum, the initiative for labor flexibility did not erase the legacy of dual labor but widened the gap between workers by firm size and unionization.

In chapter 6, I summarize the major findings and review the neoliberal transitions of other developmental states of Japan and France to provide a brief comparative discussion. I explain how their "developmental" institutional legacies led to similar interpretations of economic challenges and policy responses: they framed market adjustments as national projects and promoted active government coordination to deal with the conflicts from market adjustments. The Korean experience showed that the neoliberal values were highly legitimated in the policy discourse. However, they were compromised, modified or abandoned in the process of institutionalization within the developmental policy frames.

CHAPTER 2

THE INSTITUTIONAL ETHOS AND LIBERALIZATION DURING THE 1980S AND THE 1990S

1. The Institutional Ethos of the Developmental State

1.1 Pragmatic policy orientation and private sector mobilization

This chapter discusses the core policy orientations of Korea and the trajectory of liberalization during the1980s and the 1990s. Korea's rapid economic growth and full-fledged industrialization for several decades had counted on pro-growth policy orientation. They used active state interventions which often transgressed public-private boundaries. There are theoretical concepts to highlight the state-society relationship unique to the "developmental states." The concept of “embedded autonomy” (Evans 1995) captures critical components of the developmental state capacity: being "separate from" (autonomy) but at the same time "connected to" (embeddedness) private actors. State 's autonomy means that the government was not captured by private powers and did not solely serve the interests of elite social groups. In Korea, cohesive executive bureaucrats could set national goals and dominate the policy making process through their expertise in drafting laws, regulations, and licenses that govern society. This could allow for coherent policy implementation (Rueschemeyer & Evans 1985, 46-50). State's embeddedness refers to the government's connections to social constituencies that differ from personal networks or elite clients. It implies "a concrete set of connections that link the state intimately and aggressively to particular social groups with whom that state shares a joint project of transformation" (Evans 1995, 59). Keeping a close but distant relationship, the government employed sticks to elicit compliance and offered carrots of incentive packages to guide businesses to invest in target sectors.

Another concept to characterize the developmental state-society relationship is the "elusive state" (Wolfren 1989, 66). The Japanese state-craft shared its power with semi-autonomous non-governmental groups. States power and market power belong to bureaucrats and businessmen alike, and they enhance each other. It is not clear "where state structures leave off and social structures begin" (Cumings 1999, 65). This relatively blurred public-private boundary is based on its logic of reality perception. Japanese did not accept Western metaphysics based on the idea that there are universal truths, rules, principles or morals that transcend all circumstances. Instead, they count on situational rules and values, adjusting their beliefs to changing circumstances. Their cultural outlook has much more tolerance of contradiction in their reality perception. Based on this political culture, Japanese public policies possessed outstanding openness and adaptability to form hybrid policy orientations (Wolfren 1989). The technocratic bureaucrats were plan-rational in managing the economy, given the environment of development, lack of resources and the need to trade (Johnson 1982). While cultivating cooperative relationships with conservative groups such as bureaucrats, businessmen, and landlords, the government could effectively mobilize the private sectors in solving emerging national problems. Japanese conservatives were not ideologically rigid but could keep adapting their positions as a situation changed. Based on this “creative conservatism," Japan could achieve unprecedented economic success with minimal social costs (Pempel 1982).[7]

Scholars depict this tight but distant alliance found in the developmental states as a variant of corporatism.[8] In European corporatism, social groups are relatively autonomous, equally entitled to a space in policy making, and can promote policy initiatives through a representative party system. In contrast, Korea's "state corporatism," was led by the autonomous state based on its coordination with less autonomous societal associations (Pempel 1999). The embeddedness was concentrated in a few ties between state and representative social associations. Unlike the societal corporatism, the bureaucratic-authoritarian state of the 1970s controlled labor within the corporatist frame which was used to link to the labor sector only to secure its exclusion. The peak union associations recognized by the state had been kept passive enough to be excluded from representation.

Following a similar path to Japan, Korean economic growth evolved on the intensely coordinated state-society relationship. There was weak ideological commitment to drawing definite boundaries between government and market. The Korean economy had counted on effective private mobilization in responding and adapting to endless

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[7] The government could rely on the intense partnership with a limited number of "peak associations" that are licensed by the state as official representatives of social sectors. The state's negotiation with these monopolistic organizations representing major private sectors facilitated effective top-down political control (Pempel 1982).

[8] The concept of *corporatism* refers to a system where representatives of major interest groups (called corporations) regularly structure their expectations about others' behavior and settle any problem and conflict through negotiation and joint agreement (Schmitter 1974).

emerging economic challenges. Its policy making had shown the great adaptability to situational goals, often constraining ideological-driven or interest politics.

This legacy was well actualized in major policy inventions in the period of high growth. A series of national campaigns from the 1960s to 1990s is the best example. The government actively mobilized the people as members of a cohesive national community to achieve a variety of practical goals. The New Village Campaign was initiated by President Park Chung-Hee in the early 1970s. The national campaign originally aimed to restore the collapsed rural economy and gradually expanded to urban areas and factories. The campaign entailed full-fledged bureaucratic mobilizations and massive budgetary support. The central government bureaucrats worked intensely with the local government, enterprises and community leaders, often promoting competition among involved villages and cities.

The Two Children Only Campaign during the 1960s and the 1970s aimed to ease the pressure of drastic population growth after the Korean War. The local public health agencies worked closely with women's organizations in educating and supervising fertile women. The nationwide Buy Korean Commodity campaign and household saving campaign were constantly promoted during the era of export-driven economic growth when foreign loans and domestic savings were the major source for business investment.[9] The campaign of mixing rice with barley was initiated during the 1970s when overproduction of barley and increasing rice imports emerged as problems. Energy saving, blood donation, wage control, and foreign currency saving campaigns were all

[9] The national fever of "Buy Korea" and "Collecting Gold" campaigns right after the crisis in 1997 reflects this enduring policy legacy.

pursued to deal with emerging economic challenges. These were heavily coordinated by the government. Those national campaigns revealed that the government freely intervened in the private domains such as family planning, commodity purchasing, food consumption and household saving. Public-private domains were not in strict tension but their boundary often blurred for situational and practical purposes. In addition, the urgency of national security under the constant threat of war boosted the nationalist impulse for integration and solidarity. These public sentiments enhanced the government's capacity for mobilization.

1.2 The policy ethos of prioritizing key industries and the dual labor market

The Korean economy grew rapidly during the 1960s and 1970s. Many commentators attribute its success to the subsidizing and coordinating investment decisions by the government (Rodrik 1996). The government's intervention by protecting infant industries and supporting key industries triggered the growth. During the 1960s, labor-intensive light manufactures (i.e. textiles, clothing, leather goods) had increasing share in total exports. Entering into the 1970s, the government made important strategic policy decisions given the changing environment. In 1971, the United States reduced its military force in Korea by a third. Perceiving it as the first move of a full military withdrawal, the Korean government believed that it needed to develop strategic industries for defending itself. The Korean economy also faced growing protectionism in the developed countries against labor-intensive exports and increasing competition with other East Asian countries in light manufacturing industries (Panagariya 2008).

Consequently, the government embarked upon strategic investment in the capital-intensive heavy and chemical industries such as steel, shipbuilding, automobiles, machinery, and petrochemicals. As a country competing without new technology, Korea deliberately used subsidies to "get prices wrong” to stimulate investment and trade (Amsden 2000). The government nationalized the main commercial banks and regulated their interest rates. The most critical intervention was to set interest rates on long-term foreign loans and channel them to strategically favored firms.[10] To such firms, the rate was constantly negative in real terms during the 1960s and the 1970s. Along with foreign loans, tax and trade policy concessions were used to promote the targeted industries.

To get this preferential treatment, businesses had to comply with policy goals set by the government. Successful exporting companies or capital-intensive projects were given priority in receiving preferential credits. The firms without access to subsidized lending had to rely on the unofficial capital market where they paid a much higher interest rate. The government also employed stringent tax audits, import license certification, and enforced nationalization in guiding businesses. These interventions promoted the core strategic industries as the foundation for economic growth.

The developmental states was categorized as *non-liberal capitalism* in contrast to *liberal capitalism* (Wolfgan & Yamamura 2001). The non-liberal model as found in Japan or Germany has more socially and politically coordinated markets than liberal capitalism. For example, the Japanese labor market has relatively low turnover, strong

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[10] These investments relied on foreign loans guaranteed by the government through the Korean Development Bank.

seniority rules and cooperative labor unions. This long term commitment between labor and businesses was made possible by patient business investment for long term growth, which limited the pressure for short-term business profits (Aoki 1994). In contrast, liberal capitalism is driven by the search for short term business profits, which fosters weak commitment between business and labor. Employers in liberal labor market have more freedom to fire workers.

There was strong policy commitment to employment security and income maintenance in Korea. In the 1960s and the 1970s, labor policy focused on creating more job opportunities as a way to solve the unemployment problem, and the wage level kept increasing. Entering into the 1980s, the Korean labor market had to deal more seriously with economic fluctuations. The second oil shock came in 1979, exerting great restructuring pressure. However, the merits of a strong internal labor market had been well appreciated. The government and business tried to make employment adjustments without disturbing the employment security guaranteed by the internal labor market. They tried to avoid firing current workers by limiting new recruitment, employing wage flexibility, and reallocating workforce. Thus, the unemployment rate remained fairly stable at 5.3%. The government also offered firms tax deductions and controlled the price of agricultural products in order to curb wage drift and inflation (Song and Hong 2008).

However, this policy commitment to employment security was not universally applied to all labor. During the 1970s and 1980s, the East Asian developmental countries fostered a dual labor market that favored full-time regular workers in the key strategic industries and public sector. The favored workforce, most important for economic growth, was well organized and politically powerful. They were entitled to employment protection and comprehensive welfare benefits. Not the extension of political rights to the working class in the Western countries, but "industrial citizenship" formed among workers within the firm was the basis of social integration in the region (Jackson 2001; Manow 2001). In contrast, non-regular workers (temporary, part-time, dispatched, and self-employed workers in small and medium sized firms or pre-capitalist sectors) had no employment security and limited access to welfare benefits. While this market duality contributed to maintaining economic stability by reducing unemployment, it created a substantial gap among different groups of workers, both in employment protection and in access to welfare benefits (Yun 2008, 240).

The strategic investment in heavy-chemical industries during 1973-1987 intensified the dual labor market in Korea. The labor market was segmented between labor-intensive light industry and capital-intensive heavy industry. The former counted on low-skilled and young female workers for lower wage. In contrast, the latter attracted more skilled male workers for higher wages and better working conditions (Deyo 1989). Until the mid-80s, the independent labor movement had been intensely oppressed by the government for constant wage limits and labor control. The rise of labor movement after 1987 brought about the development of the internal labor market in large enterprises to create a segmented labor market by firm size. Using the 'Occupational wage survey' and 'Survey on circulation conditions of labor force,' Jung investigated the characteristics of internal labor market.[11] The wage difference by firm size was enlarged and employment

[11] Jung used the concept of "internal labor market" defined by Doeringer and Piore (1971) as "an administrative unit within which the pricing and allocation of labor is governed by a set of

stability in large firms was enhanced since 1987 (Jung, E.1993). Under the strong corporate unionism in Korea, the annual wage increase was negotiated within a company and employment security was guided by internal rules of firms independently from the outside labor market.[12]

In contrast, workers in small firms still suffered from low employment stability. Because of the lack of detailed government statistics on non-regular workers, it is hard to identify the size of temporary workers in Korea before the crisis. According to a survey by the Economic Planning Board, the ratio of daily workers in non-agriculture sector is 15.9% in 1990 (Jung, E.1993). During 1980s, the percentage of temporary or daily workers got smaller with the increase of firm size. Aside from using temporary workers, employers could utilize inside sub-contracting through which a firm delegates parts of production to sub-contractors. They did not directly mange the workers of sub-contracting firms. When employers needed to reduce the labor force, they simply suspended the deal with subcontractors. These sub-contracting workers and the self-employed workers in external labor market had to deal with the lack of employment security and formal protection.

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administrative rules and procedures." The internal labor market is distinguished from the external labor market which is governed by economic variables.

[12] A strong industrial union can block the labor market segmentation as seen in the experience of Sweden (Esping-Anderson 1985). In 1987, the labor law to ban industrial level union activities was abolished with the labor law revision in Korea. Collective bargaining at industrial level was not made easily because of the government's intervention, employers' reluctance, and big unions' egoism (Jung, E. 1993).

Targeting industries and accompanying protection for labor in the sectors determined the beneficiaries of the social insurance systems. The Industrial Accident Insurance (1964), the National Pension Program (1973), and the National Health Insurance (1977) all targeted the workers in large industries. The national health insurance program, for example, started only in firms of more than 500 employees concentrated in the energy, construction, and heavy chemical industries. The national pension system was initially planned to fund long-term economic projects. In order to raise a large amount of funds for a short period, the government designed a pension system to be universal and administratively integrated.[13] As planned, 54.52% of the pension fund was used for public investments in economic projects at the time of its introduction (Kim, Y.B. 2002).

While employers and workers were mainly responsible for their financing, the government enforced the provision of retirement fund, paid vacation, maternal leave, and minimum pay level.[14] It strictly maintained the principle of cost containment and paid only administrative costs in order to minimize the state's expenditure. Consequently, only those who held secure jobs and were able to contribute could be beneficiaries.

The firm-based social protection targeting the core workers of the key industries generated a high level of political tolerance for the insufficient state welfare in Korea.

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[13] The same political intention was found in Japan too. The old-age insurance was introduced to accumulate capital for the war effort and the Ministry of Finance had been and remained in charge of administering the funds after World War II (Manow 2001).

[14] After 1987, the oppressive labor policy was eased to increase legal corporate welfare expenditure by 55%. Corporate welfare fund law was established in 1991 to enforce substantial improvement in welfare benefits (Jung & Cheon 2001).

Labor unions did not pay enough attention to the issue of universal welfare. Rather, they focused on collective bargaining with employers or business associations, fighting for their workers' benefits. Union members perceived health insurance and pension, the two main pillars of social protection, as employment benefits. Thus, their demands were channeled toward the corporations, not the government. The concept of *citizen's welfare rights* never acquired a place in political discourse. An analysis of presidential new-year speeches from 1962 to 1983 reveals that there had been little concern for state welfare and social equity in the state's policy plans (Kim, K. 1983). The concept of "welfare" was discussed only with respect to the issue of human development through universal education and full employment, not as an issue of social justice or protection.

A variety of social development programs within economic projects, functioned as a quasi-welfare system. The programs to improve health service, education, transportation, housing, and policing compensated for the limited state welfare. Moreover, social equality had been achieved relatively well in Korea because of its universal education and growing employment opportunities.

(Table 1) GINI index for selected Asian and Latin American countries (for the period 1965-90)

	1965-70	1971-80	1981-90
Korea	0.34	0.38	0.33
Taiwan	0.32	0.36	0.30
Indonesia	0.40	0.41	0.30
Hong Kong	0.49	0.42	0.39
Brazil	0.57	0.60	0.60
Chile	0.50	0.53	0.53
Mexico	0.58	0.52	0.53

*Sources: Reprinted from Campos, Jose Edgardo & Hilton L. Root. 1996. Chapter 1: East Asia's Road to High Growth, in The Key to the Asian Miracle: Making Shared Growth Credible. Brookings. * higher numbers indicate greater inequality.*

As Table 1 shows, the benefits of economic growth were distributed across social groups better than in other developing countries. These improvements were mainly driven by development-oriented politicians and administrators with weak political commitment to social justice or democratic cause. Strong family responsibility for individual risks also compensated for the limited state welfare especially in caring the elderly, the sick, and children. Government assistance was limited to the extremely poor, and was greatly stigmatized. Thus ordinary people had to find their own way of managing potential risks. As seen in Table 2, household saving rates in Korea have been higher than in most other countries, partly because of the great pressure of self-insurance. The developmental rationales of strong government intervention and strategic protection for the prioritized industrial sectors faced challenges by a series of economic and political liberalization measures during the 1980s and 1990s.

(Table 2) Household saving rates as percentages of disposable household income

	1988	1998
Korea	25.1	23.0
Japan	13.2	11.2
Germany	13.2	10.3
United States	7.8	4.7
United Kingdom	4.9	6.0
Canada	12.3	4.9
Finland	-0.5	0.7

Source: OECD Economic Outlook, Dec (2002)

2. Developmental Policy Rationales and Liberalization during the 1980s and the 1990s

2.1 Economic liberalization and the government

The next section addresses how the developmental policy ethos shaped the path of liberalization during the 1980s and the 1990s. The strategic industrial targeting and subsidizing generated problems of capital concentration, unbalanced resource allocation, budget deficits, and skewed income distribution. To solve these problems, the new military regime in the early 1980s empowered reform-minded economic bureaucrats like Kim Jae-Ik and his colleagues to initiate stabilization programs.[15] Kim served as senior secretary to the president for economic affairs from the late 1970s until his tragic sudden death in Burma in 1983. This group of bureaucrats raised interest rates to tighten monetary policy, suspended new industrial projects, removed price control, and introduced a value-added tax (VAT) to secure an additional source of government reserve (Kim, K.H. 2003).

At the same time, the government attempted to fix the growing industrial imbalances and deteriorated income distribution. These measures were pursued as the main components of the fifth “Five Year Economic Plan” (1982-1986) which differed from previous plans in its approach. The previous four plans were designed to achieve quantitative targets such as high growth and price stability. In contrast, this fifth plan aimed toward qualitative change by making administrative and economic institutions more efficient and balanced. The agenda of “small government” was introduced to limit the government's excessive regulatory control. However, this drive to fix and upgrade the domestic institutions still remained vague: there was no specific action plans or program schedules.

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[15] After the second oil crisis, the U.S. pressured Korea to receive the IMF emergency loan. In return for the loan, Korea had to demonstrate its departure from developmental policy interventions such as long-term industrial policy, overvalued exchange rates, financial control, and tolerance of high inflation.

A facet of the Kim Young Sam regime's New Economy Plan was initiated in 1993 and continuously pursued reducing government control and encouraging private sector initiatives. In 1994, two top economic departments, the Economic Planning Board (EPB) and the Ministry of Finance (MOF) were merged to constrain the MOF's power on the banking sector and its collusive ties with big businesses. However, this merger created an even larger and more powerful agency, the Ministry of Finance and Economy (MOFE). It came to possess comprehensive control over fiscal, budgetary, and other major economic functions.

Meanwhile, liberal economists, civil activists, and labor unions expected that, a "small government" initiative would promote empowerment of the Bank of Korea (BOK). The neoliberal policy rationale supports an independent central bank as the key tool for securing financial austerity and stability. The central bank should be independent from self-interested politicians who are tempted to promote inflationary policies (Polillo and Guillen 2005). This justification, however, was weak in Korea because its top economic policy makers were not elected politicians but autonomous technocrats who advocated financial austerity. With full control of the financial sector, they had persistently blocked the efforts to empower the BOK, arguing that stable currency maintenance could be effectively achieved by the bureaucrats themselves.

The ownership of the major banks was another contentious topic before the crisis. As government control over the banks began to receive negative attention, *chaebols* began to demand the right to run their own banks. The economic bureaucrats strictly prohibited *chaebols* from owning their own banks arguing that this would intensify capital concentration.[16] Who should own the banks other than the government and *chaebols* remained a confusing question to the majority of policy makers.

One of the most ambitious reform attempts was to liberalize interest rates. In the early 1990s, the United States pressured Korea to liberalize its interest rates arguing that it would promote efficient, productive, and fair resource allocation. Korea had never liberalized the rates before because low interest loans to target industries and firms had been the key policy tools. *Chaebols* opposed interest rate liberalization out of fear that their capital costs would rise. Experts argued that liberalizing interest rates was neither urgent nor necessary, but only a reaction to external forces.[17] Persistent U.S. pressure ultimately resulted in deregulation of interest rates under the Financial Liberalization and Market Opening Plan announced in 1993.

However, the government continued to exert informal "window guidance" to ensure that businesses in the targeted industries would still receive preferential credit. It still controlled interest rates in the selected financial sectors, providing relatively cheap lending in comparison with actual market rates. By the 1990s, while the number of private commercial banks increased, their lending rates still remained within narrowly defined official limits set by the government. Bankers' estimates of risk and profitability of business projects were easily ignored. Corporate lending was still contingent on the

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[16] With ownership restrictions, the government diffused the ownership shares for banks so that it could direct bank's lending practices.

[17] There were other practical concerns. Korea still had the problem of price instability and pervasive speculation, which motivated people to borrow money for speculative investments. Given the high demand for capital, the interest rate would increase under deregulation.

borrower's connection to bureaucrats and on business projects' compatibility with the government policy priorities. Privatized banks had limited discretion over lending decisions and the appointment of key personnel. The liberalization measures could not fundamentally alter the policy rationales in the financial sector. The government kept regulating the sector to funnel low-cost lending to prioritized target projects for high growth and investment.

Facing external pressure for further liberalization and internal conflicts concerning authority over the financial market, in the early 1997, Kim Young Sam administration established the Financial Reform Committee (FRC). The committee consisted of 31 private experts, half of whom were economics professors. The FRC represented the interest of big businesses. It proposed rebuilding an integrated supervisory agency under the authority of the Bank of Korea (BOK) in order to counterbalance the power of the economic bureaucrats. Meanwhile, the establishment of the FRC as the leading agency to set the reform direction, outraged the executive bureaucrats of the MOFE. Whenever the FRC announced its reform proposals, the MOFE criticized the plans as neither desirable nor feasible. The MOFE insisted on its control over banks and *chaebols,* arguing for even more integrated authority. The conflict between the MOFE and the BOK over financial authority reached its climax when the crisis broke out.[18]

[18] The MOFE could make its own independent bill with veto power only by President. The financial reform bill proposed by the MOFE was about to be passed in the National Assembly in 1997. After the crisis broke out, the elected president Kim, Dae-Jung could stop their bill. He warned that the MOFE's persistent power over the financial sector would upset foreign investors.

2.2 Economic liberalization and big businesses (*Chaebols*)

The U.S. trade protectionism started in the late 1980s to reduce its deficit with the East Asian countries. Exports to the U.S. market had been a critical source of economic growth of 9.8 percent from 1983-1990. With the end of the cold war, the U.S. began to see South Korea less as the main front-line state. The U.S. no longer tolerated huge trade deficit with Korea. The U.S., the requirements from GATT (and WTO) and IMF recommended that Korea lift trade barriers which had benefited the Korean economy in previous decades. Korea agreed to reduce its average tariff by 54% in the completion of Uruguay Round in 1993 and further reduce tariff to zero in such sectors as electronics, construction equipment, medical equipment, steel, and pharmaceuticals. Korea's trade surplus began to shrink and turned to a deficit by 1991. In addition, its labor-intensive export industries faced critical challenge by the emerging cheap labor markets in China and South East Asia. The launching of the World Trade Organization (WTO) in 1995 and joining the OECD in 1996 posed even greater pressures on market liberalization.

The national campaign of *Segyehwa* ("globalization" in Korean) during the Kim Young Sam administration (1992-1997) espoused market liberalization and institutional reform as essential to enhancing national competitiveness. Market liberalization could be easily accepted as policy rhetoric, but not as actual policy programs. Protecting the domestic rice market, for example, was the flagship promise of Kim Young Sam's presidential campaign. Considering the symbolic importance of rice in the Korean culture, opening the rice market would have been a grave political risk for the political leadership. In December 1993, only months after his inauguration, the rice market finally opened via the agreements arrived at through the Uruguay Round of GATT negotiations. In his apologetic speech to the people in December 10, 1993, Kim Young Sam justified this by emphasizing that Korea must open the rice market in order to avoid isolation from the global market. Market liberalization was simply inevitable if Korea wanted to remain as a responsible member of the global market where its firms have to sell products such as autos and ships (Donga-Ilbo, December 10, 1993).

Responding to these unfavorable global market conditions, big businesses resolved to expand the overseas market. They changed their original stance against financial liberalization and demanded more deregulation which would allow them to borrow cheaper capital from foreign institutions. With the newly available foreign money, *chaebols* expanded their risky investments in new businesses such as shipyards, semiconductor and auto production plants. Consequently, their Outward Foreign Direct Investment (OFDI) radically expanded during the 1990s, when they shifted their production sites abroad to escape from unfavorable domestic conditions such as skyrocketing wages, labor-union militancy, higher interest rates, high transportation costs, and even government regulation (Kim S. 2000). The total portfolio investment was $2.5 billion in 1991, but it drastically increased to $29.7 billion at the end of 1994.[19] Korean banks' international liabilities increased by 49 percent from $21.7 billion to $32.4 billion for the same period. These massive foreign loans for global market expansion via OFDI were made possible by government guarantees (Kim, E. 2000).

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[19] With the selective financial liberalization in the early 1980s, the government began to sell shares of the nationalized banks. Preferential finance such as loans allocated to the economic projects by government fiat decreased. Its proportion of total domestic credit was reduced from 47.4 percent in 1980-4 to 28.1 percent in 1990 (Kim, E. 2001).

Liberalization, in theory, could have limited ever growing power of chaebols through market discipline. In practice, the big businesses were allowed more leeway to escape from regulations concerning wages and from the growing political demands of labor (Gills 1996). The campaign of “Rising National Competitiveness by 10%" promoted by the government, business and media during 1995 advocated wage freeze, deregulation, and low interest rates for business investment. Businesses tried to get the public to perceive that high wage levels were the main culprit of the costly and inefficient economy.[20] In the early 1990s, big businesses could raise capital from equity and corporate bond with the rise of secondary financial institutions. As they gained increasing profitability, they counted less on government subsidized finance.

2.3 Political liberalization, labor politics, and social protection

The success of the democratization movement in 1987 facilitated unionization, especially in the core export manufacturing industries such as auto, semi-conductor plants, and shipyards. The wage level kept increasing by total 4.5% during 1979-1987. And the stronger bargaining power of unions raised it even more by 8.4% during 1987-1995. With the internal labor market strengthened big businesses, the cost of firing regular workers was getting higher, the legal standard for corporate welfare was raised, and seniority wage system became more secure. Corporate welfare expenditure increased by 55% during 1987-1988 and the legal working hours decreased from 48 to 44 hours per week in

[20] The government and media coined the term of “four highs” to identify high wage, high interest rates, high land price and high transportation cost as weakening economic competitiveness.

1988, which raised labor costs (Jung and Cheon 2001). Accordingly, the reduction of labor costs became the primary goal of business as they were losing global competitiveness in labor-intensive and low wage industries and the global market for Korean exports were shrinking with intensified market competition from Chinese manufacturers. The cost of maintaining a rigid employment policy in the internal labor market became excessive in the late 1980.[21]

On the other hand, the democratic mandate drove labors to demand greater political rights. Labor empowerment after 1987 was not enough to institutionalize its full political representation because of three legal hindrances. First, labor unions were not allowed to engage in political activities. Second, multiple unions were not allowed in a firm, an occupational or an industrial sector. Only the state-controlled Federation of Korean Trade Unions (FKTU) could participate in negotiations and it often failed to represent the labor interest. Third, third party intervention was prohibited during labor disputes. Employers believed that multiple unions would strengthen the power of the radical union leadership of the Korean Confederation of Trade Unions (KCTU). They also worried that third party intervention would intensify industrial disputes.

There were endless political contentions and labor strikes over the conflicting labor reform initiatives all during 1996. To deal with these conflicting drives around the labor market, in May 1996, the Kim Young-Sam administration established the "Presidential Commission of Industrial Relations Reform" (PCIR). The commission

[21] To secure cheaper and flexible labor, big business began using low wage labor in developing countries by building their production sites abroad, recruiting foreign workers and managing the marketing and sales under its own independent management system.

consisted of 22 representatives from business, labor and civic groups. Its major goal was to gain consensus from affected groups to revise the labor law for greater flexibility. Labor desperately opposed the reform bills that endorsed a "no work no pay" principle, flexible layoffs, and working hours adjustments. In December1997, the reform bills proposed by the government were passed in the National Assembly without the participation of opposition party members.

The passage of this legislation spurred public outcry and enormous resistance from the labor unions. Facing unprecedented national strikes and public demonstrations in early 1997, the Kim Young Sam regime had to amend the passed bills. The implementation of massive dismissal was postponed for two years. The ban on multiple unions at the industry and national levels was lifted. This retreat did not appease labor. The national union associations kept struggling for the complete removal of the bills. The pre-crisis labor reform politics revealed the public rejection of employment liberalization despite almost a decade of government and business efforts to justify its necessity for economic competitiveness.

The labor market and the welfare system were strongly locked together during the high growth era. Heavy reliance on employment and corporate welfare had been associated with passive state welfare and privately financed social insurance programs. The pro-active redistribution through state welfare was not workable. Instead, social protection counted on increasing employment opportunities and price stability which were made possible by high economic growth. The state-led liberalization during the 1980s was combined with a strong policy imperative of improving income distribution. It entailed huge investment in education, housing and transportation systems. In the early

1980s, 17-19% of the government total expenditure was spent on education and vocational training to enlarge access for all societal groups. Building small and cheap housing units and enhancing public transportations aimed to improve the welfare of low-income groups. During this period, the percentage of national income held by the lower 40 percent of Korean households increased from 16.1% to 18.9%, while that of the upper 20 percent declined from 45.4 to 42.3 percent. This income distribution is second to that of Taiwan among the developing countries (Kim, K. 2003).

The pre-crisis social protection system had evolved under the government's strong regulatory authority and limited financial responsibility. It did not fully cover the general public equally. The National Health Insurance system had 420 insurance groups with independent financing and administration with a serious equity problem. Members in poorly financed insurance groups such as the rural regions had to pay more for the same benefits than those in the better financed groups. There had been advocates for integrating all insurance groups under one financial and administrative scheme. They argued that a single national risk pooling would promote redistribution without incurring financial burden on the government.

This initiative for integration had been repeatedly blocked by presidential vetoes and the objections of businesses and economic bureaucrats. The former opposed integration for fear of losing their control over contribution funds, which they often used for business operations (Jung J. 1995). The latter played a "gatekeeper" role to control any welfare expansion that might inflict financial burden on the government (Hong and Song 2005). With their strong ties with the presidents, they could persuade the presidents to veto the bills for integration. Previously, two presidents holding office from 1981 to

1992 vetoed bills to integrate health insurance groups for two reasons. First, the integration would weaken financial accountability of the insurance system. Second, integrating funds of different insurance groups would violate the constitutional right of private property: any surplus accrued from the members of an insurance group was the private property of its contributors. Therefore, the government had no legal right to control and reallocate those funds (Kwon, O. 2011). Unlike the labor market reform, welfare reform had hardly been a major policy issue before the crisis. Even the democratization movements led by labor, students, and human rights activists failed to politicize social policy issues since they were extremely politicized but not policy-oriented. This circumstance helped the government maintain its passive role in social protection based on financial austerity and accountability.

3. The Nature of the Pre-crisis Liberalization

Liberalization during the 1980s and the 1990s was initiated by both external pressure and internal initiatives. There had been consistent external pressure for opening financial market mainly from the U.S. Internally, businesses were increasingly attracted to funds available from global capital market to expand their overseas investments. However, liberal doctrines did not permeate the behaviors of financial institutions or markets but remained only abstract policy rhetoric. Neoliberalism was introduced as a foreign academic discourse to Korea during the 1980s and had become neither a valid frame of social realities nor substantial policy references by the late 1990s.

The concept of *neoliberalism* began to gain explosive attention in 1996 when both business and labor environments faced high uncertainties. Business leaders and the elite began actively propagating research, education, and publication to espouse neoliberal doctrines for market economy. The Center for Free Enterprise (CFE) was established in October 1996 to promote pro-business worldviews to the public and students.[22] The labor activists began to use the term *neoliberalism* when they criticized the state-business alliance and the *chaebol*-centered national economy. They saw emerging labor insecurity as the product of increasingly market-centered policies. Despite its increasing usage, neoliberal rationales had remained largely political rhetoric until the outbreak of the crisis in 1997.

The policy initiatives in the 1980s entailed many liberal-oriented policy measures but their underlying orientation was less shaped by ideological conviction than by practical rationality toward social and economic development. Liberalization in the 1980s aimed to promote efficiency, deregulation, and advancement of financial institutions. Despite its apparent liberal direction, the actual efforts were very gradual and cautious in critical areas (Kong 2012). Ambitious reform bills were often drafted in an ambiguous manner, making it easy for policy actors to circumvent them. Liberalization measures in the core financial domains were largely deferred. Reform initiatives such as *New Economy Plan* provided only cosmetic rhetoric of market liberalization without specific provisions and action schedules.

Even more active liberalization measures during the 1990s could not alter the traditional policy rationales. These measures fell short of expectations: there were

[22] Originally, the CFE had been a research institute that had worked for the Federation of Korean Industries (FKI), the main national association of business, but its mandate had expanded.

incomplete implementation or compromise with counter measures introduced by opponents of the reforms (Kong 2000). Both businesses and the majority of the bureaucracy did not welcome the abandonment of the traditional policy instruments. The liberal ideas as still abstract economic models had found few proponents among policy makers who were more concerned with the real problems involved with rapid liberalization and unregulated markets.[23]

The selective liberalization during the 1980s and the 1990s worked to benefit big conglomerates as the government still maintained substantial control over the financial sectors and shielded them from foreign competition. It was only a handful of the new U.S.-trained economic team who advocated market liberalization. The prioritized sectors were still protected and liberalizing measures were implemented only when they were compatible with existing interests and rationales. *Chaebols* were allowed to expand their business using debt to achieve even greater dominance in the market. The rhetoric of globalization explicitly proposed that *chaebols*' competitiveness was the indicator of success of the national economy.

Neither democratization nor globalization was successful at curtailing government control or disciplining *chaebols*. Korea had transformed from a comprehensive to a limited developmental state with the growth of *chaebols* and labor (Kim, E. 1997). While these growing forces were struggling to expand their autonomy, the government also wanted to keep major policy domains under its control. The

[23] The trade and financial liberalization had many risk factors. The growth of imported consumer goods might increase the trade deficit and short term capital inflows would cause inflation, severely disadvantaging unprotected sectors.

government-led liberalization attempts often aimed for more integrated control over financial markets which entailed intensive bureaucratic tug of wars.

The year 1997 was full of momentum for reform because of a series of economic scandals and bankruptcies of big businesses by their over-investment and high debt. These events revealed how the developmental nexus among government, banks, and businesses had generated near-fatal consequences for the Korean economy. Nevertheless, this momentum was not based on a clear diagnosis of reality nor on a coherent policy prescription for the future. Neither democratization nor liberalization created enough of an ideological binding force to push through any reform agenda. Therefore, the pre-crisis reform agendas were molded by competition and conflict of policy makers on rights, powers, and authorities. No single reform agenda was fully legitimized: each one was subjected to constant objections and veto constraints. With the absence of any hegemonic and coherent ideas, the major reform agendas were driven by long-term power competitions among bureaucrats, business, and labor embedded in local politics. Consequently, all the reform attempts were stuck in political gridlock, blocked by the persistent and growing veto powers of the opponents until the outbreak of the financial crisis.

CHAPTER 3

HEGEMONIC NEOLIBERAL IDEAS IN THE REFORM POLITICS UNDER THE IMF'S REFORM REGIME

This chapter examines the ascendancy of neoliberal doctrines in the policy discourse under the IMF regime, highlighting the features of *hegemonic ideas* operating in the politics of hard times. I start with describing how the economic crisis created massive momentum for radical reforms on both ideological and institutional grounds. I focus on how the "moral hazard" approach to the crisis legitimated neoliberal prescriptions as alternative policy frames and facilitated the acceptance of the harsh IMF programs. At the institutional level, the urgency of the crisis management created an effective reform-making environment. Finally, I discuss the nature of top policymakers' commitment to the IMF programs and neoliberal doctrines.

1. The Economic Crisis and the Rise of Moral Hazard Perspective

1.1 The economic crisis and social dislocations

In the history of Korea, the late 1990s economic crisis is marked as the greatest disaster since the Korean War. The IMF adjustment exacerbated social dislocations. Drastic tightening of loans and credit generated a severe credit crunch and an endless cycle of bankruptcy. The number of bankrupt firms in 1997 rose from 1,469 in November to 3,197 in December. Accordingly, the unemployment rate increased from 2.6% in 1997 to 6.8% in 1998 and even surged to a peak of 8.6% in early 1999, the highest since 1970. One and a half million people lost their jobs during the single year of 1998 (Lee, K. 2011).

Although the majority of financial and corporate restructuring measures targeted big businesses, small and medium sized firms went bankrupt much faster under the credit crunch. Accordingly, their demands for workers reduced most rapidly, which increased overall income disparity as it pushed down the lower tail of wage distribution. Korea's relatively sound income distribution represented by a low Gini index (0.292 in 1997) deteriorated. Since 1999, its Gini index has been fluctuating around 0.31. A drastic increase in unemployment led to income reduction. As many households had no earnings or reduced wages, about three-fourths of Korean households experienced an average income reduction of 44.2%. The poverty rate for urban workers' households reached a peak of 8.8% in 1998 and began to decline afterwards. The relative poverty ratio of households increased from 7.7% in 1996 to 11.5% in 2000 which was almost close to the U.S. level, one of the highest among OECD countries (Jang, J. 2011). By the end of 2000, the Korean economy had recovered almost to pre-crisis conditions. The unemployment rate began to decline, falling to 3.7% at the end of 2000. However, the crisis left its mark in the policy domains by calling into question the predominant policy rationales.

1.2 The rise of the moral hazard discourse

The IMF foisted painful policies on Korea during very short period time despite that the Korean society was not equipped to withstand the consequences. This radical imposition of free-market principle would not have been possible without complete internal disillusionment with the pre-existing policy paradigms. There were two key events which paved the way for the rise of moral hazard perspective, the Hanbo scandal and the Kia crisis.

The bankruptcy of Hanbo steel corporation in January 1997 is perceived as the starting point of the Korean economic crisis. Hanbo, the nation’s fourteenth largest conglomerate, had been favored in getting government approval for constructing a new steel mill after it contributed a massive political fund to Kim Young-Sam's 1992 presidential campaign. With its assets of about $100 million, Hanbo could borrow $6 billion for steel mill construction and bribed politicians and bankers to keep rolling the loans. With government guarantee, Hanbo and their lending banks could attract massive foreign investments. Foreign investors believed that they would be saved from the loss when anything went wrong in the invested projects. Korea First Bank, the lead lender among five major lending banks gave roughly $1.3 billion in loans, almost equal to the bank’s total book value. The bankruptcy of Hanbo had the potential to damage the already unstable economy. Moreover, Kim Young Sam's second son turned out to involve in the bribery scandal of Hanbo so the government did not let it go bankrupt immediately.

While the government was delaying its decision on whether it should let the company go bankrupt for several months, the major lending banks to Hanbo went bankrupt after their depositors withdrew their funds. The official remark from the Blue House (presidential office) that the creditor banks to Hanbo could default came as big surprise, especially to the foreign investors. Until then, major chaebols and their creditor banks could avoid default by government interventions and aids. In the given context, the default of Hanbo would signal that the conventional government guarantee would no longer be available, predicting more corporate bankruptcies ahead. During 1997, 10 out of the 50 largest chaebols were at the risk of bankruptcy.

Not surprisingly, Japan branches of Korean banks couldn't get short-term loans from Japanese banks after the Blue House remarks. The head of the Bank of Korea (BOK) immediately released an announcement that the BOK would guarantee the Korean banks operating in the foreign countries. However, the confirmation filed to ease the panics of foreign investors and banks on the accountability of the Korean economy. [24] After Moody's downgraded the creditor banks to Hanbo steel, the Korean banks began to apply extremely stringent lending criteria to firms and did not extend their roll-overs. In January 1997, Hanbo went bankrupt under debts of $ 5.8 billion, 22 times its equity.[25] Chung , the chairman of Hanbo, was sentenced to 15 years in prison and nine others politicians and top bankers were sentenced for their involvement in the scandal. The Hanbo scandal not only caused enormous financial troubles but also severely diminished the political legitimacy of the Kim Young Sam administration.

The Kia crisis was another critical event that made the public aware of structural problems in the economy. Despite growing overseas sales, the top three Korean automakers, Hyundai, Kia and Daewoo, were heavily in debt by early 1997 because they over-expanded their production capacities in both domestic and overseas plants. There had been excessive domestic market competition since the early 1990s while their labor costs kept increasing. Samsung's plan to enter the automobile industry also pressured them to expand their market share.

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[24] During the first quarter of 1997, the Japanese financial agencies withdrew about $4.7 billions from 12 Korean banks. Thus, the Bank of Korea had to deposit $ 1 billion to the foreign branches of the Korean banks and provided $12.3 billions to stabilize the currency market (Lee, K.S. 2011).

[25] Hanbo' over-investment could not expect to bring a profit because it would make the company pay the interest charge of $580 million a year, almost the same amount of the net profit by the nation's largest steel company, Pohang Iron and Steel *(New York Times, January 31. 1997).*

The Kia crisis became notable on June 23 in 1997 when Kim Sun-Hong, the chairman requested the government to pressure its creditors to extend loan due. In July 1997, the government and creditor banks placed Kia under the anti-bankruptcy pact so that the company could earn more time before its bankruptcy (Jung and Kim 1998).[26] Despite the government's additional $8 billion rescue funds to the banking sector, the top managers of Kia kept requesting more emergency loans. The creditor banks, however, had learned a lesson from the Hanbo scandal. The heads of lending banks to Hanbo went to jail for their lending decisions. The creditors to Kia could predict the same thing to happen if they funded Kia. Thus, they refused to make additional syndicated loans.[27]

Kia crisis revealed the dilemma of the government in managing high debts of *chaebols* and their fallouts: whether or not they should intervene and how much. There were conflicting pressures on the government. Domestically, Kia mobilized "Save Kia" campaign to pressure the government to offer "enough" assistance. Promoting the company's image as "Kugmin giup" (People's company in Korean), the campaign emphasized that Kia had a managerial structure that differed from typical *chaebols*: the firm had been run by professional managers not owner families and the employees constituted the majority of share-holders. The campaign organizers provoked public's

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[26] One of the underlying goals of anti-bankruptcy program was to leverage the position of creditor banks over borrowing companies. Even in their creditor position, each commercial bank had no control on the debtor companies. The government believed that if the banks could act as a group of creditors, they would exert more influences on the company in trouble to facilitate corporate restructuring or disclosures.

[27] Syndicated loan refers to the lending provided by a group of lenders. Arrangers, either one or several commercial banking institutions, should arrange and supervise the whole lending processes.

anti-*chaebol* sentiment by arguing that Samsung planned to takeover of Kia and the government would assist that plan by not helping Kia enough.[28]

Externally, global credit rating agencies, observing Kia crisis, downgraded the ratings of Korean banks. Foreign investors were losing confidence in the Korean economy, which in turn let to another economic blow to debt-laden firms. Ironically, the Korean government believed that it had to convince foreign investors of even stronger state guarantee for the possible bankruptcies in order to restore their trust. However, its confirmation only increased the suspicion of the foreign investors and banks. In October 1997, Kia collapsed with 10.7 billion dollars of debt and 60,000 jobs in jeopardy.
As S&P and Moody's downgraded Korea's credit rating, foreign investors kept withdrawing capital from the Korean market. Finally, the government made an agreement with the IMF about the financial bailout on December 3, 1997.

The Hanbo and Kia crises ignited moral panic over the corruptive alliances between government, banks, and chaebols. Hanbo and Kia had followed the path of the most successful industrial groups such as Hyundae, Daewoo and Samsung. To diversify business domains and expand market shares, they mobilized loans to fund their projects of constructing new steel mill plants (Hanbo) or acquiring a steel-manufacturing firm to establish new constructing and trading companies (Kia). Most of these new affiliated companies operated at a huge loss, causing the financial crisis of the mother companies.

[28] The campaign encouraged people to establish accounts in Cheil Bank, the main creditor bank of Kia, buy Kia automobile, and send letters to the major politicians to save Kia (Kyunghyang Shinmun, July 22, 1997).

(Table 3) Capital structure of the top chaebol groups (July 1997)

Group	Family Ownership (%)	Number of Subsidiaries	Liability Ratio (%)
Hyundai	14.6	57	436.7
Samsung	4.2	80	267.1
LG	6.1	49	346.5
Daewoo	7.1	30	339.5
SK	14.6	46	383.8
Ssangyoung	4.5	25	409.4
Hanjin	21.1	24	555.8
Kia	21.0	28	519.0
Hanwha	6.3	31	751.4
Lotte	3.4	30	192.2
Kumho	2.3	26	481.8
Halla	19.0	18	2,065.4
Dongah	12.0	19	354.7
Doosan	13.8	25	688.2
Daelim	9.1	21	423.2
Hansol	4.1	23	291.9
Hyosung	14.2	18	370.1
Dongkuk	18.5	17	218.4
Jinro	17.5	24	3,075.0
Kolon	8.6	24	318.0

Source: Fair Trade Commission, Rearranged from Lee, P.S (2000)

Large, highly diversified, family-controlled and high liability had been common business framework for the top *chaebols* before (even after) the crisis as seen in Table 3. The finance with state guarantee, over-investment and excessive debt ratio suddenly became the sign of business dysfunctions after the Hanbo scandal and the Kia crisis.

However, this moral panic still centered on the corruptive relationship at personal and organization level: a banker from a leading creditor to Hanbo committed suicide during the inspection and son of president Kim Young Sam went to jail. In April 1997, the official investigation of Hanbo Scandal by the National Assembly focused on de-legitimating the presidential power and exaggerating the ugly reality of corporations.

Under political pressure, the Ministry of Finance and Economy hired the Booz Alan & Hamilton consulting firm to identify the biggest economic challenges. The so-called "Booz Alan report" was published just before the crisis. It was taken seriously in the policy discourse as the more legitimate and impartial voice to clarify the structural problems. It argued that "the miracle of Han River was over" (Kim, S. 2005, 211). The Korean economy was being crunched between Japan with its high efficiency and China with its low wage labor. The report especially highlighted structural impediments in the financial and labor market and recommended extensive restructurings in those sectors.

1.3 The moral hazard approach to the crisis

The Asian financial crisis started in Thailand in the spring of 1997 and ended in Indonesia in 1999. The seemingly favorable economy of Korea experienced a total collapse. This economic turbulence made the norm of "contagion" receive widespread attention (Hausken, Kjell & Plumper 2002). Nevertheless, the international agencies provided the diagnosis and remedies of the crisis that highlighted "defective" domestic institutions of each country. The Korean policy actors had different approaches regarding what caused the crisis. A group of bureaucrats and academic elite criticized the poor crisis management of the previous regime in order to rebuild the legitimacy of newly launched Kim Dae-Jung administration.[29] On the other hand, labor union leaders argued

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[29] After two public investigations in 1998, a former deputy premier economic planning minister and a former economic advisor to the president, Kim Young Sam were arrested for their performances in the crisis management.

that the crisis was set up by foreign forces, mostly the U.S. and capital investors on the purpose of deterring the growing power of the Asian economy (Kim, J.H. 1998).

The *moral hazard* perspective was most powerful and widely shared account (Haggard and MacIntyre 1999). The concept of *moral hazard* was derived from finance. It refers to over-borrowing or excessive risk-taking activities motivated by an insured position. The story of moral hazard about the Korean crisis highlights that financial institutions and *chaebols* were prone to engage in risky investments, taking advantage of their insured position by the government guarantees. Government guarantees for the liabilities of financial institutions pose a serious moral hazard problems (Krugman1998): the government's implicit guarantees to favor strategic projects encouraged business managers to take excessive risks in their investment (*The Economist*, November 15, 1997). The creditors of the Korean banks believed that they would be safe from risk. Consequently, financial institutions had less incentive to manage risk stringently in their investment and lending.

In sum, moral hazard embedded in the developmental alliances of government, bank, and *chaebols* became the main culprit for the economic catastrophe. It was the official opinion of the IMF, and was shared by mainstream policy elite in Korea (IMF 1998b). For the question of why this happened and how we should deal with it, even left-oriented intellectuals and civic activists joined moral criticism on the state-chaebol alliances. They shared the same position about the IMF programs: Korea had to convince the IMF of its commitment to restructuring so that it could get bailout funds for recovery (Dong-A Ilbo December 15, 1997). Commentators agreed that the crisis was inevitable and that it provided the chance to fix deep-rooted institutional defects. Newly elected president Kim Dae-Jung acted as the most ardent critic of *chaebols*. In his inauguration speech held in February 1998, he argued,

> "We must calmly look back to find out how we have arrived at this stage of affairs. This unfortunate development would not have taken place if the political, economic and financial leaders of this country were not tainted by a collusive link between politics and business and by government-directed banking practices and if the large business groups did not have a large number of uncompetitive subsidiaries.…. I cannot help but feel limitless pain and anger when I think of you, the innocent citizens, who are bearing the brunt of the suffering over the consequences of the wrongdoing committed by those in leadership positions."

The unified ideological attacks on the domestic institutions after the crisis differed from the previous criticisms. Centering on how to make the economy competitive, the 1990s policy discourse selectively adopted neoliberal doctrines to problematize wage increase or excessive government regulations. The legitimacy of those claims came from the goal of national competitiveness, not the virtue of neoliberal ideology itself. As far as they contributed to strengthening the economy, less market oriented practices could be tolerated. *New Economy Plan* launched in 1993 is a good example to show the nature of the pre-crisis economic reforms. It aimed toward making the Korean economy more competitive and suggested fixing structural impediments. The plan had an agenda to correct uncontrolled business diversification of *chaebols* and ownership structure. However, it ended up with a cosmetic reform of "many words, no deeds."

In contrast, the crisis discourse of 1997 and 1998 celebrated the fundamental neoliberal norms. This was most well represented in the perception about the *chaebol* problem. Anti-chaebol sentiment was a key component of moral hazard discourse emerging with the crisis. The policy leaders and elite espoused the model of Anglo-

American institutions and advocated *Global standard* as embodying the Anglo-American priority on efficiency, transparency, and accountability (Lim and Jang 2006). Taking advantage of the pressure by the IMF, Kim Dae-Jung could initiate the ambitious plan to discipline *chaebols*. He believed that foreign investors could be the effective agents for disciplining *chaebols* by introducing the Western business standards in managing profits and risks. In a televised national forum aired on 11 May, 1998, Kim Dae-Jung was challenged that foreign investment may colonize the national economy. He responded by asking "all the South Korean investors in Britain make Britain a Korean colony?" Then, he emphasized the potential benefits in jobs and technology that would come with foreign investment. In sum, the formidable backlash against the "developmental" arrangement led to the acceptance of neoliberal orthodoxy as an alternative policy frame even when it was locally detached and empirically untested. The IMF programs were unwelcomed but seen as the necessary and painful steps toward a recovery and further growth.

2. The IMF Programs and Neoliberal Doctrines as Hegemonic Ideas

2.1 Economic crisis and neoliberal doctrines as hegemonic paradigm

In periods of social and cultural transformation, highly articulated, explicit, and organized ideological systems emerge to suggest new strategies of action (Swidler 1986). Clear and coherent neoliberal ideas have been appealing because they suggest a road map during a time of high economic uncertainty. Countries that have entered into negotiations with the IMF were experiencing acute balance of payment problem, trade deficit, erosion of external reserves, rising inflation, and slow growth. The policymakers in these countries desperately need diagnoses and prescriptions. The IMF intervened to provide seemingly the most coherent programs for recovery. The IMF usually sees an economic crisis as the symptom, not the cause of problems. The greater consumptions and investments than the real growth of national product generate economic deficiencies. Thus, the IMF applies stabilization package that imposes high interest rates, cuts public expenditures and increases taxes. These measures are expected to restrain credits, allocate resource efficiently and reduce public debts (Polak 1997).

In approaching the Korean economic crisis, the IMF promoted the neoliberal rationales as the primary account of why the crisis happened and what should be done for a sustainable growth in the future. It debunked the "developmental" logic embedded in the Korean economy. The then IMF managing director, Michel Camdessus defined the crisis as a “blessing in disguise” arguing that the crisis initiated restructurings that would strengthen the economy in fundamental ways after painful adjustments (IMF 1997). He proposed that the IMF should maintain the momentum to go beyond temporary stabilization programs and make the system operate on the Western model.

The Korean economy was built in a substantially distinctive state-market relationship from the Western model. There has been a debate regarding the nature of state intervention in the economic success of the East Asian countries. Two contradictory views of neoclassical versus revisionist approaches dominated the debate. The World Bank’s *The East Asian Miracle* (1993) represents the neoclassical view that the frequent government interventions in the East Asian economy were not harmful because such intervention as government subsidy was basically market friendly: it was used to assist the most efficient players and its distorting effect on price was minimal. High reliance on international trade was the main component of the policy recipe for the high economic growth. In contrast, the revisionist approach argued that the developmental states used highly extensive market interventions that strategically and selectively targeted particular industrial sectors. The governments led the orderly development by actively acquiring necessary technologies and allocating funds for promising projects. Their active interventions could transform economic structure more effectively than market mechanism could do (De Long and Summers 1991).

As for the Korean experience, it is hard to characterize the nature of state intervention by one definitive orientation. Korea achieved macroeconomic stability following the orthodox neoclassical path by maintaining conservative fiscal policies and competitive exchange rates to avoid high inflation.[30] On the other hand, the Korean economy diverged from the orthodox path by engaging active state interventions such as repressing interest rates, making heavy use of subsidized credit, and interfering with investment decisions of businesses (Rodrik 1996, 18). In sum, it employed hybrid policies which concurrently confirm and diverge from the neoclassical policy rationales (Chu 2000). Whether it be praise or criticism, theoretical discussions could not dispute the central role of state-led industrial policy in explaining the success of the Korean economy. Its policy rationales had never been fundamentally denied in its critical contribution.

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[30] Neoclassical economics rejects the Marxian premise of exploitation. It justifies existing wealth as the outcome of market exchanges that is fair and just. Drawing upon principles of neoclassical economics, neoliberal policy rationales advocate the dominant role of market mechanism and suggest that governments should minimize its intervention in market by reducing its spending, limiting subsidies, and opening market to more trades.

The national campaign of *Segyehwa* (globalization in Korean) was launched in the early 1990s. Its main premise was that “national competitiveness” can be achieved only by market liberalization and domestic institutional reforms. This seemingly liberal initiative was in practice was state-led project that aimed to make Korea a first-level nation (Kim S. 2000). In this sense, Korea's endogenous liberalism was imbued with a more practical and nationalistic orientation than the Western liberalism. During the pre-crisis liberalization in Korea, liberalization measures failed to establish market discipline in the financial and corporate systems and the collusive ties between government and business persisted.

The 1997 economic crisis radically transformed endogenous liberalism in Korea into a "showcase neoliberalism" in which neoliberal doctrines as an ideological orientation dictated the reforms without concerning their relevance to the local context. There were criticisms that the IMF conditionality imposed on Korea was much stricter than those for other countries and clearly inappropriate for the Korean context (Feldstein 1998). Sachs argued that the IMF’s insistence upon structural restructuring caused Korea to carry out unnecessary and costly policy changes given that the crisis was basically temporary liquidity problem (Sachs 1997).

The resistance to the IMF regime was most actively demonstrated by the organized labor. In January 1998, the Korean Confederation of Trade Union (KCTU) mobilized street demonstrations across the nation. In February 1998, twenty four labor, civic and professional groups launched collective movement to counteract the labor restructuring. Their demands centered on withdrawing collective dismissal with stringent corporate restructuring and reliable unemployment programs. Dismissed workers or employees under threat of dismissal joined increasing number of small-scaled demonstrations. Demonstrating resistance to the IMF restructuring had to deal with negative perception that it would not help country overcome the crisis by causing social instability. Social commentators in mainstream media emphasized that labor disputes and people's resistance would deepen foreign investors' suspicion about the Korean economy (Dong-A Ilbo, May 4 1998).

Progressive intellectuals had dilemma in criticizing the IMF restructuring. They inadvertently took the side with the IMF in financial and corporate reforms. The best example is "small shareholder movement" initiated by the People's Solidarity for Participatory Democracy (PSPD). PSPD is one of leading civic organizations which aimed to promote justice in the Korean society. As ardent *Chaebol* reformer, the PSPD led the "small shareholders movement" and succeeded in collecting sufficient votes of minority shareholders to request a shareholders' meeting where they could monitor and challenge the decisions of the top management of *chaebols.*

This movement was controversial. As argued by Ha-Joon Chang, a prominent economist at Cambridge University, the Korean small shareholders and foreign investors were working together to challenge the existing *chaebol* ownership, advocating shareholder-sovereignty, one of the controversial neoliberal doctrines. He criticized that this movement actually would contribute to intensifying neoliberalization in the Korean economy by favoring the interest of speculative foreign investors (Hankook-Ilbo, February 11, 2011). During the crisis, fine line between "good" liberalism and "bad" neoliberalism put leftist and progressive intellectuals in a dilemma over how to criticize the government and chaebols without relying on market-oriented disciplines (Song, J. 2009, 123-124).

The exceptionally harsh conditionality was implemented for a short period of time. Under the guidance of the IMF, the new regime set the direction of massive reform project that differed from the previous reform initiatives. The policy makers, before the crisis, had employed hybrid policy tools as far as they were effective for achieving the situational goals in each historical context. With weak commitment to liberal economic ideology, market liberalization during the 1990s did not directly challenge the government's strategic intervention and moral hazard practices in the financial sector. The post-crisis reform started with reform agendas that demonstrated policy priorities to celebrate neoliberal values. Moreover, it was clearly planned by a package of neoliberal prescriptions to replace "arbitrary" state intervention with market disciplines. There was lack of contradictory discourse which competed for hegemony in the policy discourse, blocking sufficient discussions and negotiations among different policy groups.

2.2 The IMF programs and the neoliberal doctrines

IMF intervention is often legitimated by its apparent confidence in solving economic turbulences. Despite its ideological clarity and logical consistency, the actual effects of IMF programs have been less than convincing. An empirical study found that IMF programs solved balance of payment problems but did not improve macro-economic conditions indicated by inflation, investment, and economic growth (Shadder 1995). They had even negative effects on economic growth since reduction on public investments and high interest rates often deter economic growth (Blejer and Cheasty

1991).[31] However, borrower countries often had no choice but to accept IMF programs. The IMF's messages to creditors and investors critically influence national credit rating, which in turn affect the ability of the government to borrow in the capital markets to finance current account deficits. Accepting the programs is a signal that a borrower country is committed to its obligation to repay debts and build safer environment for investment. Given these pressures, domestic policy actors are left with limited room to veto IMF conditionality.

Domestic politics shape the context of accepting IMF programs. Market liberalizations in the Latin American countries were guided by a group of economic technocrats embracing the Washington consensus. In Mexico, policy technocrats who had a shared mindset with IMF officials actively implemented the neoliberal prescriptions. Plural ideological positions among policy actors created more critical views of the program. The dominance of liberal elite in policy domain declined with the democratization in Mexico. The diverse interpretations of the debt-crisis questioned the necessity of radical structural reforms suggested by the IMF (Jorge 1985). IMF programs assigned to an economic crisis were sometimes highly accepted by the public as found in Eastern Europe after the collapse of communism. The majority of politicians agreed that the institutional legacy of the communist era was the root of economic hardships. The ideological shift toward the Western liberalism in the region helped the public accept that

[31] However, the Articles of Agreement indicates that the IMF should provide members "with opportunity to correct maladjustments in their balance of payments without hurting prospects for economic growth." Michel Camdessus, the IMF Managing Director from 1987 to 2000, confirmed that IMF programs aimed to promote "high quality growth" which is not growth only for the privileged few, leaving the poor with nothing but empty promises" (IMF 1997).

IMF programs might be painful in the short run but would bring economic growth in the long run.

The acceptance of IMF programs was highly enforced in Korea. The United States Department of Treasury confirmed that it would not offer any assistance unless Korea implemented structural reforms under the IMF programs (NA: Special Committee, January 25, 1999). The IMF asserted that offering the bailout funds would be strictly contingent on regular monitoring and evaluation on Korea's compliances to the conditionality[32]. All the bailout funds would cease if Korea failed to achieve the conditionality sufficiently (IMF 1997). The IMF organized rescue funds of $57 billion from itself, the World Bank, the United States, Japan, and others creditor institutions. This could ease the foreign currency shortage and stabilize exchange rate by making private borrowers pay their currency debts.

In return, the IMF required that growth rate should fall from 6% in 1997 to 2.5% in 1998 and inflation rate should increase from 4.2% to 5.2%. Interest rate reached as high as 25% at one point in 1998 by the IMF guidance. These short-term goals required a draconian monetary squeeze in the midst of a brutal Korean currency depreciation. Korean corporations had maintained a high debt to equity ratio so high interest cost resulted in a surge in business defaults. The IMF prescriptions for Korea were described as "overkill" for "an economy that was rightly judged to be pursuing sound

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[32] Stanley Fischer, first deputy managing director of the IMF (1994-2001) argued that the IMF's macro-economic programs for Asia was appropriate to their circumstances because only fundamental structural changes would bring the sustainable return of growth in the region. Therefore, he argued that IMF lending should be strictly conditional on policy changes, not too easily available (Conway 2006).

macroeconomic policies just months earlier". The IMF's insistence upon market restructuring caused the country to carry out unnecessary and costly policy changes despite that the crisis was basically temporary liquidity problem (Sachs 1997).

The IMF programs were not only externally enforced but also internally justified in policy discourse. President Kim Dae-Jung confirmed that Korea should use the IMF programs as the tools for advancing the economy. You Jong-Keun, DJ's economic advisor and the governor of North Cholla Province, was regarded as the most like-minded figure to DJ and a Korean version of Milton Friedman. He emphasized that the economic crisis should be the starting point of thorough transition to a market economy. In his interview with *Fortune*, Governor You stressed that "the era of strong-armed intervention is over. The market will be the only and final judge of business decisions." (*Fortune,* May 2, 1998). He rejected the criticism that the IMF programs were not adequate to Korea's local institutions. He believed that the Asian economic crises were attributable to an Asian mode of practices which failed to follow economically rational standards and calculations. He further argued that the primary goal of business should be to create profits not to serve country. In this sense, foreign investments and their increasing influence on the Korean firms and banks should not be problematic (The Kyunghyang Shinmun January 14, 1998).

The IMF applied a package of programs under explicit neoliberal orientation. Its programs across countries shared the basic norm of reducing government roles, expenditures, and budget deficits. The IMF intervention in Korea was harsh in that neoliberal principles dictated the direction and scope of restructuring with little concern for local norms and practices. Its strict provisions greatly contradicted the existing institutions. To enact fiscal austerity, the IMF recommended tax increases despite the fact that depressing economic condition made it harder for the government to increase tax burden. Traditionally, Korea maintained tight fiscal policies with low level of government spending and debts. The government spending in the welfare had already been among the lowest. The financial crisis had nothing to do with either excessive government spending or debts.[33] The most destructive yet non-negotiable requirement was high interest rate policy. The interest rate which was about 12% before the crisis, reached as high as 22% at one point in 1998. This new rate was destructive enough for typical Korean firms operating on high debt to equity ratio. Even the financially sound firms could not survive with such a rise in costs.

The neoliberal emphasis on efficiency, accountability, and transparency no longer remained normative rhetoric. Stringent capital adequacy rules placed banks and firms into turbulent processes for a short period of time. The BIS (Bank for International Settlements) ratio which is indexed by the ratio between risk-bearing capital and risk-weighted assets, was a key instrument in financial restructuring. To get rescued, major banks should make their BIS ratio higher than 8%. This measure dramatically changed bank’s lending practices. Commercial banks desperately decreased their risk-weighted assets by reducing their lending to corporations and increased safer investment. This change caused serious damage to a majority of firms under high liquidity pressures. The corporate defaults, in turn, pressured the banks to constrain corporate lending even more.

[33] Eighty percent of the total foreign debts of the country were incurred by speculative investments of the private sector which borrowed cheap short-term loans mostly from Japanese banks and lent them as the expensive long-term loans to the South Asian countries.

Another important capital adequacy measure was the rule of debt to equity ratio. It aimed to discipline business practices on high debts. While the average debt-ratio of the top 30 *chaebols* amounted to 518% before the crisis, the government set 200% limit. There was no scientific ground to justify this limit. According to Lee, the first chairman of the Financial Supervisory Commission, the limit of 200% was set in tandem with the practices of other advanced countries (Lee, H. 2012): the average debt-ratio of the U.S. corporations was less than 100 % and that of the Japanese firms was 150-200 %. *Chaebols* found this new unilateral limit not only unreasonable but also unfeasible. Construction and heavy industry businesses complained that the rule was unfair for their industries which need massive capital investments to initiate and sustain the business.

New rules were introduced to govern disclosure, accounting, auditing, risk assessment and pricing in corporate management. A firm had to provide official statements audited by internationally certified firms and publish key data on non-performing loans, capital adequacy, ownership structures and affiliations. Board system and outside directors were empowered to monitor and guide management. Previously, political connections had been critical in the appointment of top bank positions. Accordingly, appointed bankers were hardly autonomous in their lending decisions but provided 'policy-directed' or 'politically favored lending' excluding shareholders from management of commercial banks. In 1997, outside directors representing shareholders could join the process of appointing board members. This change was supposed to limit the government interventions in credit allocation (Lee P. 2000).

It was expected that newly empowered boards and outside directors set new managerial priority on shareholders' interest, following the U.S. corporate norm which assumes share-holders as real owners of a firm. This norm had been quite weak in the Korean context where the founding-family exerted actual ownership by dominating management. The most insisting requirement from the IMF and the U.S. was trade and capital liberalization. Policy makers obsessively emphasized foreign investments assuming that they would bring global standards to upgrade the financial and corporate governances. Accordingly, foreign investors were granted the exclusive advantages over domestic investors.

However, Korea’s radical reform initiatives didn't directly improve its national credit rating. The rating increased twice only when two major banks were acquisitioned by foreign capitals. In July 1998, Commerzbank, a German bank acquired the Korea Exchange Bank (KEB) to become its major shareholder. The KEB was sold at a fire sale price with the assistance funds from the Korean government. Likewise, the Cheil Bank was sold at low price to Newbridge Capital in 1999. Given that the most urgent goal of the whole restructurings was to restore confidence in the global market, these two acquisitions were promoted to demonstrate Korea’s reform commitment with little concern for the profitability of the deals.

2.3 The reform making institutions in the crisis politics

The normative goal of departing from old institutions constituted the main drive in the post-crisis reform landscape. Celebrating new rationales, the IMF programs played as coherent action plans for the policy actors. Despite its drastic and coercive manner, the resistance to the IMF programs was manageable. Even progressive elites and activists enthusiastically joined the criticism on the government and *chaebols* rather than the IMF and its programs. Unilateral criticism against the old institutions marginalized the alternative interpretations of the IMF regime, accepting it as necessary adjustment.

Along with this ideational environment, the political context of crisis management created favorable condition for radical reforms. Considering all the failures of Kim Young Sam regime in its major reform efforts, the achievements of the Kim Dae-Jung administration could not be imagined without the economic crisis. One of the gravest crises in a half century created a new context for the ever weakening state policy capacity. Before his presidency, Kim Dae-Jung's party, the National Congress for New Politics (NCNP), took only 26% of the seats in the legislature, forcing him to form an alliance with the opposing but conservative United Liberal Democratic (ULD) party. The NCNP-ULD coalition was still short of a majority in the legislature. This coalition was very shaky because of their different regional bases and ideological orientations.

However, the crisis enabled the Kim Dae-Jung administration to gain enormous policy autonomy over domestic actors, especially business powers, labor, and anti-reformist bureaucrats who blocked the reform initiatives during the preceding regimes. The urgency of crisis management often created a political opportunity for government (Tilly 1975). The power of the president was maximized to the extent that Kim Dae-Jung could enforce centralized bargaining and trade-offs among the groups with conflicting interests. He launched the temporary but powerful task force teams such as 12 People's Emergency Task Force. He prodded policy actors to draft reform bills and pushed them to 'fast track' the legislation.

Kim Dae-Jung empowered the Financial Supervisory Commission (FSC) that was newly established in 1998. It pushed for radical corporate and financial restructuring, defying the resistance from anti-reformist bureaucrats and business associations. The FSC, backed by the full support of Kim Dae-Jung, achieved more than suggested by the IMF. A total of 171 financial institutions including five major commercial banks were closed down or suspended by 1999. Later, the IMF showed satisfaction with Korea's observance of international standards and codes especially in the financial sector, stating in its report that "this sector has undergone significant consolidation: banks have become more profit oriented, cutting costs, streamlining their operations, shedding staff, and consolidating branches…. Foreign participation in the banking sector has tripled since 1996" (IMF 2003).

Although the crisis environment created a breakthrough to stalled reforms, changing the labor market was the biggest challenge for Kim Dae-Jung, an iconic leader in the democratization movement. Facing pressures from the IMF, he had to abandon his personal policy priority of protecting employment security. The IMF conditionality proposed that labor market should become flexible by lifting restrictions on dismissal. To ease the burden of layoffs and expedite reemployment, the IMF recommended vitalizing employment insurance programs (Yun, J. 2008). As an elected president, Kim Dae-Jung publicly stated that if necessary for global competitiveness, wage reductions and massive layoffs should be tolerated (Daily Chosun, Dec. 25 1997).[34]

Specifically for the task of labor reform, Kim Dae-Jung launched the Tripartite Commission one month before his inauguration. The commission had an evenly balanced

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[34] Under the Kim Young-Sam government, Minister of Labor Jin Nyeom played leading role in revising the Labor Standards Act. At that time Kim Dae-Jung criticized him. However, Kim appointed Jin as the Minister of Planning and Budget in 1999 (Yun 2008).

composition among government, business and labor.[35] By bringing together the representatives of labor, business and government, the Tripartite Commission acted as a "peak bargaining arrangement" (Cumings 1998). The government could use the commission as its organizational legitimating device. Its deliberations focused on how to compensate labor enough to make them accept the legalization of massive dismissal. Each representative group had to negotiate on 90 major agendas within a very short time. After conflicting and frustrated talks, an agreement was finalized in the name of "Social Agreement to Overcome the Economic Crisis" that planned to legalize collective dismissal on February 6, 1998. The threat on traditional job security was to be offset by the expansion of labor's political rights and the enhancement of the social security system, including the integration of the health insurance system (Wong 2004).

In sum, the maximized presidential power and minimized interest politics created effective reform making environments. Major reform bills blocked for a decade were immediately passed by the National Assembly which was summoned to pass the legislations required for the IMF conditionality. The traditional veto powers against the reform initiatives were temporarily paralyzed within an insulated policy making domains and fast-track legislative processes. Most of all, the urgency of crisis management was the most binding force behind all these temporary dynamics.

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[35] With the vice president of the ruling party serving as chairman, 11 members from different bodies participated: labor representatives from the FKTU and the KCTU, business representatives from the FKI (Federation of Korean Industries) and the KEF (Korea Employers Federation), government representatives (the Ministers of the finance and labor departments) and the representatives of ruling and opposition parties.

2.4 Incomplete ideological conversion to market discipline

Disillusionment with old institutions was a crucial ideological force in the post-crisis transition. However, it did not guarantee a wholehearted embrace of new institutional frames. Neoliberal doctrines still had a long way to go before their full institutionalization as permanent policy rationales, especially among the policy makers. In 1998, the Bureau of Auditing inspected the top policy makers' crisis management and the National Assembly formed a special committee in 1999 to investigate what caused the crisis. These investigations revealed that the top economic bureaucrats did not share the dominant moral hazard criticism that domestic institutions were the main cause of the disaster. They held the view of "good fundamental" emphasizing that the Korean institutions were working properly to generate sound economic performances. Even right before the crisis, the Korean economy showed sound economic performances with 6.8% GDP growth rate, 2% unemployment rate, and 4.9% price increase rate. An increasing trade deficit, a high risk investment situation, and decreasing business profit rates were existing as risk factors but the bureaucrats regarded them as more like cyclical risks. They saw that the root of the disaster lay in not the institutional pitfalls, but a very specific practice: *chaebols* and financial institutions borrowed short-term foreign debts which far exceeded foreign exchange assets. The creditor banks' refusals to roll them over generated temporary and acute liquidity problem, but it was not the fundamental insolvency. This claim was completely overshadowed by the political drive to find the target of blame (NA: Special Committee, January 25.1999).[36]

The top economic bureaucrats had to act as the forefront agents who should not only demonstrate their full commitment to but also actualize the IMF programs. They perceived the situation as *a crisis of trust* believing that restoring confidence from the foreign investors by raising credit rating was only way to overcome the crisis. However, even after Korea made an agreement with the IMF on the rescue fund, the major credit rating agencies lowered Korea's grade, labeling the country as inappropriate to invest in. Facing the unfavorable responses, the top economic officials complained that the global media agencies such as the Wall Street Journal or Bloomberg viciously exaggerated the dysfunctions of the Korean economy using unidentified information (NA: Special Committee, January 25, 1999).

Commercial banks from the G-5 countries (the United States, the United Kingdom, Japan, Germany, and France) held the majority of the short-term debts of Korea and they were still suspicious about whether Korea had actually followed the IMF requirement (*The Wall Street Journal*, Dec. 11, 1997). To earn a back-up guarantee from the shareholders who were still hesitant, the IMF-Korea's negotiation team had to make even more stringent conditionality in order to improve the prospects of the IMF bail-out projects (Copelovitich 2010). The top bureaucrats orchestrated the radical restructurings

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[36] The whole investigations to identify who was most responsible for the crisis concluded that there were both internal and external causes. Domestic banking and financial systems generated nonperforming loans and the panic of international lenders and the harsh credit ratings contributed to exacerbating the crisis. In addition, the rapid market liberalization without sufficient preparation, the top officials' poor advising of President Kim Young Sam, and delay in receiving the help from the IMF programs were criticized as contributing factors (NA: Special Committee, January 25,1999).

and even more liberalizations for the practical purpose of raising the credit rating and receiving bailout funds. The elected-president Kim Dae-Jung kept affirming his commitment to the IMF programs, taking a tough stance on all major restructuring despite that they were expected to cause enormous social turmoil. The reform efforts played as messages to the global market which was deemed more important than the original goals of the reform itself.[37]

The perceptions of the top economic bureaucrats suggest that their commitment to the IMF programs and neoliberal doctrines was heavily driven by the pragmatic goal of stabilizing the economy. When it comes to the internal politics, they attempted to use the economic turbulence as the opportunity to regain their control over the financial and corporate sectors. Kang Kyung-Sik, the Vice Prime Minister of Economic Affairs (March-December 1997) was seen as "fake market fundamentalist" from liberal oriented elites. Although he kept advocating "market economy" in his speeches and interviews, he believed that only comprehensive and effective government intervention could achieve the goal of building a market economy. He was obsessed with the legislation to integrate financial supervision under the Ministry of Finance and Economy. He asserted that the reform to integrate authority would be only way to solve the existing problems of the Korean economy.

Kang's vision represented typical orientation of the top economic bureaucrats. They had always come up with the government-led plans as seen in the cases of New

[37] Contrary to the bureaucrats’ expectation, as of October 1997, the majority of fund managers on Wall Street were already aware that the Korean economy would be in deep trouble regardless of its reform efforts. The top inner group in the Wall Street had already decided to withdraw their funds and set the schedule to do that (NA committee: January 27. 1999).

Economy 100 Day plan in early 1990s or the campaign of “Rising National Competitiveness by 10%” in mid 1990s. This policy orientation to emphasize bureaucratic leadership dominated the state-led globalization and liberalization projects before the crisis. These campaigns did not constitute a real institutional shift to market economy.

Right after the 1997 economic crisis, the central/local government agencies, civic organizations, and corporations initiated campaigns for "Saving Our Economy." Aiming for rapid economic recovery, these campaigns centered on austerity by curbing consumption. The most famous one was the campaign of “Collect Gold for the Love of Korea.” Ordinary citizens donated their gold ornaments to augment the nation's foreign exchange reserves. Other campaign-like collective actions included trimming salaries in companies, postponing children' study abroad, constraining the purchase of cars and clothes, removing lights in offices, and using public transportations. These self-disciplinary austerities in behaviors had nothing to do with market discipline. On the contrary, the restrained consumption would strangle the already serious liquidity problems in the economy. The campaign fever revealed that the public approached the crisis as the national hardship to overcome and got back to the old legacy of goal-oriented collectivity for hard times. In the context of crisis management, there was limited room for market discipline to create substantial change in people's perceptions and behaviors.

Neoliberal discourse achieved hegemonic status with a blind faith in “global standards” which led to ideological attacks on the old state-centered institutions. It has been agreed that Korea became more "neoliberal" in its economic and social institutions after the crisis. Still, it is not clear what this neoliberal transition actually signifies. To understand the nature and scope of the ideational power of neoliberalism, it should be examined to what extent reform agendas could permeate to policy domains after the acute crisis dynamics. Institutionalization of free-market ideas requires more than an intellectual hegemony. The next chapter asks whether the powerful neoliberal ascendancy combined with the IMF enforcement ended with altering key policy rationales and practices concerning government and market relationship.

CHAPTER 4

INSTITUTIONAL ETHOS OF GOVERNMENT INTERVENTION AND PRIORITIZATION

1. The Persistence of the Developmental Policy Rationales after the Crisis

This chapter discusses incomplete implementations of the major reform agendas in the financial and corporate restructuring. I attend to the "developmental" policy ethos behind the reform in the making: how they shaped strategy, preferences, and the path of the post-crisis transition. Swidler argued that we see the continuity of an ethos in action despite conversion in ideas and values. During a cultural transformation, “ideology forms around ethos, rather than vice versa” since commitment to a specific ethos which regulates action shapes the selection and development of a doctrine (Swidler 1986, 276-279). A country tends to experience a gradual return to its conventional paradigm as new ones cannot gain full credit for its validity or effectiveness for long-term basis (Hall & Soskice 2001). It is not easy for new rationales to become entrenched in an almost reflexive way among participants in political processes. These theoretical insights raise a question regarding the extent to which neoliberal impulses created changes in long-term institutional ethos that governed the government-market relationship in Korea. Identifying change or continuity in the developmental policy ethos helps us better understand the nature and scope of the historical transition facilitated the crisis and the IMF reform.

I extend the analysis into the institutionalization of reform agendas. Institutional change is not entirely shaped by a master plan or a coherent ideological orientation. Pre-existing political culture, emergent contingencies, and sectoral responses may work against a master plan across different policy domains. This chapter starts with addressing major reform agendas that were driven by neoliberal imperatives. They include small government, fiscal austerity, bank autonomy, capital adequacy, corporate transparency, and capital liberalization. These agendas challenged the developmental policy rationales based on the spirit of "government may intervene if necessary." I identify key developmental rationales that characterize the government intervention: the pragmatic policy orientation and strategic protection of core sectors. How did these long-term policy orientations, preferences, and tools compromise the implementation of the key reform agendas?

1.1 Small government doctrine: the administrative reform

Since the Korean government had maintained a low level of public spending, the criticism of the government was focused on its excessive regulatory control. After the presidential election, Kim Dae-Jung confirmed that he would initiative a “revolutionary” government restructuring to realize a “small and efficient government.” He emphasized the delegation of government functions and authorities to private sector and local governments. However, the efforts were limited to reducing the size of government staffs by eliminating the least powerful agencies or firing the lowest rank female workers. The size of agencies and staffs were recovered by the end of the Kim administration. Moreover, the central government agencies were more empowered by increase in the number of regulations and budget increase (Kim, K. 2005).

In May 1999, the Kim Dae-Jung administration established the Civil Service Commission (CSC). As the highest personnel authority, the CSC set the direction for the civil service reform: the Korean bureaucracy should move from rank and seniority to performance based system.[38] Highly influenced by global trends in human resource management, the CSC adopted strategies such as changing civil service examination, recruiting private experts to the government, and building performance based promotion and reward system (NA: CSC committee. November 4, 2000).

The Korean executive bureaucracy is highly prestigious and internally cohesive group. They are recruited through merit-based open competitive examination. Anyone can apply for the examination regardless of their personal background, gender, school, and region. The civil service examination is classified into three levels according to the entering grades. The Senior Civil Service Examination is for the highest entering grade (Grade 5: junior manager level). The examination selects successful applicants by their exam scores only, which is considered fair and objective. It is highly competitive and effective in recruiting the most talented young applicants to the managerial civil service positions. Open competitive examination contributed to establishing the merit system and professionalism of the Korean civil service. It also created a coherent group of bureaucrats who had high pride in their jobs. They enjoy a high degree of job security and automatic promotion by strict seniority and rank system. However, there are downsides to maintaining a prestigious and cohesive bureaucracy. The civil service has

[38] The CSC had been personnel bureau of the Ministry of Government Administration (MOGA). It started with a staffs of 65, all of whom formally worked for the MOGA.

been an extremely closed organization. The key positions for making economic policy are usually occupied by those with similar educational and career backgrounds: the majority of them graduate from Seoul National University and start government career at managerial level (grade 5) after passing the civil service examination (Kwon, M. 1998).

The CSC used the term of "Human Resource Management" (HRM) as key guiding concept for the civil service reform.[39] The CSC defined the Korean bureaucracy as closed, rigid, and inefficient. It aimed to change the system by introducing advanced private practices that include the Open Position System (OPS), performance based programs, job analysis, and 360-degree feedback appraisal. The "Open Position System" (OPS) was an ambitious initiative to strengthen the government competency by recruiting the best person, especially specialists who built their career in the private sector. Managerial positions had been filled by only career civil servants who passed the Civil Service Examination. The OPS was designed to provide opportunity to those who had the best qualifications in both the public and the private sector. When the OPS was introduced, each ministry designated about 20% of its positions of grade 4 and above for the program. In 1999, total 129 positions across the central departments were chosen for the OPS recruitment. The number extended to 142 until 2003. When any of these positions were vacant, they should be filled through the OPS procedure. Anyone who meets the announced qualifications was eligible for applying for those open positions.

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[39] In 2002, the OECD and the CSC jointly hosted an international conference on the HRM in public sector and its overarching theme was "the Person, the Core of the Future Government." The participants discussed such subjects as "open government," "appraisal system," and "performance based HRM" to evaluate Korea's administrative reform.

After all, the OPS failed to achieve its intended goal of incorporating private experts. Each department designated marginal positions in terms of authority and function. They also set eligibility criteria that were difficult for private specialists to satisfy. As of 2000, total 55 positions were filled through the OPS and only 11applicants from the private sector filled the positions. Among them, 6 applicants had prior civil servant or military career experiences. Either each department or the CSC led the selection processes. All 28 positions led by a department were filled by civil servants within the government (NA: CSC, November 4, 2000). Table 4 shows that as of 2001, out of 115 positions recruited by the OPS, only 14 were filled by people from private sector and half of them had prior civil service career experiences. Among 101 successful civil servant applicants, 96 people (83.5%) were recruited from within the same department.

(Table 4) The career background of the successful applicants of the OPS (%)

Total	Civil Servants (%)		Civilians (%)
	Same department	Other department	
115	96 (83.5)	5 (4.4)	14 (12.2)

Source: National Assembly:CSC: 2001

The failure of the OPS was attributed to the lack of the bureaucrats' support. The bureaucrats themselves did not believe in the desired effect of the OPS. They strongly believed that work experience in the government (including organization specific knowledge and personal connections) would be more desirable than expertise and career experiences in the private sector (NA: CSC, September 26, 2003). Among the CSC reform plans, the OPS was most distrusted by the civil servants. They opposed the program for the reason that private experts might be more competent but would lack the sense of responsibility for policy outcomes, which they believed, is the most important qualification for any civil service position. Therefore, the bureaucrats approached the OPS as way to promote competition among the bureaucrats (Civil Service Commission 2000).

An equally ambitious initiative was to introduce performance-based promotion and reward system. This contradicted the long-established rank and seniority rules in the civil service. The most daunting challenge was to make a performance appraisal system. The CSC hired a private consulting firm to create job descriptions for civil service jobs. However, quantifying the effectiveness of a performance was challenging. For example, "leadership" required for high rank positions counted on how effectively an office holder can connect to members within and outside departments. The whole civil service was internally cohesive by sharing similar educational, career, and personal backgrounds. Therefore, personal ties were critical in their capacity to get things done and this kind of capacity was hard to quantify.

Not only making but also applying the performance appraisal system was challenging enough. The CSC initiated performance-based bonuses program for public school teachers. There was fervent resistance. Teachers argued that it is impossible to evaluate teachers' performance in objective and fair manner. Some of schools refused to receive bonus funds or returned them. In many cases, schools divided the funds equally among members or allocated them by seniority rule by manipulating performance evaluations (NA: CSC, September 15, 2001). In sum, the failure of the administrative reforms of the CSC shows how legitimate reform agendas are compromised by local norms and unmotivated actors.

1.2 Fiscal austerity doctrine

Fiscal austerity had been a critical policy rationale in Korea. Although the government maintained its balanced budget with a low level of public spending, it employed flexible taxation geared toward high economic growth. Until the early 1980s, the taxation was devoted to promoting investment and private saving. For the strategic investment on heavy-chemical industries during the 1970s, many tax incentives were legislated through the Tax Exemption and Reduction Control Law. Favorable tax incentives were given to targeted industries such as shipbuilding, machinery, basic metals, petrochemicals, automotive products, electronics, and chemical fertilizers. The tax treatments included temporary reduction or elimination of a tax, investment tax credit, and special depreciation. Consequently, the Korean government had to heavily rely on indirect taxes.

During the 1980s, the government lowered both income and corporate tax rates. Personal income tax was relatively low compared to Western countries and only about 40 percent of workers were paying their income taxes. Relieving tax burden on low-income earners had been popular promises of politicians. The tax reforms in 1988 favored poor-working class. It led to reduction in tax revenue, which in turn limited the expansion of welfare programs for low-income families. During the 1990s, the government reduced corporate tax rate to enhance business competitiveness. Corporate income tax was low at

20% for up to 80 million won, and the excess was taxed at 30 percent (Kwack & Lee 1992).

The IMF prescriptions after the crisis recommended balanced fiscal policy by higher taxes and reduced government spending and subsidies. However, it was impossible to raise taxes under the economic hardship. The government planned even more tax incentives for restructuring related transactions such as corporate mergers and acquisitions, business divisions, asset swaps, alienation of business assets, and contributions by company owners (Yoo 2000). After the crisis, the corporate tax rate was cut from 28% to 27 %. In 1999, the average corporate tax rate of the OCED countries was 34.8%. In 2003, Korean corporate tax rate (27%) was higher than Hong-Kong (17%), Singapore (22%), Taiwan (25%) but lower than the U.S. (31.4%), and Japan (30%) (OECD Tax Database). Corporate tax cut supporters argued that it would enhance economic competitiveness, attract foreign investment, and facilitate economic recovery. The opponents from academia and civil activists argued that corporate tax cut would reduce fiscal health by reducing national reserve. The personal income tax has been minor source of the revenue in Korea. Individual income taxes amounted to only 11.5% percent of total tax revenues in 1980 and 12.7% in 2003. On the other hand, corporate income tax increased its share to 15.3% of total tax revenue in 2003 (Jun, J.S.2009). Foreign investors with advanced technology were eligible for exemptions from corporate and local taxes for the first 7 years and 50 per cent reductions for the next three years. Foreign investments to the Foreign Investment Zone were eligible for government support and tax benefits (Lee et al. 2006).

Widening income inequality after the crisis promoted initiatives to raise tax on high income groups. Comprehensive taxation on financial income was initiated in 2001 to collect more tax from financial income earners but yielded no substantial redistributive effects. For its political popularity and redistributive effects, the government had a series of tax supports for middle and lower classes such as tax cut for small sized housing mortgage and non-taxable saving accounts for seniors and the handicapped.

Due to the tradition of fiscal austerity and underdeveloped state welfare, Korea still had the second-lowest public spending (22.5 percent of GDP) among the OECD countries in 2003. However, its fiscal discipline became increasingly difficult after the crisis. Recapitalizing the financial sector cost a fortune: the government began to issue government guaranteed bonds of 97 billion U.S. dollars which amounted nearly 18 % of GDP. Consequently, the government debt rate had radically increased from 8% in 1996 to 19% in 1999 and kept increasing to 22.4% of GDP in 2002.[40] This was still relatively low compared to the OECD average, 73.0%. Moreover, assisting corporate restructuring, expanding welfare programs and launching cooperative businesses with the North Korea contributed to expanding government expenditures (OECD Economic Survey 2003). Increasing government spending, debts and tax cuts were inevitable policy choices to deal with the troubled economy, which violated fiscal austerity doctrine.

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[40] The government raised the public rescue funds for troubled financial institutions by issuing bonds by the Korean Deposit Insurance Corporation (KDIC) and the Korea Asset Management Corporation (KAMCO). The debt created by these government-guaranteed bonds did not count toward the national debt. From 2003 to 2006, the bonds worth 49 trillion won were converted into treasury bonds in the national balance sheet. This resulted in a drastic increase in the national debt from 11.0 percent of GDP in 1997 to 33.4 percent in 2010 (Kim K.O. 2012).

2. Market Discipline versus Government Control in the Financial and Corporate Sectors

The financial and corporate sectors had been the toughest places to reform in Korea. The government, business and bank alliance persisted as effective policy tool for rapid economic growth. The role of "policy-financing" by state-controlled banks in nurturing and supporting industries was the core mechanism for the development (Woo 1991). Government oversight was critical in directing capital to strategically targeted sectors. Banks were under full control of government with little autonomy in disciplining corporate managements (Haggard et al. 2003). In this context, the pre-crisis market liberalizations were selective, cautious, and incomplete. They did not dismantle the developmental arrangements geared for economic growth. The Korean economy still counted on *chaebols'* performances and was guided by government's policy coordination despite increasing tension between the government and *chaebols.* The post-crisis restructuring was driven by monetarist rationales to build market disciplines. How did that initiative reorient the government and market relationship?

2.1 Banking sector reform

Neoliberal doctrine advocates central bank autonomy as tool for restricting government's arbitrary intervention and inflation pressure. The issue of central bank independence in Korea had been debated in the rivalry between the Ministry of Finance and Economy (MOFE) and the Bank of Korea (BOK). It was not an ideological confrontation but a tug of wars over policy authority. The Law of Bank of Korea was revised after the crisis to make the BOK focus on price stability and inflation control. It stripped the BOK of its authority to inspect and supervise banks, which made it even harder for the BOK to control the currency (Haggard et al. 2003). The president and top economic bureaucrats set interest rates and currency policy. They could nullify the decisions made by the BOK and even intervene in its budget and personnel decisions. Under the top bureaucrats' control on banking sector, banks still lacked autonomy in their lending decisions and capacity of estimating business credibility, profitability, and risks.

The most non-negotiable and destructive guideline by the IMF was high interest policy. This aimed to limit money supply, stabilize inflationary pressures and encourage more accountable business. In May 1998, however, the policy was shortly abandoned as the real economy was collapsing by a series of credit crunch, transforming a financial crisis to a total social collapse. The government had to stimulate the economy by lowering business costs. After the crisis, there was a global trend to lower interest rates and raise government spending across the United States, European countries, and Japan. The Korean economic bureaucrats who had never believed in high interest rates joined the movement. In return for accepting the Korean government's request for lowering interest rates, the IMF pressured even stronger financial and corporate restructuring. The government continuously lowered interest rates to boost investment and encourage consumption.[41] Accordingly, firms' interest burden declined from $20.1 billion in 1998 to $5.4 billion in 2004 with bank loan interest in the same period dropped from 15.2% to 6% (Yun, J. 2009, 285). High interest policy was even regarded as one of the biggest policy failures later.

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[41] Low interest rates did not result in a rapid increase in corporate investment. Financial agencies began to prefer safer state-public bonds investment, rather than using corporate lending. It only contributed to increasing the household debts as excessive inflow of capital was made to households.

Introducing market discipline needed powerful agents who impose new rules, monitor compliance, and sanction violation. In January 1998, the Financial Supervisory Commission (FSC) was established to push restructuring. Backed by the President's full support, the commission exerted comprehensive control over financial institutions and corporations. It imposed 8% rule of *Bank for International Settlements* (BIS) as a criterion for bank restructuring. This capital adequacy requirement aimed to make financial system more accountable by changing banks' lending portfolios: shifting toward less risky assets and depositors.[42] In June of 1998, the FSC closed 8 banks that failed to meet the requirement through mergers and assumptions. Since it was impossible to raise new capital given the depressing capital market, commercial banks tried to meet the requirement by reducing risky corporate loans.

Strict capital adequacy requirement targeted highly leveraged big enterprises whose capital loss by business failure caused the crisis. However, the measure had particularly devastating effect on small and medium sized firms (Choi, G. 1999). [43] To meet new standards, the less capitalized banks that had lower BIS ratio radically desperately curtailed loans to their main clients, small and medium sized firms. Meanwhile, the government issued massive volume of government bonds for rescuing troubled banks. This intervention resulted in the capital concentration in a smaller number of the biggest banks. The top three banks had 27% of financial assets in 1997 and

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[42] Banks should maintain enough capital at least 8% of its risk-weighted assets. They reduced risk-weighted assets like corporate lending and replace them with less risky securities and bond.

[43] Before the crisis, firms with larger return or working for larger firms or chaebols were most leveraged. At the same time, belonging to chaebols reduced the chance of bankruptcies (Choi, G. 1999).

their share increased to 63% in 2005. The bank sector reform was characterized by the excessive government intrusion which was driven by the practical goal to achieve short-term stability by visible restructuring achievements. Meanwhile, banks were extremely passive and barely motivated for the initiatives.

2.2 Corporate governance reform

In the pre-crisis policy discourse, there was a lack of explicit attack against typical corporate governance of *chaebols*. *Chaebol*'s typical structure was based on affiliated firms linked through inter-subsidiary shareholdings, debt payment guarantees, and centralized planning and coordination by owner families. *Moral hazard* discourse after the crisis directly problematized their ownership structure, over-investment, and structure of capitalization. This led to five reform agendas: 1) enhancing corporate transparency; 2) eliminating cross-credit guarantees; 3) improving firms’ capital structure; 4) concentrating on core businesses; 5) strengthening accountability of shareholders and managers.

Chaebols' high debt was regarded as a direct cause of the economic crisis. Neoliberal perspective assumes that business on high debt is doomed to fail and induces "immoral" government bailouts. In contrast, highly leveraged business had been a norm in Korea for decades (Joh, S. 2004). High debt was inevitable for spurring high growth in a credit-based economy. Although much financial capital was invested for unprofitable projects, it was still effective in creating "patient" long-term investments that were less sensitive to short-term profits (Wade & Veneroso 1998). There is an argument that high corporate debt per se could not cause the crisis. During the 1960s, the Japanese manufacturing enterprises had average debt-equity ratio of 320% and it peaked at 500% in the mid-1970s and remained 385% during the 1980. It was the poorly administered financial liberalization that led high corporate debt ratio into a crisis in Korea (Chang, H. 2006).

To solve the high debt problem, the government imposed a unitary rule of debt equity ratio of 200%. This measure was supposed to limit credit-led business diversification and reliance on government guarantees (Lee et al. 2008). Before the crisis, the average debt-equity ratio was around 400% among top 30 *chabeols*. It was challenging for them to lower the ratio below 200% in a short period of time. Instead of actually paying off debts, *chaebols* issued higher volume of stocks and made their subsidiaries purchase these stocks in massive amounts, which constituted "circular investment." Increase of new equities contributed to lowering debt-equity ratio more than reduction in debts. Although actual debt increased by 10% in total, the debt-equity ratio of the top 30 *chaebols* dropped from 393.73% in 1999 to 164.1% in 2000. The reduction in the debt-equity ratio itself did not represent a substantial improvement in capital structure since there was no actual reduction in debt (Haggard et al. 2003).

A new accounting system introduced after the crisis helped *chaebols* lower the debt-equity ratio too. Korea used to adopt the same accounting system as that of Germany and Japan. The old equity appraisal system counted on cost rather than current market value as used in North American system. Such assets as land or properties used to be appreciated after the initial purchase but the North American system reappraised them to boost the size of equity. The surplus from asset revaluation increased by 94% between 1997 and 1999, which made it easier for firms to meet 200% debt-equity ratio (Haggard et al. 2003). *Chaebol*'s reliance on high debt was not resolved since they could still engage in circular equity investment and count on non-bank financial institutions such as bond market.

As for capitalization structure, *chaebols* could inflate their apparent size through cross-debt guarantees or circular equity investment among subsidiary companies. The circular equity investments formed a chain such as subsidiary companies A>B>C>A. Company A could rule another affiliated companies B and C via company C's purchase of A's shares. It generated fictitious capitals and allowed an owner family to control the subsidiary companies despite holding small portion of stakes. In 1999, the government banned cross-debt guarantees in order to change the ownership structure and encourage chaebols to eliminate their incompetent subsidiaries. This was the most visible success among five corporate restructuring agendas.

However, the government allowed *chaebols* to engage in circular equity investment for a practical reason. When barriers to mergers and acquisitions by foreign capitals were all removed, *chaebols* found themselves exposed to hostile M&A threats by foreign capitals. *Chaebols* enhanced the share of owner family by using circular equity investment so that they could defend their managerial rights from foreign investors. As a result, the equity ties among subsidiary firms remained strong and the ownership among affiliated firms became more concentrated around owner families. The inside ownership level was 43.3 percent in 1996 and reached 50.5 percent in 1999 and the stake controlled by affiliated firms had increased (Cho, M. 2003).

Among corporate restructuring programs, President Kim Dae-Jung was most enthusiastic about the success of "Big Deals." Kim repeatedly confirmed to labor that there would be radical corporate restructuring in return for legalizing massive layoffs. This confirmation was all the more imperative given the public perception that moral hazard in *chaebols'* business, particular, over-investments by high leverage, critically contributed to the crisis.[44] The program targeted the top 5 *chaebols* for the goal of streamlining their businesses and overly expanded production capacities. The sales of Hyundai, Samsung, Daewoo, LG and SK were equal to about 30% of the national GDP (Lee, H. 2012). The government pushed major business swaps, warning that if *chaebols* refused the deal, they would be excluded from not only government bailouts but also banks' corporate lending. There were incentives as well. By joining the program, the top *chaebols* could secure tax benefits and write-offs. They also could be shielded from the workout process and bankruptcy except Daewoo (Haggard 2000).

Under the deal, Daewoo had to give up its electronic business in exchange for Samsung's automobile. LG was forced to give up its semi-conductor business, which Hyundai took over. In return, LG had to acquire Dacom, a communication service company which was already in high debt. Although both LG and Hyundai refused the deal, the government pushed hard to make it complete. The deal turned out to be a curse for both companies. Hyundai's Hynix went into default due to financial cost of acquiring LG's semi-conductor business under severe recession in global semiconductor market. LG also went into deep financial trouble in normalizing their new business with Dacom. These deals have been used as examples to show how politically motivated government

[44] Moreover, Robert Rubin, the United States Secretary of the Treasury pressured the government that the foreign investors were paying attention to the "Big Deals" program as the tests for Korea's commitment to corporate reform and the IMF programs.

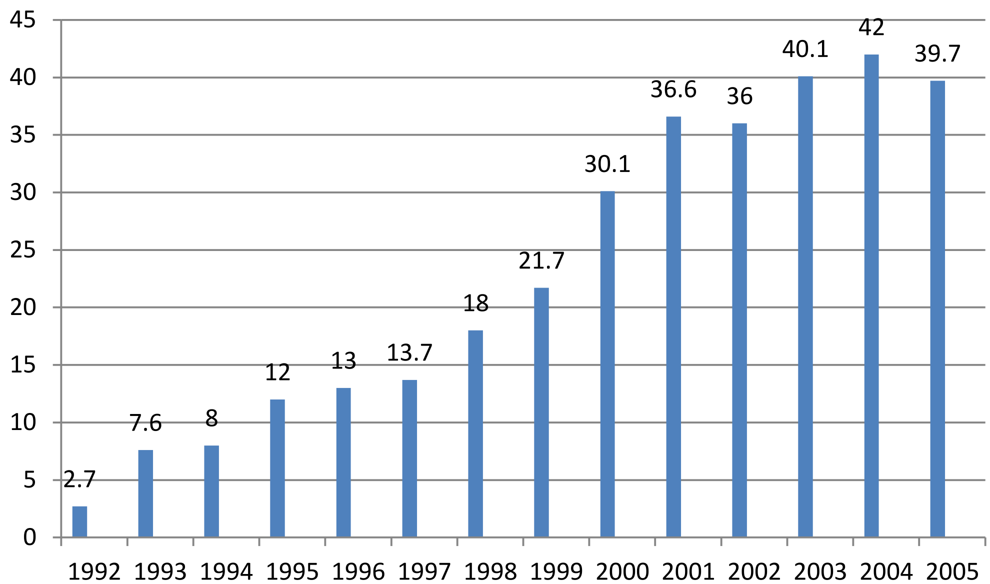
intervention violated market discipline and efficiency that they should espouse. Even the then chairman of the Financial Supervisory Commission, Lee Hun-Jae later confessed that he really regretted his pushing this reform measure (Lee H.J. 2012).

Despite stringent rules to discipline corporate governance, the actual changes were limited by political and cultural inertia. The development of the institutional capacity to impose new rules and oversight cannot be made in a short period of time but limited by the lags in both corporate and financial culture (Haggard et al. 2003). For example, new programs for enhancing corporate transparency were disappointing. The requirements for shareholders to exert to their rights were eased: they could request the removal of a director, demand for convocation, and inspect account books, affairs, and property. Any shareholder with 0.01 percent of firm ownership could file a derivative suit. However, small individual shareholders did not contribute to effective monitoring because of the free-rider problems associated with the public-good property of monitoring (Joh 2004). Owner families and top managers still held their privileges and initiatives in exerting shareholder rights. Outside directors in board committee were empowered to monitor corporate managements. However, a majority of board members were selected by recommendation from the controlling shareholders, family owners. Outside directors approved the agendas by 99% and their attendance rate was very low when the boards have to approve activities related to controlling shareholders.

2.3 Foreign investors as the agents of market discipline

One of the greatest changes after the crisis was the increasing power of foreign capital. To deal with market adjustment, firms desperately sought foreign financing or sold their assets to foreign investors. As the limit on the maximum share for foreign investors was removed, the foreign ownership of listed companies rose from 13% in 1996 to 42% in 2004 (Figure 1). With their increasing shareholding and portfolio investment, foreign investors were better positioned to take over the domestic firms.

(Figure 1) The shares of foreign investors in the Korean stock market (%)



Source: Korea Stock Exchange; Reprinted from Shin, J.S. (2008).

Their attempt to hostile take-over was a real threat to domestic shareholders of *cheabols*, usually owner families. In 2003, Monaco-based Sovereign Asset management started purchasing shares of SK Corporation, the nation's third largest conglomerate. Sovereign accused the CEO and other top executives of SK Corporation of accounting fraud and illegal trading to inflict damages on the affiliated SK companies. To justify its attempted take-over, Sovereign funds argued that they would wage a battle to reform the corporate governance of SK in a way to prioritize shareholder’s interests. The founding family of SK group managed to defeat this take-over attempt with help from domestic investors.

As this episode suggests, foreign investors claimed to be new disciplining agents who wouldn't tolerate the lack of accountable and transparent management. It was also expected that they would introduce advanced managerial and financial techniques. Then, what kinds of changes did foreign capitals brought to the market? The experience of the Frist Bank (Chae'Il Eunhaeng) is worth discussing. The bank was the largest creditor to Hanbo Steal, Kia Motors, and Daewoo all of which were bankrupted around the crisis. The government nationalized and recapitalized the bank using massive public funds through the Korea Deposit Insurance Corporation. In December 1999, Newbridge Capital, a global investment firm, acquired full managerial rights with its 50.99 percent shareholding. While the government poured about 8 trillion and 400 billion won ($7.6 billion) to the bank, it allowed Newbridge Captial to acquired controlling rights only for 500 billion won ($417 million) even with "put back option." This means that the government would cover any deficit from non-performing loans that would happen for next 5 years.

Consequently, in the first half of 2000, the Fist Bank achieved a capital adequacy ratio of 13.7 percent, far exceeding 8% BIS rule and sound return on equity (57%) and asset ratios (4.6%). The nonperforming loan ratio was reduced from 18.5 percent in 1999 to 10 percent (Yun, M. 2010, 252). These improvements in short term were largely attributed to the massive amount of government aids, not the managerial advancement. The bank's new managerial team shifted its priority from large corporate lending to less risky retail and household lending. They could maintain sound indicators in terms of profitability and risk management. Moreover, with the leadership of its foreign CEO, the bank was less constrained by the government intervention. It rejected several government requests to help stabilize the market by purchasing particular corporate bonds or keeping credit lines to troubled funds (Yun, M. 2010). Commentators argued that the bank rejected any public role that it used to play. Lee Hun-Jae, the Chairman of the FSC admitted that the foreign capital managers of the First Bank didn't bring expected benefits but only focused on yielding profits (Lee, H. 2012).[45] The case of the Korean First Bank reveals that the pragmatic goal of achieving immediate stability drove the government to violate market principle: the government poured massive public funds to private financial institutions, favored exclusively the foreign capitals, and failed to consider profitability and risks in attracting foreign investment.

Among the IMF programs, trade and capital market liberalization had nothing to do with the causes of the crisis and trust in the global market. Commentators criticized that foreign investors took advantage of the IMF bail-out conditions in opening Korea's financial market (Lee, K. 2011). Overall, capital liberalization did not bring productive foreign investment, contributing little to the recovery process. During the period 1991-1997, the foreign direct investment averaged $2.4 billion dollar per year and it increased to $11.3 billion average per year during 1998-2005. However, finally paid-investments amounted only $5.6 billion. Almost half of those paid foreign investments were made by

[45] In 2005, Newbridge Captial sold the bank to Standard Chartered Bank which came to possess 100 percent of shares. Newbridge Capital didn't pay any tax for their profit of 1.15 trillion won from this deal.

Merger and acquisitions which created neither new production facilities nor long-term quality jobs (Shin 2008).

With declining state autonomy in planning and implementing long-term industrial policy, the post-crisis reform guided the Korean economy into the path of lower investment and growth. One of the most salient changes was the transition from bank to stock market centered system. Shareholder-centered management prioritizes high stock prices and larger dividends to shareholders. Reaping high interest from short-term speculative investment was preferred to over ensuring the quality of growth.[46] Even when corporations had resources to invest, corporate managers tend to avoid high risk and high return investment, which reduces the number of overall investments. Those with financial assets became crucial reference for economic policies but their interest in raising asset value was often incompatible with the macro policies for long-term economic growth.

3. The IMF Reform and the Developmental Policy Ethos

The post-crisis reform proposed comprehensive and drastic institutional changes in the financial and corporate sectors. The particular agendas include fiscal austerity, small government, banking autonomy, capital adequacy, corporate transparency and accountability, and capital liberalization. In the crisis context, these agendas were ideologically legitimate in that they would contribute to replacing the government's and firm owners' arbitrary controls with market discipline (IMF 1998b).

[46] They placed priority on securing short-term profit by directing the majority of the incurred profits to dividend and capital reduction by cash payment, which left little funds for future investment.

Seemingly unified voices criticizing the government's "distorting" and "excessive" intervention, however, revealed great confusion regarding what role the government should play and who should take over the existing government role in market. For example, corporate restructuring should have been led by creditor banks, not the government. However, these banks were not able to lead massive restructuring. They were fighting for their own survival under stringent government supervision (Park, K. 2003). The entire transition was intensely coordinated by the government leadership.[47] As the failure of “small government” initiative demonstrates, compounding complexity in the post-crisis regime empowered the government to exert stronger power over the market. For the project of introducing market discipline, the government embraced the role as an executor who should impose, monitor and sanction.

The government's regulatory power with new rules and standards was not used to fundamentally alter the way *chaebols* operated and thrived.[48] The *chaebol*-centered economic arrangement was not abandoned. Over-investment using debt and credit had been long-established strategy for economic growth in Korea. It efficiently exploited potential economies of scale and scope in the course of technological catch-up (Amsden 2000). During the corporate restructuring, creditors continued to prop up the largest conglomerates, expecting the government to shield them from bankruptcy. Commentators

[47] Kim Dae-Jung administration established "reform" agencies such as the Financial Supervisory Commission (financial/corporate sector), the Bureau of Planning and Budget (public sector privatization), and the Civil Service Commission (government sector).

[48] The problem of capital concentration was not resolved by these new rules but continued thereafter. As of 2013, 16 years after the crisis, the most central reform issue was so called “economic democratization” which concerns how to make corporate governance more transparent and ensure fair transaction between big and small businesses.

suggest that the government still maintained paternalistic intrusion which rendered financial institutions passive in the corporate restructuring process (Park, K. 2003). Rapid capital liberalization after the crisis led foreign capital to enter profitable finance, service and even manufacturing business domains. However, *chaebols* remained dominant in the leading sectors. The largest business groups exploited control over non-bank financial institutions such as bond market, opening a second window for moral hazard.

The adoption of neoliberal economic programs was more driven by political need to blame old institutions and practical need to restore confidence in the global market, rather than by ideological conviction. The goal-oriented bureaucrats regaining integrated power could effectively achieve an immediate economic stability. New rules were imposed and quantitative goals were met for a short period of time. However, it was only nominal success if the reformers really aimed at dismantling the developmental policy rationales (Lee et al. 2008). While being ideologically challenged, the government's intrusion into market was practically accepted and promoted for the national project of the "IMF reform."

CHAPTER 5
CHANGES AND CONTINUITIES IN THE LABOR MARKET

This chapter discusses the changes and continuities in the labor market after the crisis. Promoting labor flexibility was an integral part of the market adjustment as a way to facilitate financial and corporate restructurings. Legalization of collective dismissal and dispatched workers critically weakened employment security. There are two patterns of labor market insecurity: a drastic increase in the number of non-regular workers and a widening gap between regular and non-regular workers in wage, employment security and access to social insurance protection. Expanded welfare and social insurance programs did not effectively deal with growing insecurity among non-regular and unemployed workers. Corporate unionism persisted and protected the employment security for their regular employee members. On the other hand, labor market deregulation imposed greater burdens on unorganized non-regular workers. The initiative for flexible labor did not overcome the legacy of dual labor market. This chapter addresses how the legacy of corporate unionism affected the labor market deregulation.

1. The Economic Crisis and Its Impacts on the Labor Market

1.1 Labor market flexibility after the crisis

In contrast to excessive number of requirements for financial and corporate sectors, the IMF imposed fewer labor-related conditions. However, it explicitly demanded immediate legalization of massive layoff, which was destructive enough. It was still difficult and costly for employers to fire regular workers under the existing labor law. To amend the law, the president-elect Kim Dae-Jung had to persuade labor. At the end of 1997, he held talks with labor and business to elicit cooperation to form a tripartite body. In January 1998, the Tripartite Commission was launched for social dialogue.

The Federation of Korean Trade Unions (FKTU), a state-sponsored union association passively accepted the government proposal. In contrast, the other nationwide union association, the Korean Confederation of Trade Unions (KCTU), agreed to join the dialogue only when the government would ensure the suspension of legalizing collective dismissal. Kim Dae-Jung firmly believed that flexible labor market was essential for gaining confidence from the IMF and creditor countries. He was desperate to arrive at an agreement through the Tripartite Commission to convince foreign investors of successful labor reform in the upcoming negotiations. After painful discussions, the Commission reached so called "2.6 Great Compromise." The pact proposed immediate legalization of collective dismissals and dispatched workers.[49]

As predicted, the legalization of collective dismissal, flexible working hours, use of dispatched workers or substitute labor during strikes adversely affected employment security. A severe streamlining was underway in the financial sector. The manufacturing and construction sectors adopted a labor-shedding strategy, while maintaining high wage and job entitlement for a small number of high-skilled workers. A variety of adjustment measures were introduced to control labor costs such as flexible and merit-based wage

[49] The KCTU rank and file members refused to accept their representatives' agreement with the pact so they replaced its leadership. The new representatives kept moving in and out of the negotiations to finally walk out of the Commission. This severely damaged the legitimacy of the Tripartite Commission as the institution for social pact.

system and early retirement. As of 1999, a survey among 4,303 firms employing more than 100 workers reveals that 649 enterprises introduced yearly lump sum payment. The number of firms with the program was only 94 in 1996 and 205 in 1997 (Sun, H. 2000).[50]

The most notable change was the sharp decline in the number of regular employees, which increased the number of non-regular workers. The rate of non-regular workers was 43.4% in 1996 and it surged to 52.9% in 2000 (Kim, S. 2001). Fixed term employment contracts became prevalent in such industries as electricity, gas, water, finance, insurance, real estate, retail consumer, lodging, food, public and private administration, and particularly service industries. Newly created non-regular jobs were not voluntary part-time but rather temporary or daily employment without option. These were often occupied by female, less educated, and service job employees.[51] Over 70% of the working poor were female employees who were hired in non-regular and short-term positions. The wage level for non-regular workers was only 53.7% of the regular workers (Yun, J. 2009). A growing number of newly laid-off and retired workers started running small-businesses to be self-employed or entered low-skill service sectors such as small restaurants, lodging, and taxi driving. Competition was already excessive in these domains. The percentage of service sector employment increased from 58.2% in 1997 to

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[50] A yearly lump sum payment system was supposed to reward workers by their performances, not by seniority rule or rank. This practice enlarged wage gap by education, skills, and occupation. At the same time, this system was widely used by employers as a way to cut wages or control employees, regardless of performance.

[51] Since the 1994, the rate of maintaining a job for less than a year had monotonically increased but after the crisis, it drastically increased in particular groups of female workers, manufacturer, service, and sales jobs.

64.8% in 2004. About 60% of those in poverty were working with very low employment security and many of them were self-employed (Yun, J. 2009, 284).

Consequently, income inequality grew at a pace unobserved in other OECD countries. This was driven largely by rapid income reduction of those at the bottom of the wage distribution. Labor market polarization exacerbated the problem of household poverty. Household debt began to exceed household net disposable income. The household net savings rate which was 15-16% before the crisis, dropped to 9.9% in 2000 and 2.0% in 2002.[52] When households are divided into five groups by their income, Group 5, the households with the highest income did not experience substantial drop in saving rate (38-39%). Group 2,3, and 4, the middle income groups experienced dramatic reduction. For example, the saving rate of group 2 which was 20%, decreased to 10%. Most of all, the saving rate of the bottom 20% group came to be held at negative rate which means that they had to live on borrowing (Chung, K. 2007). While households of permanent or regular workers recorded a low debt-ratio, the unemployed or self-employed household experienced the highest level of debt ratio in subsequent years.

1.2 The labor market reform and the expansion of social protection

The disintegration of job-for-life tradition and extreme social dislocations generated greater awareness of social security. After the outbreak of the crisis, neoliberal discipline dominated financial, corporate and labor reform, but not social protection. It

[52] The household net savings rate is measured by dividing net private sector savings by net adjusted disposable income in the national accounts (Chung, K. 2007).

was because Korea had no excessive welfare programs to be attacked. It had had low level of public expenditure on labor market programs. However, Korea had maintained high level of employment protection, more or less equal to the Western welfare countries like Finland (Yun, J. 2009). Labor market liberalization began to undermine the job security and this threat politicized welfare issue, providing a momentum for a radical policy shift in social insurance and state welfare (Song and Hong 2008).

The term of "social safety net" had been rarely used before, but came to be commonly used by the top policy makers in the post-crisis policy discourse. For example, the Minister of Labor proposed the project of "Building Social Safety Net" which planned to strengthen unemployment programs. Previously "individual" or "private" risks began to be discussed in relation to public responsibility. Poverty and unemployment were newly identified as “social” risks. For the low income population, the government began to take greater responsibility under the Minimum Living Protection Law in 2000. This program guaranteed the state assistances to all households below minimum income with medical service and education, regardless of their working capacity.[53] The covered population tripled from 500,000 to 1,500,000 and consequently the state budget for the program increased by 50%.

The crisis environment generated strong political incentive to manage insecurity, creating breakthroughs in long-time stalled social insurance reform. Increasing employment insecurity was to be counterbalanced by the enhancement of labor’s political

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[53] In the past, even household earning less than minimum income couldn’t get assistance if they had an employable family member who assumed to have responsibility to take care.

rights and social security system (Wong 2004). The greatest improvement was made in the health insurance system. Over the previous decades, the initiative to integrate the health insurance groups into single risk pool had been blocked by presidential vetoes and the economic bureaucrats' gatekeeping actions. Without the economic crisis, this history would have been repeated.[54] When the provision to integrate health insurance was agreed by the 2.4 Great Compromise at the Tripartite Commission in 1998, the traditional opponents couldn't block the plan. The different health insurance groups were integrated under the single administrative authority to enhance risk sharing at the national level. The same dynamics operated in the pension reform to achieve more universal coverage and cross-occupational solidarity. In 1999, anyone whose age is 18 to 60 could enroll for the national pension system. The contribution rate was quite low (9% of wage) and the level of income maintenance was 60% which was relatively high compared to that of the U.S. (41%), the U.K. (40%), France (50%), Canada (49%). As a powerful regulator, the government could build new legal frames to expand eligibility and benefits in the four major social insurances.

2. Dual Labor Market and Growing Gap between Workers

2.1 Dual labor market and employment security

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[54] A group of civic activists and health related professionals formed an organization called 'Health Coalition' in the mid-1990s. The coalition advocated the integration of health insurance groups at national level to increase risk pooling. With support from the progressive labor associations, the KCTU, they could effectively influence the health insurance reform.

During the high growth period from the 1970s to the 1990s, Korea had emulated the Japanese model of dual labor market. The government had supported regular workers in big enterprises and public sectors with employment security and income maintenance. Employment protection could be maintained by high economic growth and growing job opportunity. In the early 1990s, the Korean economy slowed down when firms had to compete with cheap labor in China. Its labor productivity failed to keep up with increasing labor costs. Businesses pressured the government to promote labor market flexibility, enthusiastically attacking the automatic wage increase as the greatest obstacle for economic growth.

Despite growing labor market insecurity since the early 1990s, regular workers in big firms and public enterprises still enjoyed relatively high job security and wage income. Since the 1987 labor movement, the unionization rate increased especially in the big enterprises of the most strategically important industries. During 1987-1997, the wage level increased by 13.9% annually. Responding to these trends, big businesses employers began to introduce so called "human resource management" for more flexible employment. Finally, the Labor Standard Acts in 1998 provided business with more leeway to dismiss their regular workers and utilize alternative forms of employment.

Considering the potential political upheaval, the IMF allowed the Korean government to have some flexibility in negotiating with unions and employers (Caraway et al. 2012). The government was aware of the importance of organized labor in achieving political stability and successful market adjustment. The Kim Dae-Jung regime needed to counterbalance the labor market deregulation to maintain labor’s support. Thus, a complex set of rules for dismissal was added to the legislation for flexible labor. Before the crisis, an unfair dismissal claim was resolved not by legal process but by monetary compensation. The new collective dismissal provisions had the clauses to mandate employers to follow strict procedures for firing workers: they should make all possible efforts to avoid collective dismissal and discuss with workers' representatives. As of 2003, the conditions for "dismissal by managerial reason" became stricter. Employers had to notify the workers of his/her dismissal 60 days prior to the date of termination and it had to be done in consultation with unions. Substitute workers during labor disputes should be drawn only from workers within the company. Business and conservative critics complained that the new labor legislations left much room for legal disputes by its ambiguity and even reinforced existing labor rigidities. According to a survey conducted by the Federation of Korean Industries (FKI) in 2001, 75 percent of the staffs in the Korean branches of foreign firms perceived that labor disputes, high wage level, the strict administrative regulations and nontransparent business transactions were the greatest hindrances to foreign investment to Korea (Haggard et al. 2003).

As a measure of labor market flexibility, the OECD developed the indicators of employment protection that incorporated procedures and costs involved in firing and hiring individuals or groups of workers. Table 5 compares the strictness of employment protection across the OECD countries. Before the crisis, Korea had maintained relatively higher strictness (3.23) in protecting regular employment. This means that it imposed a great deal of inconveniences in satisfying the rules of dismissal process, notice periods and severance payment. The employment protection for temporary or fixed term workers (2.25) had been lower than Germany, France, and Norway but higher than Finland, Sweden, and Japan.[55] After the crisis, the strictness index dropped to 2.37 for regular employment and 1.69 for temporary workers. The legal employment protection for regular workers was still among the groups of higher protection with Sweden, Finland, Germany and France. As of 1999, the Korean labor market was more rigid in dismissal compared to labor markets in Germany, the United States and Japan (OECD, Employment Outlook 1999).

(Table 5) Strictness of Employment Protection of OECD Countries

	1995~ 1997		1998 ~2002	
	Regular	Temporary	Regular	Temporary
Korea	3.23	2.25	2.37	1.69
Sweden	2.90	2.08	2.86	1.63
Finland	2.79	1.88	2.31	1.88
Germany	2.68	3.50	2.68	2.00
France	2.34	3.63	2.34	3.63
Norway	2.25	3.13	2.25	2.88
Japan	1.87	1.38	1.87	1.00
Canada	1.25	0.25	1.25	0.25
U.K	0.95	0.25	0.95	0.25
U.S.	0.17	0.25	0.17	0.25

Source: OECD. StatExtracts

Table 6 shows the difference in employment security by firm size and gender. The average length of employment was greater in larger firms: male workers in small firm (less than 30 employees) were employed for less than 3 years while their counterparts in large firm (more than 300 employees) are employed for more than 9 years.

[55] The measure of protection for the temporary employment considers work agency contracts with respect to the types of allowed work and duration and requirements for temporary workers to receive the same pay and/or conditions as equivalent workers in the firm, which would raise the cost of using temporary workers relative to hiring workers on permanent contracts (OECD. StatExtracts).

There was huge gap in the percent of short-term employees by firm size: compared to 25.9 percent in the large companies, 71.8% of male workers in the small size firms work for less than 3 years. Gender is a significant precursor of employment security. Women had much shorter length of employment than men regardless of firm size.

(Table 6) Average Length of Employment at a Company by the Firm Size (as of 2001)

The number of employees	1-29	30-99	100-299	More than 300
Average length of employment (years)				
Men	2.72	5.80	6.56	9.12
Women	1.47	3.96	3.13	4.13
Percent of employees working for less than 3 years (percent)				
Men	71.8	50.3	39.9	25.9
Women	81.5	59.7	64.0	54.5
Percent of employees working for more than 20 years (percent)				
Men	2.5	8.4	6.8	10.8
Women	0.4	4.5	1.6	3.1

Source: Rearranged from Jung and Cheon (2004)
** This research used "Korea's labor force survey."*

Using another survey, Jung and Cheon (2004) compared the employment security between 1992 and 2001 to find that employment security in large firms had not weakened. In 1992, male workers' average length of employment in large companies (more than 1,000 employees) was 7.71 years and increased to 10.10 years in 2001. The percent of workers working less than 3 years decreased from 22.5 in 1992 to 16 percent in 2001.[56]

[56] The firm size effect on wage also increased. In the manufacturing sector in 1992, firm size effect was 17% which means that college graduate male workers in large firms (more than 1,000

In sum, Korea's employment security was quite low except in large enterprises and its degree of labor market segmentation was greater than in Japan and Taiwan.

2.2 The legacy of corporate unionism and limited union politics

In return for their concession that allowed immediate legalization of collective dismissal and use of temporary workers, labor could secure the expansion of legal rights of trade unions and unemployment programs. However, these improvements did not directly ease the increasing insecurity of unorganized non-regular workers. Only less than 10% of government budget for unemployment programs was assigned to direct assistance. Its rest was spent on the conventional programs such as assisting firms' job training and expanding loans to employed workers. These programs favored employed workers, not the unemployed (NA: The Committee of Ministry of Environment and Labor, February 11, 1998). Corporate unionism persisted and led union activities to focus on firm level wage negotiation and working conditions.

Figure 2 compares the union density rate of Korea, Japan, and Taiwan during 1985-1999. Korea's density rate rose from 12% to 18% by 1990s with the successful democratization movement. Entering into the 1990s, the rates of three countries slowly declined.[57] Empirically, high union density is associated with national level of collective

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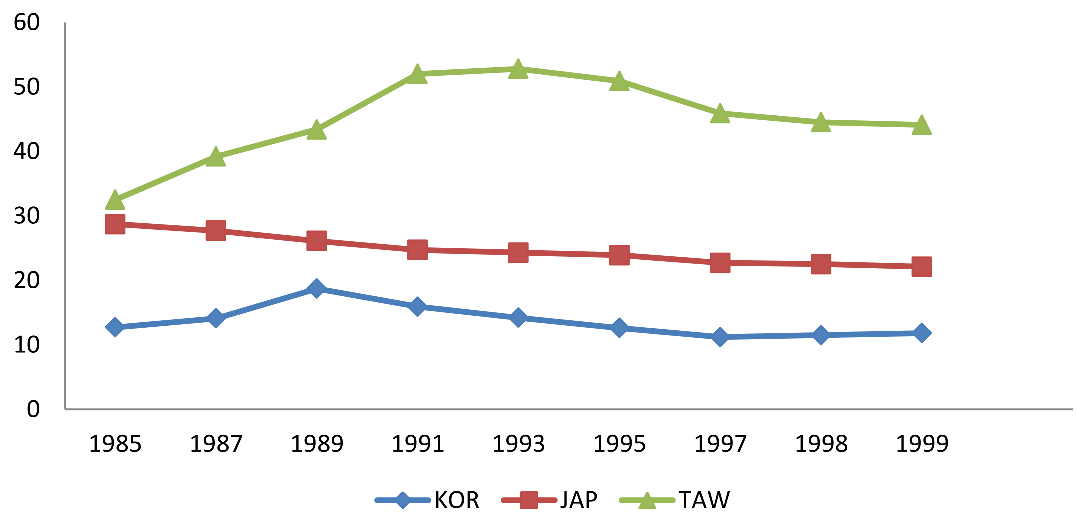
workers) were paid more than their counterparts in small and medium sized (10-99 workers) by 24.3 percent. In 2001, this gap increased by 30.1 percent (Jung and Cheon 2004).

[57] Trade union density in Taiwan was higher than in other Asian countries because membership of a trade union was mandatory by law: refusal to join a legal union could lead to suspension from job. However, the implementation of this law was incomplete so many workers in practice did not join unions (Chen et al. 2003, 320).

bargaining, wider coverage rate, and strong influence of unions on social policy (i.e. Sweden).

(Figure 2) The Union Density Rate of Korea, Japan, and Taiwan (%): 1985-1999



Source: Rearranged from Kuruvilla et al. 2002

In contrast, fragmented union system is associated with firm-level collective bargaining, lower coverage rate and limited influence on national policy-making (Kuruvilla et al. 2002). The unions of the Asian countries are closer to the latter category with their fragmented and limited power on national policy making. In the early 1990s, trade unions of Korea and Japan had the most decentralized organizational and bargaining structures among ten countries in the Asia-Pacific region (Jeong, J. 2001). The segmentation in Taiwan was weakest among three countries but it still had huge gap between public and private sector in employment security and wage income (Jung and Cheon 2004).

In Korea, the unionization rate in the small number of large companies was very high, reaching more than 70 percent. About 88 percent of total employed workers worked for small and medium sized firms which employed less than 300 workers but their unionization rate was very low. Consequently, collective bargaining covered only a small share of all employees, about 10 percent in 2000. The organized unions could still have bargaining power by their capacity to mobilize nationwide strikes, protests and walkouts. Hyundai Motors strikes that occurred in July 1998 was the first testing event whether the legalized collective dismissal could be actually implemented despite the opposition from one of the strongest unions in the country. Hyundai Motors' management announced that it planned to dismiss 1637 workers which instigated the union's strikes that lasted for about two-months. The dispute ended through the mediation of the Minister of Labor when the union and the management agreed to fire 277 workers. The event showed that the major unions still could bargain for their employment security. The majority of foreign investors showed their concern that Korea had long way to go for flexible labor market (*Wall Street Journal*, August 12, 1998).

However, firm-based collective bargaining excluded the majority of non-regular workers. Only 8.1% of non-regular workers were working for company with a labor union. Non-regular workers were not eligible for union membership and had low incentive to take issues against employers. About half of part-time workers were married women and their unionization rate was only 0.1% as of 2003 (Kim S. 2004). Despite similar level of education, the wage level of non-regular workers was about 59% of the regular workers (Jung and Cheon 2001). The unions’ failure to represent the increasing non-regular workers weakened their organizational capacity and legitimacy.

With the legalization of multiple union associations, the FKTU, which had been the single legal union association, had to be in rivalry with the progressive KCTU, previously illegal association. Both could not make a unified position due to their different ideological orientations. Moreover, firm-based unionism empowered neither of KCTU nor FKTU to act as the peak labor organization and their bargaining power with the government and business became substantially weaker (Kim and Moon 2000). Consequently, labor unions had weak commitment to universalistic social welfare.[58] In sum, collective action problem among fragmented and atomized corporate unions led to high employment protection for regular workers in big enterprises at the expense of non-regular or marginal workers without appropriate level of social protection (Yang, J. 2006).

Given these union politics, the newly expanded social protection did not directly respond to increasing risks of the politically weak and unorganized labor groups, mostly non-regular or unemployed workers. The best example was found in the limited success of employment insurance program. Following the IMF recommendation, the government revitalized the program which had been almost non-functional. In 1998, all firms were eligible to the program. Its minimum contribution requirement was eased and the average duration of benefit was extended. Despite these improvements, a limited number of those without work could receive any benefit. Only wage workers were legally eligible in many

[58] For this reason, the demand for the universal welfare had been too fragmented to exert substantial influence. For example, in the late 1980s, the farmers demanded the integration of all insurance groups and the expansion of the state’s financial supports to rural groups. However, their movement was not supported by unions and civic organizations. According to Kim Gi-Sick, the most publicly visible leader of civic groups, admitted that civic activists paid insufficient attention to welfare issues simply because they did not recognize their significance (*Welfare Perspective* , May 2001).

cases. The majority of daily and temporary workers working less than a month in a firm were not eligible. Even legally eligible non-regular workers often did not take burdens of declaration process and administrative filling with their frequent turnovers.[59] Overall, about 42% of the working population was legally eligible and only 10% of them actually received any benefit during 1999, which is significantly lower than that of any other OECD country. The majority of the government fund for unemployment problem was spent on creating temporary jobs in public work projects. These jobs were taken by the elderly or recent college graduates (Cho, W. 2001).

The government remained fiscally conservative in social insurance system, leaving greater financial responsibility to employers and workers. Employers paid half of contributions for health insurance and pension. Companies had to pay 8.65-9.25 % of wage for a worker's contributions of pension, health insurance, employment insurance, industrial injuries, and wage bonds. From 1997 to 2005, firm's expenses for workers' social insurance contributions increased by 183.5%, growing by 14% annually (Hwang, I. 2006). This drove employers to count more on non-regular workers who were not legally granted for the equal protection available for regular workers. This incentive was much stronger in small and medium sized companies. The increase in the proportion of non-regular workers was smaller in larger firms that could somehow afford increasing burden. In contrast, small and medium sized companies who couldn’t afford increasing insurance

[59] The legal criteria judging whether a claimant is involuntarily unemployed was so stringent that anyone who quit their jobs without justifiable reasons was regarded as voluntarily unemployed and not eligible for the benefit.

costs sought for flexible labor to save labor costs. These companies had a larger increase in the percentage of non-regular employees (Korea Development Institute 2004).

The expansion of social insurance could not effectively deal with the problems of increasingly market segmentation. The effectiveness of social insurance is weak for flexible labor market. With growing diversification in employment styles and wage flexibility, many workers could not meet the eligibility requirements with their unstable employment and income. Table 7 shows the percentage of employees who were not covered by major social insurance programs by employment type, firm size, and type of job. While majority of workers were covered by health insurance, 7.5% of daily workers were excluded from the program.

(Table 7) Percent of Non-covered workers by Social Insurance Programs (as of 2007)

		National Pension	Employment Insurance	Health Insurance
Employment Type	Regular	14.9	18.9	0.9
	Temporary	62.5	69.6	2.4
	Daily	85.0	92.3	7.5
Firm Size	Less than 30	58.4	56.1	3.0
	30 and more	15.9	15.2	1.1
Job Type	Manual, Service & Sales	65.1	63.3	4.4
	Others	21.8	20.6	0.7

Source: Rearranged from Kim, S.W. (2009)

Compared with 14.9 % of regular workers, 85% of daily workers did not participate in the national pension plan. Their gap in employment insurance was huge as well: 92.3% of daily workers were not covered compared to 18.9% of regular workers. Firm size was strong predictor of social insurance availability. All firms were legally eligible for the pension program. However, about 60% of employees working for the small firms (less than 30 employees) were without pension plan. The gap by firm size also appeared in employment and health insurance programs as well. There were practical conditions that account for this low coverage in small-sized firms. Individual attributes, employment type, firm size, industry, and wage structure were all interrelated to affect workers' chances of being excluded from social insurance programs. A path analysis found that firm size was the most important variable. Smaller firms were more likely to hire temporary or hourly workers to save labor costs. Employees were forced to accept the exclusion to remain employed and avoid the reduction of disposable income (Kim, S. 2009).

The initiative for labor flexibility eased the rigidity of labor market, drastically increasing the number of unorganized insecure workers. The government responded by expanding government welfare, upgrading social insurance, and allowing greater political rights to labor. Under the persistence of corporate unionism and the increase of labor costs for social insurance, labor deregulation imposed greater burdens on unorganized labor. This widened the gap among workers and intensified labor market polarization. The IMF criticized that the labor reform initiatives ended up "protecting a dwindling pool of insiders at the detriment of a growing body of outsiders" (IMF 2006). The OECD suggested that easing the protection for regular workers would mitigate increasing insecurity of non-regular workers. The Korean labor market remained still rigid but at the same time extremely flexible.

CHAPTER 6

CONCLUSION

1. Questions and Major Findings

This study seeks to understand the encounter between exogenous neoliberal ideas and endogenous "development" policy ethos in the context of post-crisis transition in Korea. The restructuring enforced by the IMF aimed to "upgrade" the Korean economy following the Western model of market economy. The preexisting policy orientations were delegitimized under neoliberal policy prescriptions. To understand the nature of the post-crisis transition, I traced the major reform efforts by asking the following questions. First, how do we explain the rise of neoliberal ideas as an ideological force to determine the direction of reform? Second, how did espoused neoliberal doctrines contradict the developmental policy ethos? Third, how did the developmental ethos countervail the institutionalization of neoliberal doctrines?

To answer these questions, the research started with clarifying key concepts of *hegemonic ideas* and *institutional ethos.* In uncertain times like an economic crisis, a set of ideas become dominant by suggesting explicit and coherent action strategies (Swidler 1986). Policy makers are subject to dominant ideas as “road maps” in solving problems (Goldstein 1993). Over the last decades of the 20th century, economic ideas and norms called *neoliberalism* became the hegemonic framework for perceiving the economy. This ideational hegemony drove many countries to plan and adopt a wave of privatizations, deregulation, welfare retrenchment, tax cuts, and liberalization (Fourcade-Gourinchas and Babb 2002; Campbell and Peterson 2001).

On the other hand, the concept of *institutional ethos* captures pre-existing orientations and understanding of reality that are taken-for-granted. I focus on policy rationales as representing institutional ethos in policy domain and they are actualized through recurring strategies, preferences, and capacities. In the research literature, the key assumption about government and market relationship is the critical basis for long-term policy ethos in a given country. It also influences people's perceptions of a crisis and policy responses to the pressure of neoliberal reform (Fourcade-Gourinchas & Babb 2002).

In this study, I approached the post-crisis reform in Korea as a historical context in which the two policy paradigms collide and together shape reform politics. The developmental and the neoliberal policy frameworks are built in distinctive perceptions of government and market relationship. While the developmental rationales use government intervention to pursue practical policy goals, neoliberal ideas discern the boundary between them and advocate maximizing market autonomy (Fourcade-Gourinchas and Babb 2002). I attended to monetarist doctrines in the IMF prescription as *hegemonic ideas*. The developmental rationales as *institutional ethos* are not based on a coherent theoretical model or ideology, but on more informal and implicit orientations. A crisis generates enormous momentum for change, but at the same time can maximize the traditional policy capacity for solving problems. I described how the interaction between these two determined the nature of "neoliberal transition" in Korea.

Chapter 2 discussed the long-term policy ethos and the liberalization initiatives in Korea during the 1980s and the 1990s. I emphasized two developmental policy rationales. First, a pragmatic orientation allowed the government to employ hybrid policy tools geared toward economic growth. The weak ideological commitment to market autonomy or social justice allowed the government more maneuverability in mobilizing banking, business, and labor. Second, there was consistent policy preference that strategically supports key economic and labor sectors. The government allocated resources unequally to promote key industries and supported their workers. The strategic prioritization was highly effective for achieving rapid economic growth. However, it caused problems such as capital concentration and unbalanced resources allocations.

During the 1980s and 1990s, there were both external and internal pressures to curtail government's controls in the market. The government pursued liberalization in a selective, cautious, and gradual manner. Many of the attempts were largely cosmetic. The conventional policy priorities remained largely unchanged to maintain a *chabeol*-centered economy and regulated dual labor market. The government still controlled interest rates and corporate lending decisions. *Chaebols* could secure extended source of capitalization and unionized workers could maintain their employment security. Not a single reform agenda was fully actualized. Major reforms were driven by power competitions among bureaucrats, business, and labor. Consequently, legislative proposals for reform plans had been stuck in political gridlock, blocked by the persistent and growing veto powers of the opponents until the outbreak of the financial crisis.

Chapter 3 described the rise of neoliberal policy doctrines as the main ideological drive behind the reforms. Left with little option in dealing with the demands of the IMF, the U.S. and foreign investors, the top policy makers had to accept radical conditionality and tried to even overachieve them. The moral hazard perception mediated the acceptance of neoliberal doctrines by highlighting the defects of developmental institutions. As remedy, neoliberal norms of small government, financial accountability, bank autonomy, and labor flexibility were endorsed as reform agendas. The environment of crisis management provided favorable reform-making institutions. The IMF programs were accepted as painful but inevitable tools for upgrading the economy.

Chapter 4 discussed the persistence of the developmental rationales in the major reform attempts. The administrative reform toward "small, open, and efficient government" failed because of the cohesive and exclusive culture of the civil service. The bureaucrats' support was crucial in political stability so that any reform measure to provoke them was prone to fail. The practical need to achieve immediate economic and political stability encouraged the expansion of the government spending, which compromised the norm of fiscal austerity. Newly introduced "global standards" provided new regulatory tools for the government to intervene in the market and resulted in more integrated supervision by the government. Disciplining *chaebols'* ownership and capital structures had to be selective since they were still the core forces in the Korean economy. Rapid capital liberalization was most successfully implemented with the growing influence of foreign investors.

Chapter 5 addressed changes and continuities in the labor market after the crisis. Promoting labor flexibility was an integral part of market adjustments. Labor market reform increased the number of unorganized non-regular workers. The expanded social protection did not properly respond to growing labor market insecurities. Big enterprises' corporate unionism excluded non-regular workers from collective bargaining. Consequently, labor market deregulations imposed more burdens on unorganized non-regular workers, enhancing dual labor market legacy. The gap in the wage and social protection by firm size and unionization drastically increased after the crisis.

(Table 8) The contexts for incomplete institutionalization of neoliberal agendas in Korea

Agendas (ideas)	Reform outcomes	Contexts (ethos)
Small government (Fiscal austerity)	Cohesive and closed bureaucracy Increasing government spending and debts	Pragmatic intervention Prioritization
Market (bank) autonomy	Integrated market supervision (Establishment of the FSC)	Pragmatic intervention
Corporate transparency	Concentrated ownership among affiliated firms (circular-equity investment)	Prioritization
Flexible labor	Enhanced labor market segmentation Increasing gap among workers	Prioritization
Capital liberalization	Increasing influence of foreign capital Low investment/low growth	*Most successful implementation

Table 8 summarizes the reform outcomes of the major agendas and the contexts for their incomplete institutionalization. Despite strong ideological impulse and explicitly neoliberal agendas, the reforms did not alter the "developmental" government-market relationship. Top policy makers approached "neoliberal reform" as a state-led project that should produce visible achievements and bring immediate stability to market. In this context, the government counted on the developmental policy capacity and strategy, violating neoliberal doctrine of small government and market autonomy. New rules of "global standards" provided the government with legitimate disciplining tools for regulatory intervention. At the same time, political and economic incentives to protect cohesive bureaucrats, expansive *chaebols*, and organized labor compromised the agendas of small government, market initiative, corporate transparency, and flexible labor. The strong persistence of pragmatic interventionism and prioritization constitutes the key policy ethos that explains the incomplete neoliberal transition in Korea.

2. Neoliberal Transitions in Comparative Context: Japan and France

This section briefly reviews neoliberal reforms in Japan and France to compare them with the Korean experience. The review attends to two questions. First, how did institutional legacy affect their interpretations of economic crisis and policy responses? Second, did their experiences exhibit a "developmental" version of neoliberal transition that differs from those of non-developmental countries?

2.1 The neoliberal transition of Japan

There had been constant initiatives to reform the traditional structure of the Japanese economy by deregulation to reduce the government role in economic affairs. These efforts during the 1980s and 1990s were not successful because of effective resistances from the bureaucrats and pork-barrel politics. These opponents claimed that deregulations would harm the delicate protection mechanism for the less privileged economic groups. In fact, they feared that deregulation would weaken their interests associated with regulatory authorities. On the other hand, business leaders advocated deregulations arguing that they would create more jobs, lower prices and raise real wage level (Hitawari 1998).

Japan cultivated highly regulated bank-centered economy. The major source of business capitalization was government-guaranteed lending. The government often rescued bankrupted financial institutions by using public funds. Japan's "bubble economy" came to an abrupt end at the start of 1990s with the beginning of "lost decade." The financial reform called "Big Bang" was initiated in the mid-1990s. The project aimed to redirect capital funds from the banking sector to stock and bond markets, assuming that the Western model of stock market-centered capital accumulation makes the financial market more competitive and investor-friendly (Dore 1999).

However, the priorities of stock market and shareholders' interest were not compatible with the Japanese bank-centered financial system and stakeholder-oriented corporate governance. The American corporate model is based on "shareholder sovereignty": the goal of business should be the maximization of returns to shareholders because they are the real owner of a firm. Therefore, if management fails to satisfy shareholders' interests (i.e. high profits and dividends), it should be ready to accept a take-over by another managerial group (*Economist*, April 22, 2010).[60]

In contrast, the Japanese corporate governance prioritizes stakeholders' interests. Stakeholders include employees, customers, suppliers, and society at large. Long-term managers and presidents regard themselves as firm's owners instead of shareholders' agents. They do not believe that firm's share price represents its real value or performance,

[60] Corporate transparency was critical in shareholder sovereignty since correct information regarding corporate management was essential in investors' correct judgment on company's value. Japanese banks were obviously not capable of estimating or monitoring the management of the firms to which they provide lending. This incapacity promoted transparency as an important agenda of corporate reform even higher.

which made them less sensitive to short-term profit that their Western counterparts. The major firms defend their managerial autonomy from individual investors or shareholders through their "cross-shareholding" with banks. Cross-shareholding refers to equity shares that two companies hold in one another. The cross-shareholding arrangements involve "understood but unstated obligations." They were designed as tacit mutual pacts to insulate the management of both sides from any threat of hostile takeover. In other words, stable cross-shareholding relationship functioned as a strategy to limit shareholder rights to govern the firms (Scher 2001). Even under the pressure of labor market flexibility, firms' managerial autonomy can avoid massive dismissals of workers (Dore 1999).

The *Big Bang* reform planned a partial bailout system to limit using public funds for rescuing firms. However, a series of bankruptcies of major financial institutions postponed this plan. Although the exclusive firm-bank relationship began to falter, shift from bank to stock-market centered economy was not successful. Household savers were still directed to spend their money or deposit funds for saving in banks. Firms were not inclined to capitalize themselves through the stock market. The percent of individual investors was quite low in the stock market because of excessive restrictions.

The worsening economic conditions during the "lost decade" generated greater momentum for market liberalization. The Koizumi administration (2001-2006) embarked on market-friendly reforms, emphasizing that the Japanese economy should be adapted to the global economy. Its reform focused on a series of deregulations along with tight fiscal policy. As in past, the attempts were unsuccessful especially in the public sector which were dominated by powerful bureaucrats and politicians. The government pushed deregulations harder in declining industries where weakly organized small-medium companies could not effectively mobilize opposition (Teranishi 2009).

Without sufficient safety net programs, it was difficult for the government to push radical market adjustments (Levy 2006). The developmental policy paradigm cultivated a modest welfare system. Japan, South Korea, Taiwan, and Hong Kong had shared "East Asian welfare model." Social security was weakly perceived as a right of citizens and counted heavily on family and company (Kasza 2006). Like Korea, the Japanese bureaucrats and politicians maintained fiscal austerity fearing that Japan would be financially burdened by a European-style welfare state. The social insurance counted on employers and workers' contributions with low benefits. Despite its passive financial responsibility, the government played a leading role in framing employment, welfare, and tax policies.

The Japanese welfare system was highly segmented to benefit various groups unequally. Its distributive interests were represented more by inter-industrial groups rather than by capital-labor division (Teranishi 2009). Since the mid-1970s, the corporate welfare of large firms in oligopolistic industries was enhanced in return for workers' acceptance of wage control. This enlarged the welfare gap by firm size. Regular workers in key industries were well protected by corporate welfare. On the other hand, support for the unemployed or workers in backward sectors were relatively unreliable. During the 1980s, the government's labor market policy centered on maintaining employment security of large firms. It utilized wage moderations by limiting new recruitment, cutting overtime pay, encouraging early retirement through generous severance allowances and relocating dismissed workers to affiliated or subcontracting firms. Under these efforts, employment protection for regular workers remained secure, marking highest in the rank of employment security among the OECD countries.

Then, how to support the small and medium sized firms and declining industries emerged as one of the key issues for the market adjustment. New measures, however, shouldn’t incur financial burden to the government. While pursuing welfare retrenchment, the government tried to maintain social solidarity through coordinated burden-sharing and subsidization among workers (Hitawari, 1998; Teranishi 2009). It expanded its assistance to the employees of less protected sectors or the self-employed. The costs of pension, health care, and tax increase were distributed among key and declining industries. It reallocated the contributions of the large firms to the medical costs of the elderly, which was previously covered by the insurance scheme for the self-employed.

2.2 The neoliberal transition of France

During the first two decades of the post-war era, France achieved rapid economic growth by channeling resources to key industries (Levy 1999). The government nationalized industrial sectors and supported key projects and firms by active currency devaluations, subsidized credit loans, and tariff benefits. These measures contributed to sheltering the French industries from international competition. France's tax structure was less progressive than in the United States and there were many pro-business regulations. The welfare system was based on social insurance programs to favor the middle class with weak commitment to income distribution. For the postwar period, France remained one of the least egalitarian countries of the advanced capitalist countries (Levy 1999).

This interventionist policy frame was effective in achieving high growth rate and making France the biggest economy in Europe until the late 1970s oil crises. The elimination of tariffs and intense competition among European countries weakened the previous competitiveness of France. The neoliberal turn at the late 1970s was instigated by the economic crisis which was perceived to be the outcome of inept state interventions. During 1976-81, Prime Minister Raymond Barre launched market-friendly reforms that reduced subsidies, abolished price controls and deregulated the business sector. However, the reform did not include welfare retrenchment. Barre's reform efforts were not successful. The general public was not ready for a market-oriented policy paradigm. Socialists' victory in the 1981 elections represented this public sentiment. During 1981-1983, the government nationalized thirty eight banks, increased aids to industrial firms, raised taxes and expanded welfare programs, which led to massive deficit problem.

During 1986-88 when Prime Minister Jacques Chirac was in office, excessive nationalization and regulations in the economic affairs were perceived as the main problems (Dobbin 1993). Chirac promised a tax cut (from 45 to 35% of GDP), reduction in government spending (by 1% every year) and privatization of a total of 61 companies (Levy 1999). He embarked on a combination of austerity budgets, privatization, de-indexation of wages, and especially tight monetary policy. The wave of deregulation was initiated by the Right, continued by Left and Right again. Companies would have to receive less government assistance, but would be freer to mobilize financial resources and set prices (Hall 1990). During the Mitterrand administration (1981-1995), key statist tools such as competitive devaluations, industrial policy, nationalization of public sector, and subsidized credits were weakened (Fourcade-Gourinchas and Babb 2002).

Nevertheless, France experienced modest neoliberal transition compared to the Britain and the United States. Its liberalization was much coordinated to deal with potential social conflicts. The government deregulated wage level and dismissal conditions, allowing employers to use flexible labor. However, the deregulation was accompanied by an increase in government spending for labor programs, social protection, and support for small business. France's pay-as- you-go pensions system was among the most generous in the world. Health care spending increased from 7.4 percent of GDP in 1980 to 9.6 percent in 1998, the second highest in the European Union behind Germany (Levy 2006). The government actively introduced early retirement, public internship and training, and guaranteed minimum income programs in labor market and expanded subsidies for low-income workers (Kus 2006). These measures were designed to buffer the blow to the working class and undermine the resistance of labor.

On the other hand, the tax system became more regressive by increasing indirect taxes: the system took a larger percentage from lower-income people or households and less profitable enterprises than from the richest households and flourishing enterprises. This enhanced loyalty to the status quo among the middle and upper classes. Consequently, the economic system was politically less vulnerable to neoliberal creeds of government austerity and rationalization of social protection (Prasad 2006).

3. Developmental Policy Ethos and the Pragmatic Neoliberal Transitions

Korea, Japan, and France shared the developmental policy ethos and institutional biases for high economic growth. They had powerful economic agencies that dictated key economic projects.[61] The top executive bureaucrats of these agencies were growth-oriented interventionists. They strategically allocated resources to targeted industries through subsidized credit loans, intervention in currency and price, and pro-business regulations. Did their shared institutional legacies create similar policy responses to economic crises? Were there unique features of their neoliberal transitions? There are three similarities found among the "developmental" policy responses to economic crisis.

First, the three countries are credit-based economies with an institutional bias for growth. They had the spirit of "catch-up to the global economy" and embraced neoliberal reform as tool for sustained growth, not as the ultimate goal itself. In this context, the impetus for neoliberal transition came from the governments, not the private sector. Market adjustments were approached as national projects to upgrade and adjust the economy to a new global economy, which was a pragmatic and bureaucratic, rather than ideological impetus. In France, neoliberalism was approached as necessary step toward survival and progress. It did not lead to ideological or political conversion (Fourcade-Gourinchas and Babb 2002). Therefore, its attempt to break with old state interventionism did not result in the actual retreat of the government. The government only shifted its focus from dictating industrial policy to providing a market enabling environment (Levy 2006). Government intervention, even ideologically problematized, was not abandoned, while ideologically legitimated deregulations were often incomplete.

[61] Korea has the Ministry of Finance and Economy. Japan has the Ministry of Economy, Trade and Industry. France has the Central Planning Agency and the Ministry of Finance .

Second, the three countries' market adjustments were accompanied by active policy coordination to deal with social conflict and inequality. Politics of pain-sharing was an essential in easing confrontations caused by radical market adjustments in Korea. The government expanded its responsibility for the lower income groups. Kim Dae-Jung and Roh Moo-Hyun regimes kept renewing programs to deal with growing labor market polarization.[62] While focusing on preserving employment security of the large enterprises, the Japanese government pursued cross-subsidization strategy to share burdens for welfare between workers in different industries. France mobilized public funds to ease the frustration of the victims of market liberalization. It enacted early retirement, minimum income program, need-based supplementary health insurance, public internship, and employment subsidies (Levy 2006). These efforts were all the more necessary because labor unions in the three countries were not politically strong without formal parties to represent them. Nevertheless, the government coordination could not solve the increasing gap between regular workers in key industries and non-regular workers in marginal labor market.

Third, their pre-existing institutional arrangements were less vulnerable to neoliberal doctrines of fiscal austerity, tax cut, and welfare retrenchment. Korea, Japan, and France had the lowest ratio of government debt to GDP among OECD countries.

[62] The expanded government supports for the least protected sectors were not successful. The government's need-based rather than merit-based aids for small and medium sized firms, weakened their competitiveness and delayed the market exit of failed businesses. Inefficient and dependent firms more counted on non-regular workers with their decreasing profits and market shares. Only low portion of assigned funds were spent for the least protected workers such as female households heads or elderly work trainees (Yun, J. 2009).

Korea had maintained a tight fiscal policy with extremely limited state welfare. Japan had developed a residual welfare system. Even with universal health insurance and pension systems, government financial responsibilities were quite low. The corporate welfare developed in large firms constituted the pillars of the social provisions where only limited group of labor received full protection (Huber and Stephens 2001). France's reliance on indirect taxes and limited welfare system during the Giscard regime (1974-1981) weakened political ground for orthodox neoliberal reforms (Levy, Miura and Park 2006; Prasad 2005). Pre-existing fiscal austerity led the three countries to an increase in government spending for new welfare programs.[63]

The developmental states' active coordination distinguished their neoliberal transitions from those of non-developmental states. Neoliberalism in Western liberal capitalism is based on faith in markets as more efficient and fair mechanism. It assumes that government interventions distort market operations to generate negative economic consequences. The aggressive oppositions against excessive welfare and the endorsement of privatization effectively mobilized all the discontented people, making transition more conflicting (Kus 2006). The absence of bureaucratic autonomy and central coordination in the United States and Britain aggravated conflicts over to what extent neoliberal reforms should be carried out and how to buffer the pains from adjustment. They

[63] The three countries pursued market adjustment in different intensity. France could dismantle the statist policy framework more than Japan because of its active investments to social policy (Levy, Miura, and Park. 2006). Korea had to embark on the more radical restructuring because of acute economic crisis and the IMF enforcement.

experienced intense ideological and political confrontations around welfare reform and failed economic policies (Gourinchas and Babb 2002).

In the neo-patrimonial context of weak states elsewhere in the developing world, clientilism and low state capacity shaped the nature of the neoliberal transitions (Van De Walle 2001). Persistent failures to achieve development despite the externally imposed IMF economic reforms were attributed to the neo-patrimonial features of the African countries. During the reforms, the regimes were devoted to securing the familial interests of a small number of state elites, transferring the larger burdens to their population. The state capacity was hampered by prebendalism where officeholders systematically appropriate public resources to generate their own material benefits. Political elites use their offices to pursue clientilist practices such as patronage and rent-seeking. Without the developmental orientation and proper state capacity, the patrimonial regimes have been successful only in keeping aid flowing, not in ending the persistent economic crises. Moreover, after the neoliberal reform impulse was subverted, the patrimonial ethos dominated the reform dynamics rather than coordinated "pain-sharing" politics as seen in the experiences of developmental states.

4. Hegemonic Ideas and Institutional Ethos in the Post-crisis Reform in Korea

This dissertation seeks to understand the nature of the post-crisis transition in Korea by examining the encounter between exogenous neoliberal ideas and the endogenous "development" policy ethos. The move to market liberalization was more dramatic in Korea than in other countries. It was enforced in the wake of debt crisis and driven by severe disillusionment with the pre-existing institutions. What did this momentum for change actually aim to achieve and what were the consequences?

Economic collapse puts systems under high stress and cultivates public disapproval of existing cultural paradigm and policy rationality (Gourevitch, 1986). Reform agendas are usually the product of hard times when existing orders and policy paradigm are deemed unequipped to solve the problems (Dobbin 1993). With the late 1990s economic crisis, neoliberal ideas became a hegemonic policy framework, providing a coherent set of reform agendas and policy rhetoric. The economic hostage-taking by the IMF and foreign investors left little room for the Korean government to deal with their demands. However, the acceptance of the IMF programs was not only externally enforced but also internally legitimized among the policy makers who were not able to suggest other alternatives for dealing with the crisis. The IMF programs came as the most ideologically coherent and practically viable road map to recovery.

The interpretation of the causes and remedies of the crisis were shaped by an ideological attack on the developmental policy paradigm. Western opinion leaders were impressed and frightened by the extraordinary economic growth observed in the East Asian countries. Their achievements questioned not only the Western market economy model but also its dominant ideology regarding the proper relationship between government and market. However, the financial crisis in the late 1990s seemed to prove that the Asian growth is a "myth": the growth was driven by not real gains in efficiency but mere inputs of labor and capital (Krugman 1994). Government intervention in the market began to be framed as not only inefficient but also immoral. Neoliberal policy frames were quickly accepted as the tools to fix the existing institutions. The major neoliberal doctrines such as small government, independent central bank, strict capital adequacy and labor market flexibility were explicitly endorsed as ways to constrain highly problematized government intervention. At the same time, they were designated as the necessary means to regaining national credit and launching a new path for sustained growth. The acceptance of the IMF programs was not merely ideologically driven but practically motivated.

An institutional approach to political economy predicts the gradual return to the old rationales after the momentum for change is subdued. After all, a country tends to repeat their old policy strategies because its policy institutions can effectively solve the problems or the country's governing elites lack the administrative capacity to realize new policy strategies (Dobbin 1993). Neoliberal values were powerful as rhetoric to criticize the existing institutions. However, as the new agendas were subject to the countervailing institutional inertia, they were compromised, modified or abandoned by the practical concerns, organizational interests and political culture that are built around the developmental policy ethos.

The government did not experience a drastic retrenchment: it expanded its size and functions in managing post-crisis regime, maintaining closed and rank-based career bureaucracy. Changing the structure and practices of *chaebols* was limited because they were still the core players in the Korean economy. The capital concentration around owners and affiliated firms even increased. The labor flexibility initiatives did not weaken the traditional dual labor market but only widened the gap among workers by protecting insiders at the risk of disadvantaging outsiders. The most successful implementations were made in the policy agendas related to the growing power of foreign capitals such as the banks' firm lending and investments.

There are two institutional and political contexts that compromised the institutionalization of neoliberal doctrines in Korea. First, the acceptance of neoliberal policy frames was driven not so much by ideological force as pragmatic concern. Neoliberal reform was a state-led project that should yield visible and measurable outcomes in a short period of time. Its explicit goal was to stabilize the economy by improving credit rating and restoring market confidence. This context of crisis management vitalized the long-term developmental policy capacities. For example, the government's coordination capacity was enhanced by the politics of pain-sharing. The normative power of pain-sharing had more binding force than neoliberal values in persuading social groups to accept painful adjustment. The urgency of economic recovery made it very hard for each group to defy the call for cooperation from the government. In the trade-offs by the Tripartite Commission, labor had to accept the legalization of collective dismissal, business had to accept streamlining, and the government had to promise the expansion of social protection and administrative rationalization. These policy moves which had been blocked for more than a decade, finally came to fruition. In sum, the projects of market adjustments and pain-sharing revitalized the government interventions rather than constraining them. As happened in the past, the goal-oriented bureaucrats supervised the project of "neoliberal reform." The top bureaucrats used the new rules and standards as regulating tools to intervene in the financial and corporate sectors. This reform context limited realizing the initiative of "market autonomy" by providing the government with the more legitimated disciplining tools for its intervention.

Second, a series of radical reforms did not sacrifice organizational interests and the policy preferences to protect core sectors. Disciplining chaebols and rigid labor market were the main agendas of the market adjustments. These would shake up two protected domains to make the markets more fair and efficient. As discussed above, the government could not fully discipline the problematized practices of chaebols but took a selective approach. Chaebols did not go through fundamental alteration of their capital and ownership structures. The government still maintained rigid rules to protect organized labor. The initiative for labor flexibility could not dismantle the legacy of the dual labor market. On the other hand, expanded social protection could not deal with growing labor insecurity and polarization. Unorganized and less protected workers were not represented by corporate unionism, excluded from collective bargaining and most burdened by deregulations and market adjustments. The gap between workers in employment and protection by firm size and unionization increased.

This study suggests that we need to consider two different stages and dimensions of the post-crisis transition: the adoption of ideas as policy references and the institutionalization of them as enduring policy rationales. The stage of setting reform agendas was more dominated by exogenous, rhetorical, and short-term influences. Neoliberal doctrines emerged as a dominant frame to shape the interpretation of the crisis, set the direction of reform and provided coherent master plans. Policymakers acted as adherents to small government and market autonomy and pro-market advocacy were prevalent in policy rhetoric.

In contrast, the stage of institutionalizing agendas was influenced more by endogenous, enduring, and practical influences. The policy ethos of bureaucratic mobilization is not based on coherent ideology or written rules. However, it dominated the reform processes in which the goal-oriented bureaucrats used neoliberal rules and standards to discipline and guide the markets. The developmental institutional arrangements were imbued with political and economic incentives to protect *chaebols*, organized labor, and cohesive bureaucrats. Neoliberal doctrines were compromised when their implementations contradicted the interests of these prioritized sectors. Recapitalizing the financial and corporate sectors and expanding welfare were practically and politically essential for the success of market adjustments. This increased government spending and debts, violatig the doctrine of fiscal austerity.

The commitment to local ethos that regulated actions influenced the selection and development of a doctrine (Swidler 1986, 279). The dominance of neoliberal doctrine came in the historical event of a severe crisis and the IMF enforcement. The IMF intervention was seen as a shameful but necessary event for penalizing the developmental nexus and setting a new path for the market-economy. The post-crisis reform entailed excessive government intrusion and mobilization of passive private sectors. Korea tried to keep pace with "global standards" while the dominant policy rationales remained defiant of market autonomy. When Korea returned full bailout fund to the IMF in August 2001, its rapid recovery made it a poster child for the success of IMF program. This success, however, did not mean the successful institutionalization of neoliberal doctrines. Severe disillusionment and urgent need for alternatives in the middle of economic breakdown made the policymakers embrace the alleged superiority of Anglo-Saxon model in the reform discourse. However, it did not alter the long-term developmental policy rationales to guide government-market relationship.

Appendix

The National Assembly of the Government of Korea
The transcripts can be accessed through "Knowledge Management System"
(http://likms.assembly.go.kr/record/index.html)

1. The Committees of the Civil Service Commission
2000 年度 國政監査: 國會運營委員會會議錄
2000. November 4

2001 年度 國政監査: 國會運營委員會會議錄
2001 September 15

2002 年度 國政監査: 國會運營委員會會議錄
2002 October 4

2003 年度 國政監査: 國會運營委員會會議錄
2003 September 26

2. The Special Investigation Committee on the Financial Crisis
IMF 換亂原因糾明과 經濟危機眞像調査를 위한 國政調査特別委員會會議錄

1999	January 25	National Assembly Session 200, no.10
1999	January 26	National Assembly Session 200, no.11
1999	January 27	National Assembly Session 200, no.12
1999	February 8	National Assembly Session 201, no.20
1999	February 9	National Assembly Session 201, no.21
1999	February 10	National Assembly Session 201, no.22
1999	February 11	National Assembly Session 201, no.23

3. The Committee of Ministry of Environment and Labor
環境勞動營委員會會議錄

1996	November 5	National Assembly Session 181, no.8
1996	November 6	National Assembly Session 181, no.8
1996	November 22	National Assembly Session 181, no.11
1996	November 29	National Assembly Session 181, no.12
1996	December 12	National Assembly Session 181, no.15
1997	February 19	National Assembly Session 183, no.2
1997	February 20	National Assembly Session 183, no.3
1997	March 10	National Assembly Session 183, no.4
1997	May 16	National Assembly Session 183, no.9
1997	July 14	National Assembly Session 184, no.6

1997	September 24	National Assembly Session 185, no.3
1997	October 30	National Assembly Session 185, no.4
1997	November 4	National Assembly Session 185, no.6
1998	February 10	National Assembly Session 188, no.1
1998	February 12	National Assembly Session 188, no.3
1998	March 18	National Assembly Session 190, no.1
1998	April 2	National Assembly Session 190, no.4
1998	April 2	National Assembly Session 190, no.4
1998	May 15	National Assembly Session 192, no.2
1998	August 15	National Assembly Session 196, no.2
1998	October 15	National Assembly Session 198, no.2
1998	November 19	National Assembly Session 198, no.10
1998	December 18	National Assembly Session 198, no.16
1998	December 23	National Assembly Session 199, no.1
1999	February 5	National Assembly Session 200, no.3
1999	March 7	National Assembly Session 202, no.2
1999	March 18	National Assembly Session 202, no.3
1999	April 19	National Assembly Session 203, no.1
1999	August 5	National Assembly Session 206, no.2
1999	November 17	National Assembly Session 208, no.6
1999	November 29	National Assembly Session 208, no.7
2000	June 23	National Assembly Session 212, no.4

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