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# Discussion Of “Democracy And The Korean Economic Crisis”



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### DISCUSSION OF "DEMOCRACY AND THE KOREAN ECONOMIC CRISIS"

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## **I. Response by Neil Munro**

[The following response is by Neil Munro of the Centre for the Study of Public Policy, University of Strathclyde, Glasgow, Scotland, UK]

The essay by Jongryn Mo and Chung-in Moon entitled "Democracy and the ROK Economic Crisis" makes clear that the policy errors which directly contributed to the ROK economic crisis were the result of ten years of gridlock in the political system. The underlying problem, in their view, is in "the incompatibility between inherited political culture and the requisites for the effective functioning of democracy."

Logically, then, there are two options: either you keep democracy and try to change the political culture; or you accept the culture, and get rid of democracy. Sample survey evidence from 1997 shows that while the mass of Koreans show a range of attitudes that could be characterised as "authoritarian," nevertheless, around 80 percent explicitly reject such undemocratic alternatives as rule by the army. At the same time close to 90 percent agree that the political system should be a lot more democratic than it is now. See the website of the [Centre for the Study of Public Policy](#) for further details of these studies.

## **II. Response by Taehwan Han**

[The following response was submitted by Dr. Taehwan Han of the Department of Political Science at the University of Hawai'i at Manoa]

I read the posting by Jongryn Mo and Chung-in Moon with great interest and pleasure. Their argument not only corrected neo- classical political economists' "I-told-you-so" response to the Korean or Asian economic crisis, but very persuasively challenged those who argue and sometimes advocate that authoritarian regimes are more conducive to economic development than democracy. Although they successfully argued that democracy (or democratization) was not a causal factor of the Korean crisis, the authors failed to answer the follow-up question, which is, "If not democracy, then what is real causal factor of the Korean crisis?"

Mo and Moon argued that "the ultimate cause of the economic crisis in Korea can be found in the failure of the political system that has undergone the process of democratization." For empirical evidences, the authors critically examined three major undemocratic practices or government paralysis and gridlock under civilian democracy after 1992: namely the Kim Young Sam government's inability to reform; its inconsistency and incoherence; and top-down policies and failure to "foster dialogue and cooperation." These patterns persisted throughout the Kim Young Sam regime. They concluded that, "The problem in Korea was not democracy, but the way in which it was practiced."

But these patterns do not seem to be ultimate causal factors but phenomena or problems of government paralysis and gridlock. What the authors should have explained more clearly and specifically is why the Kim government, which received about a 90 percent approval rating in 1992, was paralyzed. I still see a missing link in how those problems caused the financial crisis. There should be both empirical and theoretical debate.

The authors pointed out many economic and political "causes" (i.e., problems in the banking sector, chaebols, bureaucracy, labor, and government) of the crisis under the Kim Young Sam government.

After reading it, it is still confusing which one is the major causal factor or contributing factor(s). If one factor is more important than the others, why is the major causal factor more important? And how do we know?

What's to be done? Partly because of discordant causal factors, the article does not provide sound policy implications and prescriptions. There should be fundamental reasons why the Kim Young Sam government could not implement reform measures thoroughly. Without uncovering and explicating the reasons, the Korean financial crisis is continuously black-boxed.

In conclusion, although the article by Mo and Moon is very timely and persuasive in explaining that democracy did not cause the Korean crisis, it needs more theoretical, methodological, and empirical refinement. The authors described very well what happened in Korea. But what we are still looking for is the explanation of the crisis. I hope the article will be a theoretical and empirical springboard for further discussions of the Korean crisis.

### **III. Response by Hugo WheeGook Kim**

[The following response is by Hugo WheeGook Kim, President of East- West Research Institute, Washington, DC]

#### **1. Why Do I Comment?**

I enjoyed the essay written by Jongryn Mo and Chung-in Moon (hereafter M&M), and I would like to comment on their paper owing to my previous paper presented to a conference at the University of Pennsylvania on February 13, 1998: "Evolution of Democracy and Economic Development in South Korea" (East-West Research Institute Monograph, February, 1998). Please note that the endnotes are not listed to reduce the volume.

M&M's paper focuses on the causes of the financial crisis in South Korea in two categories: economy and politics. In the economy the authors pointed out three elements as causes of the financial crisis: banking failure, heavy external borrowing, and declining profitability of firms. In politics, the paper argued that no fundamental reforms have been achieved, government policies have been inconsistent and incoherent, and top-down reforms created problems rather than solutions -- the immature nature of Korean democracy. In conclusion the authors wrote that "The problem in Korea was not democracy, but the way in which it was practiced.... The public may blame democracy for their economic troubles; even before the crisis, the movement to reevaluate and restore President park Chung hee was gaining strength."

I have three comments on this paper. First of all, the root of the financial crisis is deeply related to the entire system of South Korea: politics, economy, and society. The authors mentioned the issues partially here and there but organized discussions are necessary. Secondly, the paper did not provide reform measures for the government to take actions, which a policy-oriented paper should usually pursue. Finally, I cannot agree with the conclusion: "the problem in Korea was not democracy." I firmly believe that the problem of South Korean economy was and is democracy. Those three points are discussed in the following.

#### **2. The Root Of Financial Crisis**

The major causes for the financial crisis can be investigated through the long history of the political-economic complex. The merger of politics with the economy in South Korea started when President Park Jung Hee launched the First Economic Development Plan in 1962. In the early stage of

economic takeoff, it was necessary for the Korean government to allocate limited resources to specific industries based on the unbalanced growth strategy. President Park provided various subsidies for import substitution and export promotion by suppressing labor movement like in other developing countries, and special favors went to selected business owners in his home province. This created a fortified political base for him to defend the weakness of his regime's legitimacy and to supply easy funds for political operations, which helped maintain his life-long dictatorial rule against anti-government movement until his assassination in December 1979.

As a result, the Korean version of conglomerates, the so-called chaebols, monopolized the domestic market. President Chun and Roh followed the same pattern by enjoying the existing premium, which helped the chaebols grow bigger and stronger. The labor union leaders in Seoul claim that chaebols have accumulated wealth at the people's expense through monopolistic profits, various subsidies and privileges, and suppressed low labor costs, so that a large part of their wealth should be shared with the people. The three theories can be considered here. Firstly, labor movements were suppressed by authoritarian regimes so that a portion of workers compensation unfairly went to business owners. Secondly, chaebols accumulated monopoly profits which were provided by corrupt bureaucrats, so that some parts of the profits should go to consumers. Thirdly, chaebols borrowed money for business, but invested in real estates and gained huge profits illegally, which was protected by politics.

The corruption is deeply rooted in the mixture of preoccupied interest groups in all of the society which are closely connected by region or school. The privileged individuals have enjoyed special treatment on the jobs and have had better opportunities for education, assignment, and promotion in government as well as in business. Senior positions of powerful ministries have been occupied by dominant interests groups, and the number of generals in the Armed Forces was out of proportion with the population share by region. Only one of the three-star generals in the Korean Army was from the Cholla provinces as of January 1998. Major positions even in research institutes have been occupied by the privileged group, and the heads of such groups have tried to justify government policies. The people from the Cholla provinces were treated like third class citizens and suffered from a long history of discrimination. Even successful individuals from Cholla provinces in the government could not consider themselves to belong to the mainstream of bureaucrats. Injustice and inequality reduced efficiency.

The financial crisis in South Korea was caused more or less by corrupt politics, over-expanded businesses, and not-compromised labor. Corrupt politics forced financial institutions to give loans to business groups without proper examination of credit qualifications, so businesses had easy access to the financial market. This caused business over-expansion through debt- financing, raising the capital cost in production. Meanwhile, the Parliament passed labor laws prohibiting layoffs, so the workers could force employers to comply with the continuous demands for wage increases. The high labor cost made businesses prefer investment in foreign countries to seek lower wages, which expedited capital outflow and shortage of foreign exchange reserves. In short, the politics sold their generosity to the businesses as well as to labor for easy compromise, which cannot survive forever in the economy. The high costs of capital and labor reduced the country's economic efficiency and competitiveness, and invited economic decline. Let us investigate these three contributors.

#### (a) Politics and Government Subsystem

The government has been a main source of corruption to protect the chaebols' interests, owing to the lack of checks and balances in politics, bureaucratic monopoly within the administration, and judicial injustice influenced by special interest groups. The candidates for major elections such as for Parliament Members or Provincial Governors are nominated by political party bosses without primary elections, so that the personal loyalty of each candidate to the party boss is essential for

nomination. Dictatorship in political parties is unavoidable as a result, and those elected officials are not free from the control of party bosses. In other words, the bosses of both the ruling and opposition parties steal the voting rights of primary elections in each electoral district, strengthens his or her own political power in the party, and monopolizes party politics. The main source of corruption in South Korea is the lack of checks and balances between the legislative and administrative branches. The Parliament should have impeached President Kim Young Sam in May 1997 for the Hanbo scandal, but his son and his personal staff were jailed instead. DJ won the election in his fourth attempt as a presidential candidate, which could never happen in the United States, which introduced the primary election system one hundred years ago, so no dictatorship in the political party can survive.

The bureaucratic monopoly has interrupted administrative efficiency in Seoul. The Ministry of Finance and Economy monopolized fiscal and financial planning function by controlling central banking, financial supervision, and budget allocation. This Ministry has been a bureaucratic machine of the political- economic complex to protect the interests of chaebols. The Ministry provided or removed regulations for their interests under the guise of efficiency or national interests. In addition to structural and functional problems, the Ministry has been dominated by a special interest group connected by region and school, which was linked to the chaebols. The planning office of chaebols, which is planned to be closed in the new administration, had better access to updated information produced by the government, despite the lack of information flow between ministries. The government bureaucrats have shown to be rigid and without managerial capability in the nation's emergency. The lack of transparency in government contracts has been a source of corruption. Weak coordination between agencies and structural overlapping caused inefficiency.

Social justice problems have been endemic in South Korea. The judicial system, particularly in terms of the senior positions of judges and prosecutors, has been dominated by a special interest group, the graduates of the Law School of Seoul National University. Many trial cases showed that judge-prosecutor- defense attorney were closely connected by their law school alumni gatherings. Meanwhile, the Supreme Court has been a rubber stamp in major political cases. As a result, many Koreans have the general perception that "small fish are caught while large fish run away." This expression must not be far from the reality in light of the Hanbo scandal. Seven big fish serving prison terms have been released, including a son of the President, a personal staff member for the President, and an influential Parliament Member of the opposition party. The theory of non-interference in the judicial system by the administration and by prosecutors set off a transactions of bribes, which became a understandable routine of subsidization or social welfare in the system. If social norms and rules are relaxed by not forcing violators to pay appropriate prices for their wrongdoing, the social justice disappears and goodness is destroyed by badness. If the better quality of human resources is expelled by the worse one, the inefficiency with high costs may prevail in the society.

#### (b) Economy and Business Subsystem

Chaebols have overexpanded under the government protection, and their monopoly power caused problems in the country's economy. Those problems include overlapping allocation of limited resources, heavy debt-financed capital structure, cross- finance guarantee system and lack of transparency, and "money-talks" pollution with unfair income distribution. Korean businesses have a problem of resource allocation owing to flexible access to bank loans, debt-financed capital structure, and ownership dominance by one family in a business group. The chaebols have expanded recklessly without considering the domestic industrial structure, creating idle capacities in one industry and bottlenecks in the other. The overlapping investment with limited resources expedited a shortage of capital and introduced foreign currency problems. For example, Samsung Group

entered the automobile industry in 1994 when South Korea had suffered from over-capacity in that industry. Hanbo Group, the fourteenth-largest chaebol, collapsed by leaving US\$5.8 billion in bad loans in building a steel plant. Hyundai Group was planning to enter the steel business while Dongbu Group announced plans to enter the semi-conductor business, though they shelved the plans after the financial crisis. These raise the adjustment costs for industrial restructure in the future. It is fortunate the IMF rescue program can force corrections, though old habits die hard.

Heavy debt financing in business raised capital costs, weakening global competitiveness. The chaebols could secure bank loans relatively easily owing to the cross-finance guarantee system with political support from the ruling party, so businesses preferred bank loans to public offering of company's stocks for governance of company's decision-making. The average debt of thirty chaebols was 3.33 times their average net worth by the end of 1996. The high debt-equity ratio raised capital costs and the prices of their products. High costs reduced competitiveness and exports, inviting a trade deficit and causing balance of payment problems. The high labor costs pushed domestic industries to seek overseas investment for lower production costs and easy access to the market, which expedited capital outflow and reduced foreign exchange reserves. Stock-financing is safer if the business is riskier, but debt-financing would not be bad if the business seems to be profitable. The borderline lies in the survival of businesses with strong competitiveness in the world market in terms of costs for the same quality products in the same industry.

The cross-finance guarantee system within the group companies and lack of accuracy with transparency in financial statements made heavy debt financing possible. A company is legally allowed to be financially guaranteed by other companies within the group to get bank loans, which means that companies in a group are mutually supportive in financing that was not available to non-group companies. This jeopardized fair competition between group and non-group companies in the same industry, so that the chaebols killed most small and medium sized businesses. This kind of monopoly introduced a chain of subcontracting systems in South Korea, which raised overhead costs charged by various middlemen in subcontracts. Therefore, available funds for the last subcontractors became far shorter than actual production costs, which threatened the quality of output products and led to the collapse of bridges and department stores in Seoul in recent years. The lack of transparency in financial statements helped chaebols to hide their financial weakness in loan applications. This also made it possible for chaebols to avoid paying the proper amount of taxes for their transfer of assets to the second generation by giving stocks or property ownerships.

The monopolistic or oligopolistic profits of chaebols worsened income distribution and widened the gap between rich and poor. The chaebols have largely contributed to contaminating the traditional values of the society by spreading a wrong idea that bribes can make everything possible, as evidenced in the Hanbo scandal and the trials of former presidents. The pollution of "bribe talks" confused the people about truth, justice, love, equality, and efficiency in the society and invited antisocial crimes among the young generation. The corruption is the main source of inefficiency and inequality in the Korean economy.

### (c) Society and Labor Subsystem

It is understandable that labor unions became violent, aggressive, and non-compromising in negotiations to recover their interests which were exploited in past authoritarian regimes. An input-output analysis shows that the share of employee compensation in GDP in manufacturing industries for South Korea and Taiwan was 31.8 percent and 44.3 percent in 1974, 41.8 percent and 47.1 percent in 1980, and 42.6 percent and 50.0 percent in 1986, respectively. This implies that employees of South Korea gained 8.3 percent less compared to those of Taiwan in terms of GDP share. Assuming other factors were not much different between the two economies, labor in South Korea lost over 8.0 percent of GDP in average labor income than that in Taiwan during the period of

1974-1986, which went to business owners. However, the workers have partially contributed to the current financial problems since 1988 by creating high labor costs, prohibiting layoffs, and other costs caused by labor unions.

The labor unions have become powerful in wage negotiations with chaebols since 1988, when their members gained more compensation than productivity growth on average. The high wages raised production costs and reduced the competitiveness in foreign markets, which lessened exports. On the other hand, businesses sought out low-cost labor in foreign countries for investment such as in China, Vietnam, Indonesia, India, and eastern European countries. Both export reduction and capital outflow for overseas investment expedited the shortage of foreign currencies.

When a business loses its competitiveness, sales go down and employment falls, then layoffs become necessary for survival. The labor unions should understand that the collapse of business will cause the loss of entire jobs as a natural consequence. Under the IMF program, the forced layoffs are unavoidable in the process of economic restructuring. It is the workers' rights to force both government and business to take the proper responsibilities in structural adjustment, but the layoffs are a different issue. The prohibition of layoffs is a kind of socialism which is not for efficiency, but for equality. This is not acceptable to survive in the competitive markets of the age of globalization.

The employees who did not work should not get paid. The current labor laws through the latest revision prohibits union staffs from receiving wages from members' employers. However, union leaders have tried to regain that privilege in negotiations with the Tripartite Committee. The rule of "no work and get paid" cannot survive in the capitalist economy. It is unbelievable for union staffs to try through negotiations to receive their payrolls from the employer for labor activities against management. This is labor's collaboration with management or a kind of cheating by themselves, which is not ethically acceptable. The high overhead cost in the business reduces its competitiveness in the market and its efficiency in the economy.

### **3. Economic Development And Democratization**

In the modernization process, the political leadership in developing countries emphasizes economic development to escape from the vicious circle of poverty. Authoritarian leaders organize resources to build the economy by restricting political freedom, which can be partially compensated for by economic gains. As the economy grows, it becomes possible for the business power to purchase politics by bribes. The corrupt politics provides monopoly power to certain business owners in return, which reduces efficiency and competitiveness in the world market. The loss of competitiveness gradually reduces the country's exports, employment, and income, which invites recession to the economy. The economy would not revive until the corruption is removed because the lagging political development interrupts economic efficiency. So the policy of balanced development between politics and economy is introduced. The corruption requires adjustment costs for the system to balance the differences between the two subsystems in development.

#### **(a) Evolution of Democracy and Economic Development in South Korea**

The growth of the South Korean economy can be divided into three stages by considering political development: the first stage is President Park's period of economic takeoff under the authoritarian regime (1962-1979), the second stage is the post- Park period of conflict between democracy and economy (1980- 1997), and the third stage is that of structural adjustment and harmonious growth between politics and economy (1998- ). Since the third stage is just beginning with the new administration, it includes future development and desirable policies or actions with which the DJ leadership and following administrations should improve the system to make it similar to many western industrialized nations: full democracy and full market economy. Since we already discussed

reform measures and the dynamics of politics and economy previously, the third stage will not be discussed here.

First stage (1962-1979) Economic Takeoff Under Authoritarian Regime: There was no democracy but one-half market economy in this period when President Park Jung Hee began to take over by military revolution. He fortified an authoritarian regime by suppressing all freedom factors against him and launched a series of five-year economic development plans beginning in 1962 by which the Economic Planning Board allocated available resources and managed overall development affairs. The Korea Development Institute supplied quality research for policy recommendations to the government as a dominant think tank in Seoul. South Korea pursued the export-led growth strategy in terms of import substitution by balanced growth and export promotion by unbalanced growth. Meanwhile, the industrial structure began to shift gradually from labor-intensive to capital-intensive industries during this period as projected by the EPB, which merged into the Ministry of Finance and Economy in December 1994 to reduce government intervention..

An input-output analysis by this author indicated that the export-led growth strategy of South Korea was the best choice among available alternatives due to following reasons. This strategy generates the largest amount of GDP for the same level of aggregate final demand. Import substitution requires a huge amount of physical and human capital which can be financed by export earnings, while export promotion requires advanced technology which can be accumulated by import substitution, so both are mutually supportive and complimentary. Since export promotion is accompanied by increasing demand for imports, profits coming from exports declines significantly without import substitution. Movement of comparative advantage due to the product-life cycle requires structural changes to be absorbed by import substitution, that helps to maintain international competitiveness of domestic products. Finally, the supportive strategy of domestic demand expansion is desirable when market openness does not suppress consumption of domestic products in fair competition. The government intervention was successful in the early stage of economic takeoff until the third five-year Economic Development Plan ending by 1976, but caused serious problems in efficiency, equality, and democratization in later years.

The purpose of government intervention in the free market is to achieve two goals: either efficiency or equality. The export-led growth strategy exploits economies of scale through trans-border trade despite narrow domestic markets. The competitiveness of domestic products is enhanced by taking comparative advantage with favorite patterns of trade via efficient resource allocation. This expands the production possibility frontier. The competitiveness is reinforced by both protection and subsidization, which allows monopolistic profits to export industries. In reality, the cost of incentives became serious in South Korea though overall returns from export promotion was larger than the costs of incentives in the economy. Three problems became serious as the economy grew. The first was inefficiency from distorted industrial structure due to poor resource allocation, the second was income inequality between chaebols (plus corrupt bureaucrats plus collaborating intellectuals) and others, and the third was heavy social costs coming from suppressed democracy by authoritarian regime. So the government could not achieve both efficiency and equality, and voices demanding freedom and democracy became louder in South Korea. The South Korean government analyzed that "inefficiencies have been imbedded in the Korean economy ... government-initiated investment activities as well as protective measures, such as import restriction and monopolization, have weakened economic versatility and hindered proper functioning of the market mechanism ... the inequalities between income classes and regions were aggravated." The assassination of President Park in 1979 among social instability partially reduced the problems.

Second stage (1980-1997) Conflict Between Democracy and Economy: This was a period of the three presidents of Chun, Roh, and Kim. The Chun-Roh period was one-half democracy with three-quarter



market economy when united freedom-fighting forces challenged the regime's legitimacy. President Kim Young Sam allowed full freedom of democracy, but there was no difference from previous regimes in the political decision-making process. The corrupt politics were generous to business and labor, which invited structural problems in the economy by creating lack of efficiency and competitiveness. Since we have discussed the reasons why corruption introduced inefficiency already, our discussions here is limited to the dynamics of interactions between economic development and democratization in the society.

When peoples are poor, bread is more important than freedom and democracy. South Korea did not have enough westernized intellectuals to incite military revolution against President Park Jung Hee in 1960s. But the situation gradually changed. Firstly, the export-led growth strategy of Park's government expanded foreign trade, which required more education and training internally and externally. Education and training awakened people toward ideals of freedom and democracy against the authoritarian rule. Secondly, trade expansion and technological advancement accelerated information flow between individuals without national borders due to more transportation and communications, which prevented the government from monopolizing the sources and means of information. The general public became aware of the outside world, so that no authoritarian leaders could fool the people, which expedited democratization in South Korea. Thirdly, as the economy expanded exports rapidly, accumulated profits from exports created a wider middle income class who paid more taxes and wanted more political power. An increasing middle class liberalized society due to strong voting power. Finally, increasing trade relations and foreign direct investment forced public policies vulnerable to foreign pressures such as human rights, trade liberalization, and other interests, which expedited democracy. In other words, economic development with export promotion in South Korea invited greater education and training, more information flow, wider middle income class, and rapid internationalization, so that driving forces for democratization became aggressive.

Anti-government sentiment, in fact, began to evolve in 1972 when President Park revised the constitution by force for life-time rule. The suppressing forces of the authoritarian regime were strong and the driving forces of democratization by the people were relatively weak, so that there were no hopes for further liberalization. However, liberal politicians and underground labor supported by left wing students accumulated driving forces for a democratic revolution. The Kwangju incidents forced President Chun to transfer the power to President Roh, which reduced authoritarian rigidity while the system remained unchanged. President Kim (YS) was the first civilian president and tried to remove military culture from the government. He allowed full freedom and liberty in politics, but his lack of knowledge and experience made him ignore the democratic decision-making process, and his style of authoritarian leadership caused trial and errors. After the Hanbo scandal he lost control of his presidency and President-elect DJ became in charge of a one-half presidency at his private home since December 18, 1997.

Economic development and democratization are closely related as shown in history. China has survived while the Soviet Union perished in the process of economic transformation. Economic reform proceeded political in the former, while political reform proceeded economic in the latter. "The collapse of the USSR can be explained by the fact that its failing economy could no longer support the country's vast political-military system, and the bankrupt government could no longer guarantee law and order. In contrast, Deng Xiaoping adopted an open policy, which attracted foreign capital and promoted exports, pursuing economic transformation followed by political reform." Deng's open policy increased foreign trade and overseas education, but he did not expect freedom waves coming from openness to hit a Beijing's square so fast and violently in 1989. Similarly, President Park pursued the export-led growth strategy, but he did not expect freedom waves hit the streets of major cities so violently by threatening his regime. Economic development

requires foreign trade, which brings freedom waves into the society. Any authoritarian regime can delay the freedom waves for a while but cannot stop them.

#### **4. Conclusion of Comments**

The financial crisis in South Korea was a situation of foreign exchange shortages, so the country was unable to repay its external debts. The problem was solved temporarily through IMF rescue and restructure of short term debts owing to the support of U.S. leadership. The crisis was caused by a continuous trade deficit, Won appreciation, currency devaluation in neighboring countries, sudden withdrawal of foreign funds, short term loan structure, inefficient business investment, and poor government management. Since the economy has lost efficiency, the country cannot sustain the burden of debt repayments without structural reforms by fixing three monopolies in the system. The ROK government should introduce the primary election in politics to remove a political monopoly weakening checks and balances, which will prevent corruption and will recover efficiency in the system. The chaebols should eliminate monopoly power in the market through transparency, no cross-finance, ownership-finance, and streamlining of business, which must be enforced by laws. The labor market should be flexible by removing layoff prohibitions, which will improve business efficiency and will attract foreign capital.

As the economy grows with foreign trade, the society gradually moves toward democracy. Rising education and training awaken people toward ideals of freedom and democracy. Trade expansion and technological development accelerate the flow of information despite government control. Accumulated wealth widens the middle income class paying more taxes and demanding more political power. The internationalization of the economy becomes sensitive to external pressures from human rights groups, which expedites democracy. On the other hand, the East Asian model of economic development gives the following lessons. Democracy is essential to maximize capitalistic efficiency due to lesser intervention costs with fast feedback adjustment. The balance between political evolution and economic growth is desirable to minimize adjustment costs caused by lagging subsystems. The economic development plans were efficient in the early stage of takeoff, but created more problems in the later years when the economy became complicated. The East Asian model of pursuing export-led growth strategy is the best choice, and the financial crisis is one step in economic development. The structural reforms are an adjustment cost South Korea has to pay in the process of modernization.

South Korea is now approaching the western standard of democracy and market economy through structural adjustment. The DJ leadership has been successful in facing the financial crisis, but should pay attention to the following. Firstly, the leadership must have a strong reform mind with aggressive driving forces. It is very hard to change old habits. DJ should keep in mind that chaebols never want to lose previous favors because they are ruthless profit takers. Secondly, the inner circle of leadership should not be corrupt for any reason as experienced in the previous administrations. The properties of DJ and related individuals should be closely watched by the people. Thirdly, time is essential in structural reforms and economic development. Do expedite the reform process in government as well as in business. The invested asset values are depreciated while interests of foreign debts grow day by day. Finally, Seoul should not confuse nationalism with patriotism. Purchasing Korean stocks by foreigners is desirable and better than bank loans. Nationalism hurts the economy in the age of globalization, which is not patriotic.

The economy pursues efficiency to get more profits while politics tries to accomplish equality to get more votes. Socialist countries give major importance to equality while the capitalist countries emphasize efficiency in the system. The efficiency is linked to productivity and competitiveness in the economy, but the equality is linked to affirmative actions to protect minority groups, which may reduce efficiency in the system. The conflict and tradeoff between efficiency and equality must be

managed. The labor unions in South Korea have forced rising wages, which reduced competitiveness and exports. This lowered employment and income, which returned to workers as a feedback. South Korean workers may lose around 20 to 30 percent of wages in the next two years if they don't lose jobs. The government and labor leaders should be smart enough to find the optimal point of wage negotiations. If the goal of equality damages that of efficiency, the whole industry may disappear just like the USSR, which pursued equality first and efficiency second. In the age of capitalism and globalization, the survival strategy lies in efficiency first (three-quarters), and equality later (one-fourth). The theory of "more efficiency and less equality" is applied to all countries including transition economies such as China and North Korea.

#### **IV. NAPSNet Invites Your Response**

The Northeast Asia Peace and Security Network invites your responses to this discussion or the original essay by Jongryon Mo and Chung-In Moon. Please send responses to: [napsnet@nautilus.org](mailto:napsnet@nautilus.org). Responses will be considered for redistribution to the network only if they include the author's name, affiliation, and explicit consent.

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