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Effects of International Monetary Fund's Financial Crisis Policy Program in the Republic of Korea

In 1997, the Republic of Korea (also known as South Korea or ROK) was in a massive financial crisis. Originating from Thailand, the financial crisis was causing a massive depreciation of ROK's currency and bankrupting many South Korean conglomerates. ROK government used its foreign currency reserve to mitigate the currency depreciation but failed to ameliorate the situation. Unable to guarantee its debt, ROK applied for a loan from the International Monetary Fund (IMF) in exchange for IMF's recommended policy program on December 1997 (Henow, 2022, pp. 10-11; Kang, 2018, p. 654). According to a presentation at the Korea Economic Daily Conference by IMF regional director Kunio Saito (1998), IMF's program pushed for higher interest rates to attract foreign currency to the ROK and encourage asset ownership in Korean currency; IMF also pushed for corporate and financial sector reform, a more flexible labor market, and the liberalization of capital account transactions and trade (IMF-supported Program section). Saito (1998) claimed that IMF's program was the best possible program for helping ROK with the crisis and would help ROK economically in the long term (Conclusion section). <u>However, in practice, IMF's policies in response to ROK's financial crisis in 1997 further destabilized ROK's society and economy not only to the point of causing a countermovement against IMF's policies but also by pushing ROK towards an embedded neoliberal economic system.</u> Before diving into IMF's policies, this paper will first use ideas from Jamie Peck to describe ROK's progress in neoliberalization by the time of the crisis. Then, this paper will use David Harvey's ideas to explain how IMF's policies were designed to enforce the Washington Consensus and empower the American elite at cost of destabilizing ROK's economy. Then, this paper will use Karl Polanyi's ideas to discuss ROK's subsequent countermovement against IMF's policies. Afterward, this paper will use ideas from Peck and Polanyi to discuss how IMF's policies pushed ROK towards becoming an embedded neoliberal state.

By 1997, ROK was already deep into the roll-back stage of neoliberalization. Before the 1980s, under the developmental regime of dictator Park Chung-Hee, ROK became industrialized through top-down measures with the state regulating almost all facets of the economy and centering economic development around family-owned conglomerates called *chaebols* (Henow, 2022, pp. 5-6). Moreover, the state, the chaebols, and the banks cooperated in strengthening the interdependence of corporate, industrial, financial, labor, and political institutions – creating the state-chaebol-bank nexus (Šitera, 2014, p. 84). However, after the assassination of Park in 1979, neoliberal ideas began gaining traction in ROK due to political pressure from both the public and the chaebols to move away from Park's top-down regime (Henow, 2022, p. 6). The U.S. and the U.S.-trained Korean economists in ROK's government also pressured ROK to adopt neoliberal policies throughout the 1980s and 1990s, especially as ROK tried to join the Organisation for Economic Co-operation and Development (OECD) for global legitimacy (Harvey, 2005, p. 110; Kang, 2018, pp. 639-653). Consequentially, ROK began going through the process of neoliberalization after the assassination of Park. In his book *Constructions of Neoliberal Reason*, Peck (2010) defines neoliberalization as a process of state-negotiated market-esque rule with support towards laissez-faire policies (p. 20). Peck (2010) also divides the development of neoliberalization into two phases – roll-back and roll-out phases (p. 22). The roll-back phase occurs at the beginning of neoliberalization and involves making crude movements toward deregulation (Peck, 2010, pp. 22-26). As ROK tried to join OECD in the 1990s, ROK began quickly going through the roll-back phase of neoliberalization, deregulating financial activities, international capital flows, and interest rates (Henow, 2022, p. 9). But, according to Kang (2018), ROK's deregulatory policies were implemented in haste and ended up restricting long-term foreign borrowing more than short-term foreign borrowing (p. 654). The fast pace of ROK's roll-back phase pushed ROK into financial vulnerability. Since the 1980s, the chaebols relied on domestic nonbank financial institutions (NBFIs) for funding to obtain commercial bank shares and avoid government control. However, ROK's liberalization policies caused NBFIs to rely heavily on short-term foreign debt, eventually causing many chaebols to fail from sudden changes in the foreign exchange market in 1997 (Henow, 2022, pp. 7-10).

However, as noted by David Harvey, IMF's policies were intended to enforce the Washington Consensus and enrich the Wall Street-IMF-Treasury complex even at the cost of further destabilizing ROK's economy. According to Sacchi and Roh (2016), the high interest rates and the corporate and financial sector reform led to over 20,000 firms going bankrupt in 1998; while greater flexibility in the labor market motivated remaining companies to fire many workers, massively increasing the unemployment rate (p. 362). As David Harvey points out in his book *A Brief History of Neoliberalism*, the inefficacy of IMF's policies is not surprising. A decade earlier in the 1980s, the United States (U.S.) and the United Kingdom (UK) adopted similar neoliberal policies but did not perform too well economically, whereas ROK performed better economically without adopting these policies (Harvey, 2005, p. 88). Even so, Wall Street, IMF, and the U.S. Treasury worked together to force many countries to adopt these policies through IMF's structural adjustment programs in order to gain high financial and corporate returns from the rest of the world. Such work from the Wall Street-IMF-Treasury complex contributed to the rise of the Washington Consensus in which the American and British versions of neoliberalism were seen as the solution for much of the world's problems (Harvey, 2005, pp. 92-93). According to Harvey (2005), neoliberalism is a political economy theory that encourages individual liberty and entrepreneurship (p. 2). However, Harvey (2005) also notes that neoliberalism is in practice a political project to allow the economically privileged to re-accumulate capital and regain power (p. 19). IMF's policies in ROK were not only an extension of the Washington Consensus but also of the neoliberal project of capital accumulation and power restoration for the U.S. economic elites even at a considerable cost to ROK's economy, as the U.S. tried to better its economic interest even as ROK was economically struggling (Harvey, 2005, p. 111).

In a Polanyian countermovement against IMF, ROK began disobeying some of IMF's policies and expanding its social welfare system. In his book *The Great Transformation: The Political and Economic Origins of Our Time*, Polanyi (2001) notes that modern society is organized around a double movement, consisting of not only a movement towards a self-regulated market but also a countermovement against the harmful effects of the market (pp. 136-138). ROK ended up experiencing such a countermovement against IMF's policies due to the negative side effects of these policies. For instance, to speed up its economic recovery, ROK dropped IMF's contractionary economic policies and turned to expansionary economic policies by decreasing interest rates and increasing public spending during the crisis despite criticism from the IMF and the World Bank during the crisis (Henow, 2022, p. 11). Also, during this time, ROK adopted new welfare policies such as temporary assistance programs, public works programs, and expansion of unemployment insurance to counteract the increase in unemployment from IMF's policies. Much of the expansion in social welfare can be attributed to Kim Dae-Jung, ROK's president at the time. With strong domestic support from the lower middle class, Kim saw that IMF's policies harmed both his supporters and the party members, leading him to emphasize social welfare policies (Sacchi & Roh, 2016, pp. 363-364).

However, ROK still had to adopt most IMF policies in exchange for the loan and consequentially underwent a roll-out transformation into a hybrid neoliberal regime throughout the crisis. As defined by Peck (2010), the roll-out phase occurs after the roll-back phase and involves the use of state intervention to better fulfill neoliberal ideals (p. 26). Seeing the chaebols and the NBFIs as the main source of the crisis, ROK's government pushed through IMF-requested corporate sector reform – choosing which chaebols to rescue, encouraging greater transparency and accountability in corporations, limiting chaebols' financial dependence on NBFIs, and forcing chaebols to swap their main industries – to weaken individual chaebols and NBFIs. The government also nationalized the banking sector for restructuring and recapitalization to help fulfill IMF's request for financial sector reform. Also, the government allowed for greater foreign direct investment and greater foreign stock ownership – weakening chaebols' financial power through the increased power of foreign investors in the domestic financial market while following IMF's request for deregulation (Henow, 2022, pp. 11-13; Saito, 1998). Also, ROK's government saw the state-chaebol-bank nexus as the main cause of the financial crisis, so ROK's government destroyed the nexus and changed the state's role from enforcing the state dirigisme to regulating ROK's economy in favor of the market (Šitera, 2014, pp. 86-87). As a result, ROK's government ended up establishing a hybrid regime of both neoliberal and state-centered economic policies (Henow, 2022, pp. 11). With the state intervening in the economy to implement IMF's policies, ROK entered the roll-out stage of neoliberalization.

Over time, IMF's policies caused ROK to become an embedded neoliberal state both on a global level through a reconfiguration of ROK's political economy and later on a local level through a countermovement against this reconfiguration. Peck (2010) defines embedded neoliberalism as an international system in which countries accept their existence in a multilevel, open, and market-esque world undergoing globalization and change their political economies under this acceptance (p. 30). ROK already accepted its existence in a globalized world before the crisis by pushing the nation towards the paradigm of *segyehwa* (globalization) in the 1990s (Šitera, 2014, p. 81). ROK also made its first attempt to change its political economy accordingly by letting market forces take the state's role of pressuring laborers and industry to work better via exposure to the forces of globalization, but ROK's attempt failed and only led to the aforementioned financial crisis (Šitera, 2014, p. 86). During the crisis, ROK made another such attempt by establishing an entirely new hybrid neoliberal regime per IMF's policies, establishing ROK as a more well-established embedded neoliberal state on a global level. But ROK faced massive backlash for its neoliberal policies under this regime. For instance, ROK liberalized the credit card industry to stimulate domestic consumption – leading to a massive increase in household debt and causing a liquidity crisis among credit card companies in 2003. Also, ROK faced a massive increase in real estate prices since 2001, as the deregulation of the real estate market increased demand for real estate but failed to increase the supply of real estate accordingly (Henow, 2022, p. 13). Ultimately, around the beginning of the Global Financial Crisis in 2007, the hybrid regime was replaced due to the return of developmental forces, symbolized by the election of former chaebol executive Lee Myung-Bak as ROK's president. Under Lee, ROK revived the state-chaebol nexus from the developmental era while maintaining much of the characteristics of a globalized neoliberal state. Chaebols continued to accept the global market's demands and followed the market's neoliberal push towards a knowledge-based economy. Foreign investors maintained their power over ROK's banking system. But ROK's government also began intervening in the affairs of the central bank and the banking sector while establishing new developmental trends for chaebols to follow. Essentially, ROK continued to accept its place in the globalized world but began embedding the neoliberal characteristics of its economy into the restored chaebol-state nexus in a Polanyian countermovement against the previous regime (Šitera, 2014, pp. 87-88). As a result, ROK became an embedded neoliberal state both on global and local scales.

Unfortunately, ROK's transformation to an embedded neoliberal state reduced South Korean workers' labor rights and destroyed traditionally held societal values, further destabilizing ROK's society. South Korean labor already was weakened after the financial crisis, as South Korean labor was forced by the government and businesses to adopt IMF's labor market policies (Haggard et al., 1999, pp. 211-212; Šitera, 2014, p. 91). Consequentially, ROK suffered from a significant increase in the number of non-regular workers and from discrimination in the labor market by gender, age, education, et cetera. (Šitera, 2014, p. 92). After the election of Lee, ROK's government later allowed stable employment protection for skilled workers but also took away such protection from unskilled workers to allow for their expendable and inexpensive commoditization (Šitera, 2014, p. 93). Also, while the developmental regime tried to embed the industrial economy into a Confucian industrial matrix to espouse traditional Confucian values, the embedded neoliberal regime did away with these values – encouraging competition, efficiency, individualism, and friendliness towards the market over the traditional community-centric values of cooperation, harmony, and collectivism. In the process, South

Koreans abandoned familial values and began having fewer kids, eventually turning ROK into one of the most rapidly aging and least fertile societies in the world (Šitera, 2014, pp. 94-95).

Now, there were some positives to IMF's policies here. According to Cho and Shin (2012), ROK's labor market was overly rigid and over-employed at the time of the crisis (p. 175). Cho and Shin (2012) also state that greater flexibility in the labor market moderated the impact of the Global Financial Crisis in ROK in the 2000s (p. 175). However, Cho and Shin (2012) also noted that IMF's contractionary monetary policies unnecessarily worsened ROK's economy during the crisis in the 1990s (p. 172). Also, according to Choi (2016), the increase in labor market flexibility moderated the trend of increasing inequality in ROK during the financial crisis in the 1990s (p. 1069). Choi (2016) notes that this could be because lesser-skilled workers may be given more chance for upward mobility than higher-skilled workers in a financial crisis (p. 1050). However, Choi (2016) notes that this moderating effect was modest and that such policies lowered job security overall (p. 1069).

In summary, while ROK was in its roll-back stage of neoliberalization, ROK fell into a financial crisis and IMF's policies for ROK – intended to serve the U.S. financial elite at tremendous cost to ROK's economy – destabilized ROK's society and economy so much that a countermovement ensued in the form of a switch to expansionary economic policies and the expansion of the welfare system. Eventually, in complying with much of IMF's policies, ROK entered the roll-out stage of neoliberalization and established itself firmly as an embedded neoliberal state on a global scale. However, ROK faced massive backlash from implementing IMF's policies, so another countermovement rose and made ROK an embedded neoliberal state on a local scale. ROK's new neoliberal regimes ended up destabilizing ROK's society by reducing labor rights and de-establishing traditional social values. As noted by Harvey (2005), ROK is not the only country that experienced such policies – countries like Mexico and Argentina also implemented similar policies from IMF in exchange for a loan during the time of economic instability, but IMF's policies came at the cost of societal stability in these countries as well (pp. 98-106). It is time for IMF to reconsider its policy framework so that other countries will not suffer the fate of ROK and other afflicted countries in the future.

Total Word Count: 2494

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