

Bankers Trust Company



Country Assessment

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SOUTH KOREA 1983:
A SAMPLE POLITICAL ANALYSIS

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This paper is an actual briefing memorandum prepared in January 1983. Because of the large exposure of Bankers Trust in Korea, the unusual global financial environment, and the recent political changes in Korea, the memorandum is unusually detailed. Except for its length, it represents a recommended model analysis.

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I. The Government

South Korea's political, economic, military, and diplomatic performance rest on a bedrock of institutional excellence. South Korea has been fortunate in having top leaders who are extremely patriotic, honest, and skilled at creating institutions and managing an economy. The country's central institutions, notably the military, the civilian ministries, and the principal businesses, are led by highly trained and broadly experienced executives, mostly in their 40's and mostly with the highest level of American education, supplemented by domestic management experience. The military has been subjected to the discipline of competition with North Korea, the principal business organizations to the discipline of international markets, and the performance of executives in government ministries to the disciplines of frenetic competition from highly trained competitors and incessant scrutiny by the Korean CIA (KCIA). Effective coordination of these institutions, public and private alike, has been achieved by a combination of direct presidential authority and KCIA planning and coordination.

The capabilities of these institutions are revealed by their performance in normal times and particularly in times of crisis. Since 1961, the military has become one of the world's most highly regarded conventional military forces. From 1961 to 1979, South Korea's GNP grew at a rate of almost 10% per year. The proceeds of this growth have been distributed in more egalitarian fashion than in the vast majority of Third World countries. Park Chung Hee's 18 year rule was an unusually long period of stability by Third World standards. The polity has held together in the face of repeated challenges of various kinds by North Korea. The economy has consistently performed well even in the face of severe external shocks: fully dependent on imported energy, it took only two years to restore payments equilibrium with the Middle East after the 1974 oil price rise; totally dependent on exports, it managed to increase exports 20% during the 1975 recession and to grow 6% a year during the 1981-'82 recession. It has consistently increased export revenues in the face of protectionist barriers by improving quality when volume was controlled.

This record of performance has generated a relatively broad base of social support for the government. The government is supported by a military which is convinced that the government has adequately protected national security, by government officials who are proud of their ministries' performance records, by industrialists and entrepreneurs who have benefited from rapid economic growth, by farmers who have likewise benefited, and by workers in the most advanced industrial sectors. There is a national consensus on an anti-communist political stance, on maintaining the relatively open economy, on the need for strong defense against North Korean invasion, on a major role for the dozen largest industrial firms, and on maintaining American troops in the country. Even the "radical" opposition supports these goals.

II. The Opposition (and Recent Instability)

This combination of effective top leadership, highly efficient institutions, and a relatively broad popular base has successfully dominated an opposition whose leadership has been eloquent and idealistic but narrowly experienced, whose institutions have been weakened by deliberate government

harassment and by government cooptation of most of the country's most capable technocrats, and whose social base is confined to academics, students, large proportions of the Christian community, the majority of workers outside high technology industries, and limited segments of the middle class. This imbalance of leadership, institutions, and popular support explains South Korea's generation of stability despite constant Western press predictions of instability rooted in human rights complaints.

In 1979-1980, this record of favorable political and economic performance was interrupted by the assassination of Park Chung Hee, a severe decline of GNP, a mini-coup within the army, a major social uprising in Kwangju, and a period of policy confusion. The causes of this dangerous interval were several. First, Park Chung Hee had aged and the quality of his decisions was deteriorating. Second, serious over-investment in heavy industry, three years of wage rises in excess of 30%, and the oil shock of 1978 were accelerating inflation, undermining growth prospects, and reducing South Korea's international competitiveness. Third, the aging Park became more distant and authoritarian, while economic success swelled the numbers and organizing capabilities of the key groups, most notably academics, workers, and sections of the middle class, which were determined to promote democratization and willing to demonstrate for their views. Fourth, in response to these difficulties, a major split emerged between the presidential guard, which was extremely hard-line and conservative, and the KCIA leadership, which felt that Park was making bad economic decisions and that accomodation with the newly emerging political forces was a national necessity. The head of the KCIA shot Park in September 1979, plunging the nation into a year of uncertainty.

The assassination was quickly followed by a rapprochement between major civilian government leaders and opposition leaders, who agreed on a program of democratization and on all the major aspects of a new constitution. In December 1979, however, a group of young army leaders under Chun Doo Hwan seized control of the army and began to take over the KCIA and infiltrate civilian government institutions. Meanwhile, the economy, already plagued by severe inflation, suffered from adjustment to rising oil prices, from a massive harvest failure, from world recession, and from the shock of political insecurity, and declined from an 8% growth rate to a minus 6% growth rate. Economic discontents and the emerging certainty that there would be no free election led to an uprising in May 1980 in Kwangju, the isolated, deprived home province of the country's principal opposition leader. The uprising and the economic difficulties were used as the reasons for imposition of a new government under Chun Doo Hwan.

The Chun government neutralized the key opposition political leaders, jailing one, putting another under house arrest, and depriving the third of his fortune and his right to participate in politics. Chun created his own Democratic Justice Party, which easily dominated the remnants of Park Chung Hee's party and of the old opposition party. Chun rewrote the constitution, making elections somewhat more democratic, but still ensuring effective government control. He promised to resign after a single term ending in 1987. He conducted a revitalization campaign in which thousands of government officials were purged, senior officials were sent to thought camps to have their ideas straightened out, and a massive press campaign was launched to

instill a new sense of vitality and righteousness in the population at large. He took very strong steps to bring the army under effective control and to limit the ability of students and workers to cause trouble. The Defense Security Command monitors the activities and views of army personnel in great detail, making a coup virtually impossible except as a spontaneous reaction to a sudden shock. Workers are no longer allowed to impose union shops, to form unions comprising more than one firm, or to allow the participation of third parties (particularly Christian union organizers) in the organization of unions. Up to 600 clandestine agents were planted on the campus of a single university.

III. Economic Management

South Korea has demonstrated the political will to take painful energy, anti-inflation, and wage decisions in order to make rapid progress in structural adjustment. Nationalism has inhibited promised liberalization of foreign investment rules. The political clout of key ministries, and the desire of political leaders to return political leverage, have defeated proposals for wide-ranging liberalization of the banking system. Early efforts by the Chun government to restructure Korean industry by fiat were misguided and have been abandoned. On balance, government economic policy is rational and decisive.

IV. International Environment

The Chun regime's greatest successes have been in diplomacy. The country's key international problem remains the North Korean military threat, but current South Korean strength, and U.S. support, along with Chinese and Soviet opposition to any North Korean military attack, make war very unlikely. Korean society is one of the world's oldest, most homogeneous, and most nationalistic cultures, and the Park regime was always on the defensive in the face of demands for Korean reunification. President Chun quickly made a series of proposals, including willingness to meet North Korea's leader, Kim Il Sung, in either Seoul or Pyongyang, and acceptance of several key outstanding North Korean proposals. He thereby seized the initiative on a politically vital issue. President Reagan made President Chun the first foreign head of state invited to Washington, thereby consolidating Chun's power. Chun engaged in successful summit meetings in Southeast Asia and recently in Africa. The South Koreans take great pride in Seoul's having been chosen as the site of the 1986 Asian Games and particularly as the site of the 1988 Olympics. Most recently, South Korea and Japan have compromised a major dispute over the amount of aid Japan will give South Korea, and this compromise makes possible the forthcoming visit of Japanese Prime Minister Nakasone to Seoul, an unprecedented symbol of rapprochement between countries which have spent much of their history as enemies.

V. Pressures for Change

Along with economic successes, President Chun has experienced important difficulties. First, there has been a continuing reaction from students against the means by which President Chun achieved and retains power, and by workers against political repression and continuing austerity. Economic

growth, although creditable in the present world environment, remains below the levels needed to absorb additions to the labor force and to ameliorate painful conditions in key sectors. Student demonstrations have been numerous and large, and the government must be constantly concerned that a demonstration might get out of hand, or that security forces might overreact and kill one or more students. Such student deaths would not be tolerated by Korean society. Although wages have once again begun to rise in real terms, and although overt worker demonstrations have been virtually non-existent, there is an undercurrent of strong worker discontent in key industries and key regions, and there have been some instances of sabotage. The province of Kwangju remains a sullen armed camp. The government's greatest medium-term fear is that students and workers might at some point join together.

Second, at the height of his moral revitalization campaign, which involved huge purges that affected influential families, President Chun's regime was shocked by a "kerb scandal" involving a \$1 billion illegal use of funds on the informal financial markets, leading to the collapse of several large firms. The key figures in the scandal were a sister-in-law of the President, an uncle-in-law of the President, and key executives of two major banks. The damage to the government's reputation was severe at the time, but decisive action by the President and his staff, and the conviction and jailing of the involved relatives of the President's wife, have begun to ameliorate the damage.

Third, Chun's government has suffered from a degree of fragmentation uncharacteristic of its predecessor. Partly this is because the economy has become more complex and more difficult to manage from the President's office. Partly this is because the current leadership is less broadly experienced than its predecessors. In economic policy, there are major divisions among the Economic Planning Bureau, the Ministry of Finance, and other key economic institutions. Politically, there has been widespread disillusionment with the Chun regime in the government bureaucracies themselves. Senior officials complain of erratic decision-making on the part of the President. On many crucial political and economic decisions, the President appeared to close Korean observers to be contradicted or eclipsed by three younger generals who held key advisory positions within Blue House: Her Hwa Pyong (nicknamed "the Brilliant General" initially Special Assistant to the President, then Secretary for Political Affairs), Her Sam Su ("the Courageous General," Special Assistant for Justice), and Lee Hak Bong ("the Virtuous General," Senior Secretary for Civil Petition and Intelligence Affairs). The President did not like the image that he was being eclipsed. The Brilliant General and the Courageous General took to bickering interminably with one another. Senior army officers resented the power of these upstarts. And the two may have acted more decisively than President Chun felt necessary on the kerb market scandal. As a result, only Virtuous General remains intact. Brilliant general has been dispatched to the Heritage Foundation in Washington, D.C. Courageous General has been dispatched to Japan. For the time being, this leaves President Chun more conspicuously in total control of decisions than before. It remains to be seen whether the approval of the senior generals for the ouster of these ambitious younger men will outweigh the possible resentment of the younger colleagues of Generals Her and Her.

Finally, the Chun government has appeared to lack a coherent overall political strategy. President Chun has promised a more democratic and more liberal regime, and at least some of his colleagues believe in that commitment. But even believers feel that short-run crises have necessitated practices which go in the opposite direction. The regime is widely perceived as one which snatched power from civilians while offering thin excuses. Controls on students and workers, and on Christian church activities (for instance, denial of permission for any business to advertise in certain Christian publications), is more repressive than ever before. Theoretically, democratization is to be facilitated by strengthening the political parties in connection with National Assembly elections scheduled for 1985, to be followed by a vigorous campaign for someone to succeed Chun Doo Hwan after his term is over in 1987. But the political parties are more emasculated of strong leaders, exciting programs, and institutional coherence than ever before, and as a result party politicians are popularly perceived to be mostly people who cannot succeed in any more productive walk of life. This does not bode well for democratization, and yet further government moves toward Polish practices risk a confrontation with workers.

The banishment to Washington, D.C., of formerly jailed opposition leader Kim Dae Jung in December 1982, and the announcement in January 1983 that hundreds of former political leaders banned by Chun from politics would have their political rights restored, could signal the emergence of a new, more open strategy by Chun. It is too early to tell, and such moves will eventually have to be supplemented by measures to placate labor.

VI. Risks and Opportunities

On balance, the overall situation confirms South Korea's extraordinary institutional strength and its possession of a national political-economic consensus which is broader than in most Third World countries, but in which there are nonetheless real risks as well as great opportunities. The opportunities arise from South Korea's unusual growth and unusual continuity in a world situation where any Third World growth and continuity at all are highly creditable.

The 1988 Olympics offers some singular opportunities for new business and for broad exposure. On the other hand, association with a major 1988 event involves major long-term commitments which might be premature.

Bankers Trust has benefited tremendously from its perception of South Korea's strengths, even in periods of crisis, and from its resultant willingness to support South Korea even in difficult times: e.g., after the oil price rise of 1973 when many others panicked, and in the autumn of 1980, a few months after the Kwangju uprising, when it returned to the syndication markets more rapidly than other institutions.

The principal short-term risk is that another shock like the kerb market scandal, or a problem within the army, or, above all, an incident in which a few demonstrating students are killed, could lead to the forcible replacement of President Chun. In such a situation, by far the most likely outcome would be a quick leadership transition, accompanied by strong continuity of economic

management. (A deep division and confrontation within the army is not completely impossible, but is unlikely under South Korean conditions.) In normal times, such a political blip would go almost unnoticed by the financial markets. However, in a context of pervasive Latin American and African financial collapse, financial markets are extremely jittery and might overreact. This, combined with South Korea's large short-term debt, could cause momentary difficulties. While momentary financial difficulties are an unwanted irritation during a time when there are so many problems elsewhere, the underlying political and economic strengths of the economy give reason for confidence that the long-run costs would be negligible.

More fundamental risks will arise in connection with the National Assembly elections in 1985 and the Presidential election in 1987. At those times, and particularly in 1987, the tension between the frequently stated commitment of the President to a degree of political democratization and the regime's perceived need for increasingly repressive measures, will be tested. Above all, the President's commitment to step down after a single term is completed will be crucial. There will be strong pressure for the opposition parties to be allowed truly to organize and campaign. Concomitantly, there will be renewed demands for trade union organizations which transcend a single firm. In an election period, the expression of political feelings will seem natural and legitimate. If economic times are still hard, worker resentment of poor conditions will come to the fore. If prosperity has returned, then workers will assert themselves with renewed confidence. Confrontation is not inevitable, and in the event of confrontation government victory might once again be swift and decisive. But, conversely, there will be a compelling need for a government strategy which comes to grips in a more coherent fashion with the rising potential to power of six million increasingly educated and skilled workers, abetted by highly articulate academics and clergymen. Whether such a strategy is emerging should be apparent within a year.