Chaebol Investments and Government Policy

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It is argued that one key reason behind Korea's stalling economic growth is the lack of sufficient investments in facilities, especially by the chaebol companies. The government charges the chaebols with under-investing and has put considerable pressure on them to invest more aggressively. Since one main pathological feature of the chaebols has been their propensity to over-invest, this paper examines whether there has been a change in chaebol behavior. Evidence shows that chaebols are not under-investing in facilities. The chaebols are engaging in investments that make business sense, even though these levels of investment may fall short of what the government would like to see. By misreading the true situation, the government may be initiating a complex power game with the chaebols, which will prove to be counter-productive.

Keywords: chaebol investment in facilities, production capacity utilization rates, under-investment, President Roh's chaebol policy, Korean economic reform

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I. INTRODUCTION

Korea has a love-hate relationship with the chaebols. The part of Korea that loves the chaebols does so because along with the government, the chaebols played a crucial role in producing the spectacular economic growth and development during the four decades following the Korean War. These days, the chaebol companies form the bedrock of the Korean economy and there is wide recognition that the nation's international competitiveness in global markets will most likely come from their ranks (see "Mission \$20,000" by Boston Consulting Group and Maeil Kyungje Shinmun). The special government concessions given to Samsung and LG, waiving the ban on building large production facilities in the Seoul area, are manifestations of this belief. Moreover, any feeling toward the chaebols is easily magnified because the livelihood of the average Korean is heavily dependent on them. The 30 largest conglomerates collectively account for nearly half of all sales and over 15% of GDP in value added terms.

Whether true or not, the notion that the future success of the Korean economy is inextricably tied to the success of the chaebols is a bitter pill to swallow. This is because the chaebol system is perceived to contain serious flaws. One of the earliest works that examine the chaebol problem is by Jones and Sakong (1980). Since then, substantial research has gone into understanding the historical pattern of chaebol behavior, (see Chang 2003), while other studies have explored the roots or causes of the chaebol problem (So 1994). The 1997 financial crisis gave chaebol research a new impetus with strong emphasis being placed the subject of corporate governance (see Lee 2003) and restructuring (see Lee 2000 and Ahn 2001).

But what is the 'chaebol problem'? In the narrow sense, the term 'chaebol problem' refers to the excessive concentration of ownership of economic resources, the oligopolistic market structure in which the chaebols thrive, and the process in which chaebols are formed, grow, and develop. A broader interpretation of the chaebol problem will include anti-chaebol sentiment. This study does not deal with the subject of anti-chaebol sentiment per se, but will stick to the narrower definition of the chaebol problem as described by Chang and Park (2000). According to them, the chaebol problem consists of low profitability, high financial leverage, abnormal ownership structure, a peculiar mode of financing, and excessive diversification.

Using data from other countries in different points in time and utilizing multiple measurement criteria for understanding the chaebol features viewed as pathological in nature, Chang and Park provide a refreshing view of the chaebol problem. They conclude that the so-called problems are all basically non-problems. They find that "there is no clear evidence that Korean corporate profitability is exceptionally low by international standards." Similarly, they believe the pre-crisis debt-equity ratio in Korea (between 300% and 350%) to be acceptable and not exceptionally high by international standards. Thus, they do not think that the high debt-equity ratio

should be held responsible for bringing about the financial crisis.

Chang and Park defend the cross-holding structure of the chaebol companies on the grounds that it is a way for chaebols to multiply their funds available for investing "by creating fictitious capital on the basis of which new shares could be issued." On the related topic of high reliance on debt financing while avoiding equity financing, Chang and Park claim that this is only part of the story. As they see it, the Korean chaebols were aggressive fundraisers in the equity market and if debt financing seemed to loom so large, it is because "they found even these large sums raised in the stock market insufficient for the aggressive investment strategy they had adopted." As it turns out, the "octopus tentacles" strategy, or the pursuit of excessive diversification, is also not such a serious problem. Despite the large number of subsidiaries, for most chaebols, two to four core companies generate over 70% of all group sales. Chang and Park believe, therefore, that the chaebols are quite focused.

What, then, is the real chaebol problem? Chang and Park redefine the real chaebol problem to be two things: 1) their strong tendency to over-invest; and 2) the abuse of their ever-growing political power. Perversely, current conventional wisdom believes that one key reason behind Korea's stalling economic growth engine is the lack of sufficient investments in facilities, or under-investment, especially by the chaebol companies. The government has focused on this under-investment theme and has put considerable pressure on the chaebols to invest more aggressively. So far, the chaebols have responded with words and promises only.

The purpose of this study is to assess the government policy pertaining to chaebol investment. President Roh Moo Hyun's government has repeatedly linked Korea's recent poor economic performance to the slowdown in domestic demand. Within domestic demand, facilities investment has become a focal point of government efforts to restore Korea's GDP growth rate back to a respectable level (e.g., in excess of 5%). The government blames chaebols for the weak investment in facilities and consequently the low level of domestic demand.

It is not possible to assert with any precision the exact contribution of chaebol (defined as the 30 largest, for example) investments in total facilities investment. On the other hand, according to Jwa (2002), between 1985 and 1995, the 30 largest chaebols account for 40% to 46% of assets in all industries (excluding financial and insurance industries). This lends credence to the idea that the chaebols play an important role in facilities investment and consequently, government efforts to raise the pace of economic growth has focused on chaebol investment activities. Although it would be highly desirable to make a careful appraisal of the contribution of chaebols to total facilities investment, the present study will follow conventional wisdom on the notion of chaebols playing an important and stable role in determining the level of facilities investment. It should be pointed out that this simplifying assumption allows us to treat facilities investment and chaebol investment as two objects which

move in a highly correlated manner.

The remainder of this paper is organized as follows. In Section 2, we explore some key macroeconomic data and show, contrary to government charges, that the chaebols are not under-investing. Sections 3 and 4 discuss the implications of not under-investing and how this situation affects government policy. In Section 5, we consider the open conflict between the government and chaebols and suggest how the complexity of this conflict should change if the government were to accept that idea that the chaebols are not under-investing. Concluding remarks are given in Section 6.

II. INVESTMENT AND CONVENTIONAL WISDOM IN KOREA

Over-investment has been a longstanding problem in Korea (see for example Jwa 2003). Indeed, so chronic was the problem that over the last three decades, the frequent debates were not so much about "Is there over-capacity?" but rather, "What can we do about it?" Conventional wisdom believed (correctly) in the existence of over-capacity. Today, business is in a prolonged slump, the unemployment rate among youth exceeds 7%, and the pace of economic growth is closer to 4% than the 6% predicted in early 2004 by the government. Producer and consumer sentiments are extremely poor.

It is not difficult to pinpoint the main areas of economic weakness: consumer spending and investment in facilities. Consumer spending took a crippling blow after the spending binge accompanying the mini-economic rebound of 2002. The number of individuals with bad credit rating exceeds 3.7 million, or about 10% of the population above age 15. Furthermore, with household debt in excess of KRW 450 trillion (roughly USD 450 billion), or 60% of GDP, lenders are now trying to reduce their exposure to households. However much Korea would like to see a sharp recovery in consumer spending, short of resorting to some drastic measures (which, incidentally, can never be counted out), the economy is likely to be stuck with this unusually low spending rate for the foreseeable future. The government knows this and is consequently paying greater attention to the other problem area: investment in facilities, or what today's conventional wisdom would call "under-investment."

During the early phase of Korea's economic development, between 1970 and 1986, Korea's investment in facilities averaged 7.4% of GDP. The Korean economy took off in the mid 1980s and facilities investment averaged 12.8% of GDP between 1987 and 1996. The economic recession that followed the financial crisis of 1997 had a major impact on facilities investment. As can be seen in Table 1, there was a heavy drop in facilities investment, with year-over-year growth rate plummeting to -41.1% in 1Q1998, -48.4% in 2Q1998, -45.1% in 3Q1998, and -33.1% in 4Q1998. The fall in investments can be appreciated from a different perspective: facilities investment as a percentage of GDP for these four quarters is very low, ranging between 7.8% and 9.3%.

TABLE 1. GROWTH RATE (%) OF EXPENDITURES OF GDP

	1996			1997			1998			1999									
	1Q	2Q	3Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q				
Expenditure of GDP	7.4	7.2	6.6	6.9	4.9	6.0	5.1	2.8	-5.3	-7.9	8.1	-8.0	5.9	9.7	11.1	10.9			
Final consumption expenditure	7.1	7.2	6.2	7.3	3.9	3.9	3.1	6.1	-11.0	-12.2	10.0	8.3	7.3	9.5	10.9	11.2			
Private	7.1	7.2	5.9	6.8	-0.3	3.9	3.5	10.3	-13.8	-15.5	-13.9	-10.8	8.3	11.1	13.8	13.6			
Household	7.1	7.1	5.9	6.8	-0.9	3.9	3.5	10.0	-14.0	-15.5	-14.1	-10.9	8.5	11.5	13.2	13.8			
Non-profit institutions serving households	6.6	8.3	7.6	7.2	-4.7	3.7	3.0	3.4	-4.5	5.1	-5.6	5.4	1.7	5.2	2.4	2.3			
Government	7.3	7.1	7.4	7.8	5.6	3.8	3.1	6.6	3.0	1.9	2.4	2.1	7.3	3.6	3.2	2.3			
Gross capital formation	9.9	9.4	11.8	10.7	3.5	-1.2	-1.6	-11.8	-39.8	-31.8	35.0	18.1	29.6	25.6	23.7	21.6			
Gross fixed capital formation	7.5	8.3	10.9	9.1	1.0	3.1	-1.2	-7.6	-39.8	-34.4	-25.1	20.1	26.9	26.3	10.2	13.2			
Construction	11.7	5.8	8.0	5.9	-7.9	3.2	2.2	-4.2	-4.4	-9.8	-15.8	16.3	-6.8	-1.7	-2.5	-1.3			
Machinery & equipment	3.2	3.5	13.1	13.0	3.5	7.6	-14.2	-16.2	-31.1	-38.1	-43.1	-33.1	13.6	35.8	-46.9	53.1			
Intangible fixed assets	19.1	15.0	18.3	15.0	20.9	14.6	3.3	-3.0	3.1	9.3	6.5	8.9	18.3	32.8	4.3	37.2			
Changes in inventories	-49.2	126.7	-17.6	55.7	-1538.9	691.3	132.3	-91.5	-1895.7	166.5	131.1	-67.0	-75.7	29.0	36.8	354.7			
Exports of goods & services	19.6	9.8	5.8	14.3	11.0	25.9	26.7	23.0	25.6	12.0	8.6	7.3	5.6	13.5	13.1	17.5			
Gross Imports of goods & services	15.3	13.0	11.1	12.7	8.1	1.3	3.5	-6.5	-26.9	23.1	25.3	-5.4	26.3	27.1	31.0	26.9			
Statistical discrepancy	-3801.6	-191.6	133.9	277.8	-1732.2	171.9	1.3	127.6	-1645.3	-147.7	-8.9	-337.9	-291.7	232.5	171.2	-204.1			
	2000			2001			2002			2003			2004						
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q			
Expenditure of GDP	13.1	9.4	8.3	4.3	7.5	8.7	3.4	1.6	6.5	7.1	6.8	7.5	5.1	2.2	2.4	3.9	5.3	5.5	4.6
Final consumption expenditure	10.3	8.7	5.8	4.0	2.2	4.1	3.1	3.8	5.4	8.5	7.1	5.5	3.9	-0.8	-3.9	1.1	-0.6	0.3	-0.1
Private	11.9	10.2	7.7	1.3	2.0	3.4	5.6	7.6	9.8	10.7	7.8	5.5	6.3	1.8	-1.9	-2.2	-1.1	0.6	0.8
Household	11.1	10.4	7.7	4.5	2.0	3.4	5.6	7.2	9.3	10.8	7.7	5.5	6.2	1.5	-1.9	-2.3	-1.3	0.5	-0.8
Non-profit institutions serving households	2.8	1.3	3.2	0.6	4.1	4.3	4.4	3.5	7.5	6.5	9.6	5.2	3.7	1.6	0.8	3.8	1.1	3.2	1.1
Government	5.8	2.1	1.7	2.7	3.7	3.3	6.4	6.2	7.6	7.3	5.3	4.2	4.0	3.7	3.3	4.3	2.8	3.3	3.0
Gross capital formation	27.9	10.3	13.8	-0.9	-3.7	-4.3	0.1	6.2	4.2	9.1	7.6	3.0	8.2	-0.5	1.2	1.0	-0.3	5.4	6.3
Gross fixed capital formation	24.3	14.8	10.8	3.3	-3.7	-3.5	0.3	6.2	1.1	7.3	2.4	9.1	4.6	3.1	1.6	1.6	1.8	4.5	3.0
Construction	4.7	-3.1	-0.3	0.2	1.0	6.8	9.3	10.7	11.0	6.0	2.4	8.1	8.0	7.3	3.9	1.4	-1.1	3.8	1.5
Machinery & equipment	61.9	43.1	31.1	8.3	9.1	10.5	7.7	-1.3	3.8	8.0	3.1	9.6	1.9	0.6	-3.0	-2.4	-0.3	6.2	6.7
Intangible fixed assets	56.3	22.9	5.7	13.1	7.5	6.3	2.2	9.1	13.6	15.9	3.6	13.1	2.3	-3.8	10.2	3.4	-3.3	0.6	3.1
Changes in inventories	-17.0	-3816.3	-30.0	-32.3	6.0	26.5	-1.9	5.7	149.1	-33.1	-128.1	-64.7	-56.6	135.2	337.6	87.2	103.3	-23.9	-133.0
Exports of goods & services	29.7	19.7	20.2	13.3	3.8	-2.3	-1.7	-3.4	1.1	12.5	16.2	23.5	15.9	8.1	16.9	35.1	26.9	27.7	17.6
Gross Imports of goods & services	31.4	20.6	23.1	8.4	-2.6	8.4	-5.7	-0.6	4.7	17.0	19.1	19.1	14.2	3.2	7.7	11.7	11.8	23.6	12.9
Statistical discrepancy	87.1	-20.9	-6.5	-16.3	56.6	35.9	159.3	20.9	55.8	29.8	68.2	227.3	23.8	-357.0	79.1	-97.9	-331.9	-58.9	-87.7

SOURCE: KOSIS

TABLE 2. FACILITIES INVESTMENT AS % OF GDP

	1995				1996				1997				1998				1999			
	3Q	2Q	1Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q
GDP	63.9	62.9	66.8	64.7	63.7	62.9	66.5	61.1	65.1	65.8	66.7	62.1	57.5	62.2	64.1	60.0	58.8	62.9	61.0	61.2
IFY	34.9	30.2	30.8	39.0	31.9	30.7	42.9	39.8	33.6	38.6	38.7	35.8	28.1	31.7	31.3	30.2	26.2	31.6	31.2	30.8
Mach & equip/Y	16.0	15.4	15.6	14.2	15.2	15.2	16.7	15.2	15.0	14.7	15.5	13.9	9.3	8.2	8.1	7.8	9.5	10.2	10.8	10.8
	2000				2001				2002				2003				2004			
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q
GDP	68.7	68.3	68.7	61.3	67.3	63.6	64.9	62.8	62.0	61.5	65.4	61.8	62.1	61.3	63.0	48.7	53.5	49.3	50.3	
IFY	38.6	33.2	31.9	30.6	36.6	30.9	30.7	31.9	26.9	30.9	29.9	31.5	37.1	34.4	29.5	31.4	26.2	31.1	29.1	
Mach & equip/Y	13.9	13.3	13.1	11.1	12.2	13.5	10.8	10.6	11.8	11.6	11.1	10.8	11.6	11.3	10.3	10.1	11.0	11.3	10.5	

One remarkable Korean achievement, for which President Kim Dae Jung and his government like to take credit, is the speed of economic recovery from the financial crisis. It is hard to put an exact date on when the financial crisis "ended," but by the 3Q1999, the GDP growth rate was up to 11.1% (albeit off a low base the previous year) and facilities investment as a percentage of GDP was back up into double digits at 10.8%. Incidentally, facilities investment as a percentage of GDP reached a high of 13.9% in 1Q2000, and has not dropped below 10% since 2Q1999.

FIGURE 1. FACILITIES INVESTMENT, 1970~2004

SOURCE: KOSIS

Based on the data on facilities investment as a percentage of GDP since 3Q1999, it is difficult to conclude that Korea is suffering from under-investment. To be sure, the numbers consistently are a tad (one or two percentage points) lower than the 12.8% average between 1987 and 1996. However, it is worth keeping in mind that 12.8% is a troublesome benchmark because this number comes from a period

in time when the Korean economy was over-investing. Viewed in another way, investment in facilities as a percentage of GDP for the 20 years leading up to the financial crisis averaged 11.4%. Figure 1 graphs actual facilities investment as a percentage of GDP and compares this against the 20-year benchmark average of 11.4%.

Consider some effects of investing in facilities. If for some reason there is over-investment, then the phenomenon should show up as excessive excess production capacity. In other words, since some slack in the production capacity is desirable or optimal, over-investment will enlarge the size of the slackness. The best way to discern excessiveness is to observe changes in the facilities operation utilization rates. Over-investment should result in lower capacity utilization rates. Conversely, if there is under-investment, then one would expect to observe higher capacity utilization rates.

Figure 2 depicts production capacity utilization rates since 1980. Between 1987 and 1996, the capacity utilization rate averaged 79.4%, ranging from 77.0% to 82.0%. Aggregate demand fell because of the financial crisis and the capacity utilization rate fell sharply to 68.1% in 1998. The ensuing economic recovery was accompanied by a rebound in the utilization rate; the utilization rate measured 76.5% in 1999, 78.6% in 2000, 75.3% in 2001, 78.4% in 2002, and 78.3% in 2003. All of these numbers are below the 79.4% average recorded during the over-investment years (between 1987 and 1996). To be sure, most recently since October 2003, the utilization rate has moved above the 79.4% level, going to a high of 83.4% in February 2004. However, the rate has dropped sharply since then and has hovered between 78.8% and 81.8%.

The data from production capacity utilization rates therefore appear to support the assertion that the recent levels of facilities investment in Korea are not excessively low and should not be labeled as "under-investment."

FIGURE 2. PRODUCTION CAPACITY UTILIZATION (1981-2005)

SOURCE: KOSIS

III. THE PROBLEM OF NOT UNDER-INVESTING

Followers of the conventional wisdom will be surprised to learn that Korea is not under-investing. This is because local media has given ample news coverage of the economic slowdown together with the slowdown in investments and consumer spending. On top of this, President Roh Moo Hyun and his senior policy makers have added to the sense of drama and desperation by publicly asking the chaebols to increase investments.

So what is really going on? Under-investing takes place when the level of investment falls below some optimal amount. This paper has argued that the investment behavior in Korea in recent years does not deviate sufficiently far from the investments seen during the go-go days of 1987 to 1996, when the chaebols were prone to over-invest. It may be true that the chaebols are not investing as aggressively as in the years leading up to the financial crisis in 1997, but this does not mean that the chaebols are now under-investing.

If the Korean economy is not under-investing, then the investment behavior must be either optimal or excessive. If this is the true situation, then some important implications may be drawn.

First, economic recovery will be farther away in the future than otherwise. The economy is in a vicious circle: slower economic growth lowers capacity utilization rates, which then lowers the need to invest, which in turn contributes toward slowing economic growth further. Second, the government should re-consider what motivates the chaebols. In particular, the chaebols are not being uncooperative in an attempt to threaten the new government. The chaebols are not playing a complicated game with the government, but are simply investing at levels they believe are suitable given the current market conditions and future outlook for the economy.

Third, attempts by the government to artificially raise investment may boost economic growth temporarily, but will eventually lower growth over the long term. Left alone, the tendency should be for the economy to adjust the investment levels to remove excess capacity. Government interference will exacerbate the problem of excess capacity, rendering the government action counter-productive. Fourth, the government should revisit its chaebol policy.

IV. POLICY IMPLICATIONS

The government is clearly not happy with the current low levels of investment. Unfortunately, government displeasure does not justify calling these levels of investment "under-investing." On the contrary, it is possible to conjecture that the decision-makers in charge of investments are responding optimally to poor economic conditions and a bleak future outlook. It should also be noted that past investment decisions affect today's production capacity, as well as capacity utilization.

Frustrated with the continuing stagnation in investments, the government shows signs of wanting to resort to strong-arm tactics to force the chaebols into investing more aggressively. (For example, before President Roh hosted a dinner hosted at the Blue House on May 25, 2004, the chaebol invitees all announced plans to increase 2004 investments by roughly 30%, collectively.) Upon further reflection, however, it is easy to see that pushing the chaebols more deeply into over-investment behavior is a bad idea and may be dangerous, since it may add to the speed and duration of an economic downturn in the future.

In general, investment decisions today affect future production capacity. When the investment cycle has run its proper course downward, production capacity will once again be in short supply and the economy will embark on the upward sloping part of the investment cycle. This happens quite naturally, without active government involvement in more mature economies. In the case of Korea, the difficult lessons about natural investment cycles and the required optimal investment decisions are just being learned, having just gone through a painful financial crisis. The government should realize that the chaebols are extracting the right market signals, probably for the first time collectively, and making well-informed investment decisions. Consequently, a better course of action will be to wait patiently for the economy to go through the investment cycle.

It is conceivable that an activist economic policymaker may want to intervene in the investment cycle by encouraging under-investing as a way to shorten the time taken to reach the bottom of the cycle. This seems all right theoretically, but to engineer such a forced economic slowdown may not be practical politically. Moreover, since the Korean economy has little or no experience with aggregate under-investment, the policymakers will be operating in uncharted territory.

The above arguments should not be misconstrued. In particular, the government should not think that it must not be pro-active on matters concerning investments. Since investment decisions today are a function of the economic condition and the outlook for the future, the government may attempt to change market conditions (e.g., interest rates, government spending) and outlook (e.g., FTAs, improvement in economic and systemic infrastructure).

Finally, the government will do well to avoid being impatient. Contrary to conventional wisdom, the economy is not under-investing. This means that economic recovery is farther away in the future than had the economy been under-investing.

V. PRESIDENT ROH'S CHAEBOL POLICY

In the 2002 presidential race, Mr. Roh Moo Hyun ran an effective election campaign that emphasized reform and transparency. As President, Mr. Roh has thrown his political weight behind efforts to reform Korean politics. It is still too early to say whether political reforms are headed in the right direction and go far enough. What

President Roh has done, however, is set the wheels of political reform in motion.

How about the wheels of economic reform? Sadly, these appear to be stuck. When President Roh first stepped into the Blue House in February 2002, he promised to carry out reforms throughout the course of his five-year presidency. It comes as a surprise, therefore, to see so little action on the economic front.

On reflection, there were some good opportunities. The SK Global scandal, the credit card crunch, corporate slush funds for politicians and unruly labor disputes, are just a few of the opportunities that came knocking, but which the government failed to exploit. The President also briefly flirted with two mini visions, the "North East Asian Hub" and "20,000 dollar income," but quickly put them in the backburner. On the policy front, frequent surveys show emphatically that no economic policy has managed to impress the general public.

As a result, the economy is in an anticipatory mode. Each day without action only heightens the sense of anticipation. This, of course, is bad and has unpleasant economic consequences. Take for example what happens with investments. The cycle of 'no action, greater anticipation' raises the level of uncertainty, which in turn, negatively affects investment decisions.

President Roh and his government should be more transparent on the question of economic reforms. If there is some new vision for the economy, then this vision should be carefully spelled out. Similarly, if there is a plan for chaebol reform, then those plans should be circulated. This is certainly consistent with the earlier Presidential promise of transparency.

What if there is no new vision for the economy and no plan for chaebol reform? Odd as this question may sound, it may not be that far removed from the truth. And if there is no vision and no plan at this time, this fact should be made known. Other than suffer some minor embarrassment for not being fully prepared, the damage would be negligible. The payoff, on the other hand, will be the removal of some fundamental uncertainty hanging over the economy.

VI. CONCLUDING REMARKS

Korea today is at an important crossroads. After three decades of robust economic growth, Korea's growth engine appears to be moving somewhat sluggishly. Confidence is in short supply and many economists believe that Korea is in a crisis.

Local commentators find much reason to form a pessimistic economic outlook. These include, among other things, increasing competition from China, decreasing aggregate demand, rising inflation, and declining long run potential GDP growth rate. Behind these concerns, however, lies a more fundamental problem. The government-chaebol partnership, long thought to have been a crucial element of Korea's spectacular economic growth, appears to be in a state of flux.

The government is unhappy with the chaebols for not investing more aggressively.

They have asked repeatedly for greater "cooperation," but thus far, the chaebols have only paid some lip service and have taken no discernable action. On the flip side, the chaebols are also unhappy with the government. They feel that the government is coercing them into making additional investments whose business merits are questionable. Having experienced the financial crisis, each chaebol knows that to over-invest is dangerous and that any business failure will be its responsibility.

Conventional wisdom is on the side of the government and believes that Korea is under-investing in facilities. This paper has argued that Korea is not under-investing in facilities and that the government should not misread or misrepresent the true situation. The chaebols are probably engaging in investments that make business sense. And even though these levels of investment may fall short of what the government would like to see, the government should not interpret their behavior as threatening or challenging.

A complex power game between the government and the chaebols could well be counterproductive. In some respects, the game is already tending toward an unhappy equilibrium because of the fundamental uncertainty brought about by a lack of economic vision from the new President and his government. There is no question that the chaebols fear and anticipate some sort of government backlash against their economic power. If the government has a coherent chaebol policy, it should be released the public sooner rather than later. On the other hand, if there is no such chaebol policy, then that fact should also be made known to the public. If nothing else, at least this admission will clear some bad air.

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