A COMPARATIVE STUDY OF

EAST ASIAN CAPITALISM

EDITED BY HONG YUNG LEE

RESEARCH PAPERS AND POLICY STUDIES 46

Notes to this edition

This is an electronic edition of the printed book. Minor corrections may have been made within the text; new information and any errata appear on the current page only.

Research Papers and Policy Studies 46
A Comparative Study of East Asian Capitalism
Hong Yung Lee, editor

ISBN-13: 978-1-55729-167-7 (electronic)
ISBN-13: 978-1-55729-108-0 (print)
ISBN-10: 1-55729-108-X (print)

Please visit the IEAS Publications website at
http://ieas.berkeley.edu/publications/
for more information and to see our catalogue.

Send correspondence and manuscripts to

Katherine Lawn Chouta, Managing Editor
Institute of East Asian Studies
1995 University Avenue, Suite 510H
Berkeley, CA 94720-2318 USA
ieaseditor@berkeley.edu

Institute *of* East Asian Studies
University of California, Berkeley

May 2015

RESEARCH PAPERS AND POLICY STUDIES 46

A Comparative Study of East Asian Capitalism

Edited by
Hong Yung Lee

Institute of East Asian Studies
University of California, Berkeley

A publication of the Institute of East Asian Studies, University of California, Berkeley. Although the institute is responsible for the selection and acceptance of manuscripts in this series, responsibility for the opinions expressed and for the accuracy of statements rests with their authors.

The Research Papers and Policy Studies series is one of several publication series sponsored by the Institute of East Asian Studies in conjunction with its constituent units. The others include the China Research Monograph series, the Japan Research Monograph series, and the Korea Research Monograph series.

Send correspondence and manuscripts to

Katherine Lawn Chouta, Managing Editor
Institute of East Asian Studies
2223 Fulton Street, 6th Floor
Berkeley, CA 94720-2318
ieaseditor@berkeley.edu

Library of Congress Cataloging-in-Publication Data

A comparative study of East Asian capitalism / edited by Hong Yung Lee.
pages cm. -- (Research papers and policy studies ; 46)
Includes bibliographical references.
ISBN-13: 978-1-55729-108-0 (alk. paper)
ISBN-10: 1-55729-108-X (alk. paper)
1. Capitalism--China. 2. Capitalism--Japan. 3. Capitalism--Korea (South) 4. China--Economic policy--2000- 5. Japan--Economic policy--1989- 6. Korea (South)--Economic policy--1988- I. Lee, Hong Yung, 1939-
HB501.C713 2013
330.12′2095--dc23
2013039896

This book is the result of a project of intellectual cooperation and collaboration between Yonsei University and the University of California, Berkeley. The editor gratefully acknowledges financial support received from Yonsei, Berkeley, and the Korea Foundation for Advanced Studies.

Cover design by Spoon+Fork.

Contents

Contributors

Lowell Dittmer, Professor, University of California, Berkeley

Fengxia Jiang, Assistant Professor, Beijing Foreign Studies University

Myung-koo Kang, Assistant Professor, Baruch College, The City University of New York

Joongi Kim, Professor, Law School of Yonsei University

Yong-Hak Kim, Professor, Yonsei University

Yong-min Kim, Professor, College of Business Administration, Kookmin University

Hong Yung Lee, Professor, University of California, Berkeley

Seungjoo Lee, Professor, Chungang University

Kun-Chin Lin, Lecturer, Department of Politics and International Studies, University of Cambridge

Pingqing Liu, Professor, School of Management and Economics, Beijing Institute of Technology

Hideaki Miyajima, Professor, Graduate School of Commerce, Waseda University

Sang-Young Rhyu, Professor of Yonsei University

Junxi Shi, Ph.D. Candidate, Beijing Institute of Technology

Yul Sohn, Professor, Yonsei University

Ji-Whan Yun, Assistant Professor, Ewha Womans University

ONE

Précis

HONG YUNG LEE

This book represents an initial attempt to compare China, Japan, and South Korea (hereafter "Korea"), three close geographical and cultural neighbors whose developmental trajectories, though divergent in the past, have been moving more recently toward convergence. Over the years, enquiries into the economic development of these three countries have mostly adhered to old patterns of scholarship whereby Japan is studied along with other Western liberal economies, China is considered in the context of communism, and Korea is seen as a developing state. Most existing literature on comparative East Asian economic development has been based on the case of Japan, which has then been applied to Korea, but is not yet considered applicable to China. As such, any truly comparative study of this region will require both a new conceptual framework of East Asia that is fully applicable to all three countries, and new insights about the driving forces behind economic development in each country. We would even go so far as to argue that no economic theory can claim to be valid without explaining or at least being able to accommodate some account of the extraordinary economic success of China, Korea, and Japan over the past fifty years.

To compare the development experiences of these countries, this edited volume examines similar institutions in similar functional areas within the three countries. While the elements being compared in each chapter may vary, we hope that this book as a whole will demonstrate the intellectual utility of a broad comparative study of East Asian economic development. Towards this end, several of the chapters included here are explicitly comparative. Since Japan and Korea share many similar traditions and systems, three of the chapters—chapters 2, 3, and 5—look at these two cases side by side. Other chapters are country-specific but still provide a comparative perspective when read in conjunction with the cases of other countries. If this volume succeeds in alerting scholars to the urgent need for a comprehensive theory that can cover the remarkable economic performances of these countries, it will have served its purpose.

Organization of the Book

The papers in this volume are arranged into sections according to three major areas of inquiry. Part I includes two chapters, this précis and a paper titled "Convergence and Divergence: Three Different Paths toward Modernization in East Asia" that serves as an introduction to this volume. In this section, we make an argument for the necessity and urgency of this book by briefly comparing the record of economic growth for each of these three countries, then explaining the evolution of scholarship about East Asia's economic development up to now. "Convergences and Divergences" offers a bird's-eye view of the turbulent paths to economic development followed by China, Korea, and Japan from the middle of the nineteenth century, as well as their conflict-ridden interactions with one another over the past hundred years. After reviewing the different approaches that have thus far been utilized to explain East Asian economic development, the chapter concludes by arguing for the need for a comparative study of institutions. With China's recent economic reforms, all three countries in the region can be said to be following the path pioneered by Japan, which combines the conscious decision-making processes of the state with the spontaneous decision-making processes of the market. Yet functional and operational differences (divergences) continue to exist between similar economic institutions even though they are modeled after the same sources (convergences). The authors argue that the concept of "institutional templates"—institution-building tendencies shaped by each country's cultural traditions and modern experiences—is key to understanding these differences. Following this introduction, part II examines the specific question of how two of the most important elements in economic growth—capital and labor—have been managed by these three countries, and, in particular, by their states. Part II begins by addressing the issue of capital—specifically, non-performing loans (NPLs). The third chapter, "Government Intervention for Resolving Non-Performing Loans in Japan and South Korea, 1998–2006," presents Myung-koo Kang's comparative study of how Japan and Korea dealt with the problem of NPLs after the 1997–1998 Asian financial crisis. Although Japan and Korea faced similar challenges subsequent to the financial crisis—namely, the globalization of their financial markets, and the active intervention by the state into the operation of financial institutions such as banks—the process, sequence, and speed of reforms carried out by both countries differed significantly. Whereas the Japanese government injected public funds into the economy in intermittent and indecisive ways, the Korean government took early and decisive action to recapitalize failing banks by utilizing asset management corporations

TWO

Convergence and Divergence

Three Paths toward Modernization in East Asia

HONG YUNG LEE

Given the remarkable economic achievements of China, South Korea (hereafter "Korea"), and Japan over the past fifty years, it is difficult to imagine how any account of economic development could be considered complete without a comparative understanding of the rapid, and in some respects unprecedented, rise of these three countries. Close neighbors both geographically and in terms of historical interactions, China, Korea, and Japan all began the process of modernization at about the same starting point—i.e., with roughly similar cultural roots and at similar levels of development. However, their economic performances have diverged over the last century, with each country following a slightly different trajectory to reach where it is today.[1]

The extent to which the economic fortunes of these three countries have fluctuated over the past century and a half becomes apparent when one compares the changing size of their collective share of the world economy in the years since the West came into contact with the East. According to figure 2.1, which is based on secondary literature and historical data, the combined share of the world economy held by China, Japan, and Korea in 1820 totaled about 36.72%, roughly commensurate to their combined share of the world's population. By the middle of the 1950s, East Asia's share of the world economy had drastically declined, falling to a mere 7.85%. This drastic decrease was due largely to China's rapidly shrinking economy. Offsetting that decline, an incremental rise in Japan's individual share of the world's wealth in the 1950s was followed by more rapid growth in that country, and then by the economic rise of South Korea.

[1] For the traditional regional system of international politics, see Cohen (2000).

THREE

Government Intervention for Resolving Non-Performing Loans in Japan and South Korea, 1998–2006

MYUNG-KOO KANG

In the course of industrialization, both Japan and South Korea (hereafter "Korea") have consolidated a similar bank-centered financial system for economic development. A bank-centered financial system was consolidated in Japan during the War Economy period (1937–1945) (Noguchi 2002), and Korea's creation of a bank-centered modern financial system was shaped during the period of Japanese colonial occupation (1910–1945) (see Cole and Park 1983; Kim 1994; T. H. Chung 2000; B. U. Chung 2000, 2004). The colonial imprint remained even after the liberation from colonial rule during Korea's economic take-off in the early 1960s and 1970s. Learning from the experiences of postwar Japan, the Korean government established specialized development banks to mobilize scarce domestic capital and to allocate it into select firms, *chaebols*, in order to develop strategic industries for exports (Vittas and Wang 1991; Cargill 1998; Ikeo, Hwang, and Takao 2001). The Korean government also emulated Japan's "main bank" system, in which banks play a pivotal role in mediating bank-firm relations based on long-term business relations (Aoki and Patrick 1995), as well as its policy financing practices (Cho and Kim 1997; Development Bank of Japan 1994; Cho and Hellmann 1993). While an attempt to emulate the Japanese main bank system, the Korean government's introduction in the late 1970s of a "principal transactions bank" also was intended to increase government control over *chaebols*, and, more specifically, to prevent *chaebols* from over-borrowing from particular banks (Nam and Kim 1994). Until the 1990s, no banks had failed in either country.

In the late 1990s, both Japan and Korea were confronted with a similar problem in the banking sector: growing numbers of Non-Performing

FOUR

Financial Reform in China

The Chinese Style of Marketization

HONG YUNG LEE

An efficient financial system is a prerequisite for economic growth in any society, because of the critical function it performs in mobilizing and allocating capital to the most promising and productive sector of an economy. The developmental states of East Asia have relied heavily on their ability to control financial systems in order to direct investments toward those sectors considered strategically important for economic growth (Ishi 2001).[1] However, state intervention into resource allocation frequently undermines the healthy development of financial institutions. This structural weakness eventually resulted in the Asian financial crisis, which in turn led to serious questions about the viability of the East Asian model of economic development. Viewed in this context, the unusually rapid economic growth that took place in China despite its significantly underdeveloped financial institutions has been both puzzling and surprising.

China's reform of its financial sector started much later than its reform of other sectors of the economy (e.g., industry, factory management, rural reforms, etc.), and it proceeded slowly and gradually. Only after 1997 did Chinese leaders, alarmed by the Asian financial crisis, begin the process of restructuring financial institutions. China began tackling the problem of non-performing loans (NPLs) in 1998, but this process of restructuring and reform has taken place incrementally. As a result, it has seemed to some as if the regime was playing a board game rather than tackling difficult questions head on. Many observers have warned that NPLs will remain an obstacle to continued economic growth, particularly given that China's financial sector is now open to the outside world as a consequence of having joined the World Trade Organization (WTO).

---

[1] For South Korea (hereafter "Korea"), see Woo (1991); for the Japanese case, see Ishi (2001).

FIVE

The Double Movement and New Labor Market Regulations in Korea, Japan, and Taiwan

JI-WHAN YUN

Until the late 1990s, the labor markets of Japan and South Korea (hereafter "Korea") were applauded for greatly contributing to economic growth and for achieving low unemployment (Quibria 2002; You 1998). The most qualified workers were mobilized toward the goal of production increases through a particular incentive and work ethic. Economic expansion and increasing productivity in East Asian economies generated wider wage-earning opportunities. Since the late 1990s, however, labor markets have become the special targets for unprecedented reform projects. In the process, the Japanese and Korean governments have extended reforms into similar policy areas, including liberalizing employment protection regulations, innovating social insurance programs, and developing job creation measures.

These recent labor market reforms raise the question of how to best analyze these countries' efforts toward new labor market regulations. One strand of argument is neoliberal, focusing on an increasing effect of labor market flexibility. The advisors of the International Monetary Fund (IMF) have claimed that East Asia's single best means of reform would be the "reduction of the protection given to regular workers" without any "anti-discrimination measures against non-regular workers" (IMF 2004). The IMF recognizes the necessity of public welfare programs as a functional response to growing labor market uncertainty, yet asserts the programs must be designed to serve only as a contingency mechanism. Michel Camdessus (1997), former IMF managing director, argued before a conference in Bangkok that East Asian countries have to "encourage [labor market] mobility," "keep labor costs in line with labor productivity," and "establish simpler, more transparent regulatory systems that are equitably

SIX

Moving toward a Hybrid System in Japan

The Case of Corporate Governance Reform

HIDEAKI MIYAJIMA AND YUL SOHN

Whereas the once-popular "Anglo-American" shareholder model of corporate governance has been challenged in the midst of the global financial crisis, an increasing number of studies show that changes in corporate governance systems demonstrate path dependence, forcing the existing system to persist (Bebchuk and Row 2004; Schmidt and Spindler 2004).[1] In Japan, changes are path-dependent by nature, but no single clear pattern has emerged with regard to the future of its model. A recent analysis by Jackson and Miyajima (2007, 37–38) describes the multiple forms of corporate governance mechanisms that coexist within the Japanese economy: a traditional "J-type" (shorthand for Japanese-type) that retains the old relational patterns coexists with hybrid types that mix the old relational

This work was financially supported by the Asia Research Fund and JSPS KAKENHI (19203017)

[1] Corporate governance is often defined narrowly in terms of the agency problems between owners and managers within a firm. In contrast with this definition, this chapter takes a broader view, conceptualizing it as involving relations among multiple stakeholders, such as shareholders, managers, employees, unions, banks, government bureaucrats, and political leaders. Further, corporate governance is viewed as embedded within various rules and norms that shape how these stakeholders interact in corporate decision making. Here, corporate governance is about power and responsibility within institutional contexts, such as the financial system, corporate law, industrial relations, or the regime of political economy where the elements of politics are in play (Gourevitch and Shinn 2005, 1–2). Patterns in corporate governance substantially vary with the broader institutional structures of a given capitalist system. In this sense, Japanese corporate governance lies at the core of the Japanese model. Much of what has happened is driven by it (Aoki 2001; Dore 1997, 2000).

SEVEN

Corporate Governance Reform in Korea in the Post–Asian Financial Crisis Era

JOONGI KIM

Following the 1997 Asian financial crisis, South Korea (hereafter, "Korea") engaged in an overhaul of its corporate governance framework. Enhancement of transparency and accountability of corporations and its managers and controller shareholders through changes in the legal and regulatory infrastructure became a priority. According to a corporate governance infrastructure that began to emerge for the first time, which even included the early signs of a corporate control market, directors, shareholders, stakeholders, auditors, and creditors started to carry out their respective functions. The contours of an elementary framework of internal and external corporate governance and market-oriented discipline gradually developed. In the process, the economy rebounded and market confidence in companies was restored. Through the reforms in the post-crisis period, Korean companies appeared ready to achieve a position where they could be considered to have reached advanced levels of corporate governance according to international standards.

After the comprehensive legal and regulatory amendments, however, scandals and cases of malfeasance reemerged to engulf leading conglomerates and undercut confidence in corporate Korea (*Economist* 2012). The credibility of substantive corporate governance progress was questioned once more. The persistence of problems demonstrated that, despite the reforms, serious structural problems remained. Many controlling shareholders continued to engage in self-dealing, related-party transactions, tax evasion, and other forms of unlawful behavior contrary to the interests of the company and shareholders at large. Notwithstanding overall economic achievements, analysts rated the corporate governance of Korean companies behind others in Asia. Leading corporate governance indices on average placed the transparency and accountability of Korean corporates below companies from emerging markets such as Malaysia and

EIGHT

The Evolutionary Path of Corporate Governance in China

The Interdependent Model of State-Owned Enterprises and Private Enterprises

PINGQING LIU, JUNXI SHI, AND FENGXIA JIANG

China has been undergoing a great transition, as has its governance, since the late 1970s, and many researchers of economics, political science, and other disciplines have studied the transition from corporate governance to public governance. Certain economists initially introduced the term "governance" in the same manner as it is used in foreign literature, such as "corporate governance" or "corporate governance structure," which has since then been widely used in the discussion of corporate restructuring and enterprise reform (Wu 1994; Qian 1995; Zhang 1997; Yang 1997; Li 2002). Subsequently, the concept "governance" was used in public administration studies by political scientists and other scholars (Yu 2002; Xu 2002). However, most economists in China have focused on relationships among property rights, capital markets, and corporate governance, and have paid little attention to relevant political factors. This contribution seeks to redress this absence by focusing on the political factors related to corporate governance.[1]

While the clarity and definition of property rights are prerequisites for an effective governance structure, they do not automatically lead to effective and efficient corporate governance. Property rights, which are not just defined in laws and regulations, can be implemented effectively in the political system, social norms, and cultural practices. As Andrei Shleifer and Robert W. Vishny (1997) point out, "In the corporate governance

[1] This work was funded by the National Natural Science Foundation of China (70503003 and 70872011).

NINE

Multiple Institutional Templates for Corporate China

The Evolution of Industrial Networks during Marketization

LOWELL DITTMER AND KUN-CHIN LIN

Though of course each modernizing nation-state is distinctive, the East Asian developmental experience, as Hong Yung Lee (2005) has pointed out, inherits a similar traditional cultural legacy and shares a number of broadly analogous socioeconomic patterns. These include a focus on the collective (variously defined) rather than the individual as the primary unit of accounting and identity, a high degree of pragmatic flexibility as to specific means combined with a disciplined and concerted focus on long-term developmental objectives, and high respect for authority and orthodox learning combined with considerable informality in its interpretation of particular problems (i.e., a situation ethics). Within this broad pattern there are distinctive national experiences, such as the Chinese moralistic suppression of informal groups as "factions" vs. the much greater Japanese (and Taiwanese) tolerance for factional politicking, the mainly kinship-based Chinese definition of the primary unit vs. the South Korean (hereafter "Korean") territory-based definition or the Japanese function-based definition; the greater Chinese tolerance for collegial authority and familial fissiparousness vs. the Japanese emphasis on primogeniture and patrilineality vs. the Korean intermediate position.

This chapter attempts to analyze the People's Republic of China (PRC) pattern or "institutional template" of political-economic-cultural development during the period of "reform and opening to the outside world" since the Third Plenum of the Eleventh Party Congress in December 1978, during which China quadrupled its Gross Domestic Product and in three decades became one of the world's leading economic powers. Although

TEN

The Changing Face of Network Capitalism in Korea

A Study of the Corporate Board of Directors' Network

YONG-HAK KIM AND YONG-MIN KIM

The concept of network capitalism was created to capture the unique characteristics of East Asian markets, which are quite different from those found in advanced capitalism. Scholars, however, have used the term in various ways to focus on different aspects of the East Asian market (Biggart and Hamilton 1992; Greenhalgh 1988; Hamilton 1998). Some used the term to describe the state-business relationship in which the state functions like the headquarters of an M-form, an organizational structure by which a firm is separated into several semiautonomous units controlled by financial targets from the headquarters (Evans 1995). They focused on how the state manages and regulates private firms embedded in a "political-bureaucratic-business" nexus, which are routinely mobilized for more effective state-policy implementation (Moon and Prasad 1994). Others focused on the institutional linkages among firms as found in the network of Japanese *keiretsu*, a type of business group with interlocking business relationships and shareholdings among member firms (Gerlach, Lincoln, and Takahashi 1992), or Korean *chaebols*, business groups controlled by an owner family who has almost complete control over all firms within the group (Bae, Kang, and Kim 2002). Unlike the market in the West, long-term, durable, contract relationships based on high trust exists among firms (Dore 1992; Gerlach 1992; Gerlach, Lincoln, and Takahashi 1992; Granovetter 1994, Macaulay 1963). Relations among business and

This chapter is reprinted from the authors' paper published in the *Korean Journal of Sociology* 42, no. 8 (2008): 1–26.

ELEVEN

The Political Economy of Informal Networks in Japan and South Korea

Amakudari *vs. Parachute Appointment*

SEUNGJOO LEE AND SANG-YOUNG RHYU

Informal networks between public and private sector elites in East Asia have been perceived as one of the defining features of East Asian capitalism, attracting a constant stream of attention from various fields of social sciences (Dore 1986; Pempel 1998; Gerlach 1997; Dittmer, Fukui, and Lee 2000; Colignon and Usui 2003). In the cases of high-growth periods in Japan and South Korea (hereafter "Korea"), it is frequently argued that tightly woven elite networks were the major driving forces of the rapid economic development. On the one hand, the close government-business connections gave the government additional access points through which the government could influence the private sector (Johnson 1974, 1982; Amsden 1989). On the other hand, the cozy relations among bureaucrats, businessmen, and politicians served as a conduit to facilitate the flow of information, and encouraged flexibility and adaptability towards the changing business, social, and political environments (Okimoto 1989; Lee 1992).

These arguments commonly posit that cohesion among the society's elite ultimately enabled them to construct a common direction for economic growth. The sense of commonality among elites created "embedded autonomy": policy makers did not need to resort to draconian measures to advance their policy goals, and private firms did not have to have an excessively myopic focus on short-term profits (Evans 1995). In this view, the formation of informal networks provided an institutional foundation for rapid economic growth in East Asia.

Since the Asian financial crisis in 1997, however, numerous scholars have called into question the long-term efficacy of informal networks in

Index