

Competition Policy in Korea

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A Very Good Morning to all Members of this Conference!

First of all, I would like to extend my heartiest congratulations on the holding of the Third International Conference on “Korea and the World Economy.”

My whole-hearted thanks go to Dr. Lee Jong Won, President of the Association of the Korean Economic Studies, Dr. Kim Choongsoo, President of the Korea Development Institute, and Director Kar-yiu Wong from the Research Center for International Economics in University of Washington – for allowing me this opportunity to address you on the important subject of “Korea’s Competition Policy.”

So far, this international conference, held alternately in the United States and Korea, has examined and provided keen perspectives and insights on the impending challenges and issues facing the Korean economy. Through these meetings and discussions, it has made very valuable efforts to propose the most appropriate direction for the Korean economy.

In this Third Conference, the in-depth discussion will be conducted on the theme of “the Korean Economy in Transition.” I am sure that your insights and ideas presented here will be very meaningful and useful to us, given our experience in rapid paradigm shifts in our overall social environment since the launch of the Participatory Government. In addition, it will offer us a precious opportunity to explore the future aspects of the Korean economy altogether.

Distinguished members!

The Korean economy is currently undergoing fundamental changes in its growth paradigm, moving from the input-oriented growth of the past to the trend toward total factor productivity growth that we are seeing today.

During the past decades (from the 1960s to 1980s) of government-led development, Korea had achieved a remarkable 8 percent average annual

growth, mainly driven by inputs from large business conglomerates. However, since the 1990s, the facilities investment in traditional manufacturing sector has reached its excess capacity, while the supply of cheap labor also dried up. As a result, according to the research by KDI (done by three researchers including Han Jin Hee in December 2002), the potential growth rate has steadily followed a downward trend. It has steadily decreased from 7.8% in the 1980s to 6.6% in early 1990s and 6.0% in late 1990s.

In this era of paradigm shifts, the biggest challenge for the Korean economy is to expand growth potential and improve the economic system. In order to boost total factor productivity, it is essential to develop resources for new growth paradigms. To this end, technical innovation, market reform and adoption of global standards through expansion of market opening are strongly required. Technical innovation will result in more investment in IT, BT and NT, and increase value-added in existing industries while market opening will bring higher productivity in the non-trade sector, including service industry, such as education, healthcare and legal services.

Looking specifically at the role of the Korea Fair Trade Commission (KFTC), market reform to facilitate free competition is the most important task, to set up and maintain market rules for transparent business and fair competition. This is necessary for efficient resource allocation in the market. For a fair, transparent and competitive market environment, the government should establish market competition rules so that all businesses can safely carry out economic activities under free competition.

The reason for the efficiency of the free market economic system is its firm foundation on free competition, which has its basis on the “Harm Principle” by John Stuart Mill, meaning “being free as far as not giving any harm to others in the market.” In accordance with this, if any companies give harm to other market participants, let’s say, competitors, consumers or minority shareholders, competition will be in shambles. In this case, regulation is required.

The ultimate goal in the KFTC's competition policy is also, in line with this principle, to enhance transparency and fairness, and facilitate free competition in the market. Through these efforts, the KFTC expects to enhance market confidence, ensure growth potential and expand consumer welfare. Based on this principle, the KFTC is in charge of competition promotion policy, chaebol policy, subcontract transaction policy, and consumer protection policy.

First, we will work harder to improve regulations, prevent cartels and improve efficiency in M&A review in order to promote market competition.

Despite continuous reform of government regulations, there still remain a lot of outdated, excessive and unreasonable regulations, hampering fair competition in the market, serving as an obstacle to investment and having a negative impact on the creation of more jobs.

As a consequence, the government has introduced measures to streamline 152 anti-competitive regulations in the process of pursuing a market improvement policy in each industry. Among these measures, 112 regulations in the service sector are being implemented to improve standards through 21 government-wide private-public joint task forces. In response to 40 regulations in the non-service industry, the KFTC is taking the initiative to realize the improvement measures. As regulatory reform aims to clarify self-discipline and accountability in private sector as well as to re-establish the basic framework of the relations between the government and market, competitiveness of the Korean economy will be dramatically improved through free economic activities and enhanced competition.

Along with this, the KFTC will make steady endeavors to completely eradicate cartels, often regarded as the number one enemy of the market economy. Last year, the KFTC identified various cartels affecting the everyday lives of ordinary people, such as steel and cement, imposing 105.8 billion won in fines. More recently, the KFTC has punished cartel activities pertaining to apartment sales prices.

In order to step up the deterrence effect of cartels, the KFTC will increase the upper ceiling of surcharges from 5% of turnover of relevant items to 10%. In addition, we are strengthening the leniency program for whistleblowers (or informants) and persons who assist in the investigation process.

The KFTC is working hard to improve the M&A review system and reinforce substantial reviews of M&As that are likely to form monopolies. Moreover, administrative burdens on companies arising from business reviews will be relieved.

Second, through successful pursuit of “the 3-year Market Reform Roadmap” confirmed last year, we are striving to improve corporate ownership and governance structure and transparent business management.

First of all, we are planning to improve the regulation setting a ceiling on the total amount of shareholdings of other domestic companies.

This regulation is not the one that restrains investment, but rather it aims to limit shareholdings of other domestic companies by affiliates of business conglomerates. The target for this regulation is affiliates of business conglomerates with more than 5 trillion won of assets. Its ultimate goal is to prevent the formation of inflated capital through shareholdings in affiliates.

Expanding control through circular shareholdings is not only unfair in itself but also triggers unfair competition with small and medium-sized companies and chain-reaction bankruptcies in the overall business group. As such practices are likely to cause system risk, which leads to paralysis of bond and financial markets, the government restricts the share acquisition of other domestic companies to within 25% of net assets.

However, we do set the graduation standards for business conglomerates with excellent corporate governance, holding company structure, or small gaps between voting rights and cash flow rights. When many companies

meet these standards, thereby being free from this regulation, and market monitoring mechanism functions effectively, the KFTC plans to make an all-out review over this system in three years. In addition, we are going to improve the exemption measures in more reasonable way. Permanent corporate restructuring and set-up of new industry and industries related to the next generation growth engine will be actively supported while exemption on foreign-invested companies will be imposed more strictly considering its possible exploitation for expanding control.

Meanwhile, the scope of voting rights exercised by financial and insurance affiliates under business conglomerates will be reduced from current 30% to 15% step by step for three years. Through these efforts, we are working to minimize or prevent any side-effects arising from the dominance over financial capital by industrial capital. As share ownership of affiliates with customers' capital could cause conflicts of interest, advanced countries strictly prohibit acquisition itself.

Korea granted permission for business conglomerates to have financial affiliates during the development-oriented era due to the then insufficient development of the financial market. However, exercising voting rights was restrained from the time of introducing the system in 1987 to that of legal amendment in 2002. Even though 30% of voting rights were endowed due to concerns about hostile M&A takeovers in 2002, in principle, the scope of voting rights needs to be reduced along with advancement of the financial market as it could expand the control and influence of business groups through customer's property. The decision to reduce the scope step-by-step for a three-year period is to rebuff the shock of business arising from the changes of system and prepare for a better situation.

Moreover, by prohibiting cross-shareholdings between affiliates of the holding company and share ownership in domestic companies, which are not the affiliates of holding company, surpassing 5%, the KFTC is working toward enhancing transparency in holding company structures. Not only that, but we also encourage business groups to transform into holding companies as an improved model for corporate governance structure by reducing its conversion costs.

Besides, disclosure obligations toward non-listed and non-registered companies under the business group with more than 2 trillion won of total assets will be strengthened. Along with this, the KFTC is considering the reintroduction of the rights to request information on financial transactions, and improvement of the M&A review system and the damage compensation system for anti-trust cases. Recently, by confirming the amendment drafts on the MRFTA(Monopoly Regulation and Fair Trade Act), the Administration submitted it to the National Assembly.

Third, we are making special efforts to lay the foundation for fair subcontract transaction.

Stabilizing business management and ensuring competitiveness in small and medium-sized businesses are essential parts of the driving engine for economic growth and steady job creation. The government will expand the scope of applying the subcontract act confined to manufacturing and construction industries to the service industry. In addition, by expanding the target for surveying subcontract transactions, the KFTC is pursuing “the Plan of Foundation to Establish Fair and Transparent Subcontract Transactions”.

Fourth, the KFTC suggests a vision to establish consumer sovereignty and ensure prevention and post-rescue consumer damage, thereby heightening competition pressure from consumers.

By establishing a “comprehensive consumer protection plan” within this year, we are going to explore more efficient responses to the changing environment arising from the emergence of new types of consumer problems due to the rapid growth of the digital economy.

By improving the “Important Information Notification System,” consumers will be able to get more information. Through the introduction of Escrow, damages resulting from pre-paid transactions in the e-commerce sector can be further prevented. Besides, we are taking various steps to enhance efficiency in dispute settlements and rescuing consumer damage.

Only under the environment which consumers make better choices can we expect increased competition pressure from consumers. This will ultimately lead to the promotion of business competition.

Distinguished members!

System reform in the Korean economy has not been sufficient enough to create a transparent and fair market despite steady efforts and intentions thus far.

Change and innovation can bear fruit only when they are consistently pursued with a clear vision and goal according to a specific schedule. If there is no confidence that the reform will be carried out as scheduled under a certain goal, we can hardly expect any voluntary efforts or cooperation from market participants.

With undoubted direction of reform and predictability, the Participatory Government encourages active participation of market players by suggesting the visions, goals, challenges and schedules of market reform in the 3-Year Market Reform Roadmap.

Such market reform is expected to enhance the confidence of both domestic and international investors in the Korean economy by helping to put in place a transparent and fair market economic environment.

Until now, due to the “Korea Discount,” Korean companies could not be correctly evaluated by foreign investors. We hope market reform will help to address this problem, thereby improving corporate value and nurturing growth potential of the Korean economy in the long term.

Distinguished guests!

I’m confident that many valued opinions and proposals will emerge during this conference, suggesting a clear direction for the Korean economy during a period of transition. Reiterating my sincere gratitude to all of you

as you prepare for this meeting, I would like to conclude my speech by wishing all of the distinguished guests here a productive and enjoyable conference.

Thank you very much.