

**When are Banks Sold to Foreigners? An Examination of the Politics of Selling
Banks in Mexico, Korea, and China**

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In January 2006, the Ministry of Foreign Affairs (MOFA) in Beijing received a letter from former President George Bush. In the letter, Bush urged the Chinese government to approve an impending deal in which the Chinese government would sell 85% share ownership of a troubled Chinese bank to a consortium led by Citibank. In addition to praising Citibank and the other foreign member of the consortium, the Carlyle Group, Bush also intimated that a successful acquisition would be “beneficial to the comprehensive development of Sino-US relations.”¹ Undoubtedly, this letter quickly made its way to Zhongnanhai, where the Politburo Standing Committee discussed its content. The letter was then sent to the Central Banking Regulatory Commission (CBRC), the bureaucratic entity formally charged with approving this deal, along with a set of instructions from the leadership. In March 2006, the content of the letter was leaked to the official press by the government. Instead of facilitating the deal, the leaked letter made it virtually impossible to approve the deal, since it would appear as if the Chinese government was caving into foreign pressure. Soon afterward, the CBRC announced that the deal would not be approved as it currently stands because Citibank asked for a higher share of the bank than is currently allowed under Chinese regulations.²

The amazing aspect of this incident is that a letter needed to be sent through such formalized channels in the first place. Instead of intimate gatherings where Citibank officials pitched the sale to members of the Politburo or golf outings with senior technocrats, Citibank needed to mobilize someone with the stature of Bush, who in turn

¹ China Financial Net, *Lao Bushe Lijian Huaqi Yinhang Guangfahang Jinggou Zhizheng Yuelaiyue Weimiao (Senior Bush's Lobbying on Behalf of Citibank in the Bid for Guangdong Development Bank Brought About Interesting Development)* (China Financial Net, 2006 [cited 3/20 2006]); available from www.zgjr.com.

² Feng Xia, "Guangfahang Jinggouzhan: Yinjianhui Wuyi 'Puoxian' Huaqi Huo Gaifang'an," *Shanghai Securities News*, 4/20 2006.

only had the option of sending a letter through the proper channels.³ Although some foreign investment banks have had success gaining access to the political elite, most struggle to gain regular access to even junior level technocrats in the central government. This contrasts sharply with the cozy relationship between domestic private capital and the state in Mexico and Korea and, in the case of Mexico, seemingly intimate relations between foreign capital and the state.

At first glance, the explanation of why foreign banks have had such a tough time acquiring Chinese financial institutions seems straight-forward. Sales of state banks or domestically owned private banks often take place in the aftermath of financial crises that deplete the banking system of capital. Illiquidity forces the state to change policies in order to bring in foreign capital to restructure the banks. Often, the new rules allow foreign banks to gain controlling stakes. In recent years, multi-national financial institutions (MNFIs) have acquired major banks in Mexico, Brazil, Argentina, and Korea in the aftermath of financial crises. However, an examination of the pattern of bank restructuring in Mexico, Korea, and China suggests that there is at most a loose correlation between liquidity need and successful foreign acquisition of domestic banks. Both Mexico and Korea spent enormous amount of public funds to recapitalize banks before selling to either domestic private interests or MNFIs. None of these cases exhibits a clear pattern of fire-sales to cash-rich MNFIs.

This paper explains the variation in MNFI success in acquiring controlling stakes in financial institutions in Mexico, Korea, and China by focusing on the role of *domestic* private capital in the bank restructuring process. The first pattern noted by the paper is

³ Before Citibank's acquisition of Banamex in 2001, Menezes went to Mexico City and discussed the acquisition with Vincente Fox, the President of Mexico. See John Barham, "Citigroup's Latin Platform," *LatinFinance* 2001, no. 39 (2001).

that the role of domestic capital is crucial, even in cases where MNFIs gained controlling stakes in domestic banks. Without active lobbying by powerful domestic interests, MNFIs would have a difficult time succeeding, even in a place like Mexico, where the United States looms large in the political landscape.

Furthermore, the three cases reveal one clear difference between China on the one hand and Mexico and Korea on the other hand: the continual rule by a one-party socialist government in China. The socialist legacy in China affects two crucial variables affecting government-business relations in China. First, the main selectorate of government elite does not include members of large, concentrated private business groups. By selectorate, I mean “the set of people whose endowments include the qualities or characteristics institutionally required to choose the government's leadership.”⁴ Although Kennedy's work shows that both private and state business conglomerates have regular contacts with government officials,⁵ Chinese private business groups do not have nearly as much impact on the *selection* of political elite as their counterparts in Mexico and Korea. Although there is disagreement over the composition of the selectorate in China, the disagreement is minor comparatively speaking.⁶

Finally, China's socialist legacy also affects the ownership structure of the banks, which are mainly state-owned, as opposed to banks in Korea and Mexico, which had been mainly privately owned before financial crises. The state ownership of Chinese banks means that bank managers and their bureaucratic guardians are motivated by their standing in the administrative and political hierarchy rather than by profit. Between

⁴ Bruce Bueno de Mesquita et al., *The Logic of Political Survival* (Cambridge, Mass.: MIT Press, 2003).

⁵ Scott Kennedy, *The Business of Lobbying in China* (Cambridge, MA: Harvard University Press, 2005).

⁶ Shirk makes the argument that Central Committee members are in the selectorate, while others disagree. See Susan Shirk, *The Political Logic of Economic Reform in China* (Berkeley, CA: The University of California Press, 1993).

Mexico and Korea, ownership structure also affects variation in outcomes. While the concentration in bank ownership in Mexico gave owners incentive to sell to MNFIs at a high price, relatively low concentration of bank ownership in Korea directed *chaebol* interests toward maintaining the status quo in which domestically held banks provided *chaebols* with soft loans. Because *chaebols* were highly diversified and held only small stakes in banks, they had weak incentive of selling to foreigners for a high cash premium.

Contrasting China on the one hand and Mexico and Korea on the other, because domestic businesses are key members of the selectorate in the latter two countries, they have enormous influence over national policy, including bank policies. Moreover, because the benefits of government policies accrue to a few individuals who own financial or industrial conglomerates, they have very high incentive to either singly or collectively influence government policies.⁷ Banking policies in both Mexico and Korea thus were structured to benefit a few private entrepreneurs at great public expenses, while in the case of China, bank policies were structured to bolster the position of the senior technocrats for political reasons. Instead of benefiting specific industrial or financial conglomerates, Chinese financial policies were mainly designed to benefit broad swaths of either state industrial or, increasingly, agricultural interests in order to bolster the “administrative accomplishments” of the leading technocrats. As a result, ceding control of Chinese banks to MNFIs is politically a very difficult proposition. Not only do MNFIs lack powerful domestic capital as allies, they face a political arena in which they have little influence. In Korea, MNFIs face a daunting--albeit different-- obstacle. Although banks are privately owned and there are strong business interests, it is much more

⁷ Needless to say, this is a classic Olsonian insight. See Mancur Olson, *The Rise and Decline of Nations: Economic Growth, Stagflation and Social Rigidities* (New Haven, Conn.: Yale University Press, 1982).

difficult for MNFIs to make an alliance of mutual interest with domestic conglomerates since they only have low stakes in the banks. Given that, they would rather lobby the government for bailouts of the banks, followed by bank bailouts of the business conglomerates. They have little to gain if banks were sold to MNFIs for a high cash premium.

Alternative Hypotheses

The conventional explanation of varying policy outcomes in developing countries centers on the autonomy of the bureaucracy. According to this argument, the more economic bureaucrats are insulated from politics, the more they are able to ward off rent-seeking influence and make growth-promoting policies.⁸ With respect to banking policies, if the insulated technocracy believes that private control over banks would lead to higher bank efficiency, they would quickly privatize banks through competitive bidding. They would not first nationalize banks and use tax payers' money to recapitalize these banks before selling them. More recent research reveals that bureaucrats in all three countries were subject to considerable intervention by the political leadership.⁹ As I argue below, it is not the degree of political intervention that separates

⁸ See, for example, Peter B. Evans, *Embedded Autonomy: States and Industrial Transformation* (Princeton, N.J.: Princeton University Press, 1995), Stephan Haggard and Chung H. Lee, "The Political Dimension of Finance in Economic Development," in *The Politics of Finances in Developing Countries*, ed. Stephan Haggard, Chung H. Lee, and Sylvia Maxfield (Ithaca, NY: Cornell University Press, 1993), Chalmers Johnson, *Miti and the Japanese Miracle: The Growth of Industrial Policy, 1925-1975* (Stanford, CA: Stanford University Press, 1982).

⁹ David C. Kang, *Crony Capitalism: Corruption and Development in South Korea and the Philippines*, *Cambridge Studies in Comparative Politics* (New York: Cambridge University Press, 2002), Timothy P. Kessler, *Global Capital and National Politics: Reforming Mexico's Financial System* (Westport, Conn.: Praeger, 1999), Sylvia Maxfield, *Governing Capital: International Finance and Mexican Politics* (Ithaca, NY: Cornell University Press, 1990), Victor Shih, "Partial Reform Equilibrium, Chinese Style: Political

these three cases, but the source of political intervention. In the case of China, the political elite intervened in the decisions of technocrats in order to fight off or appease political pressure emanating from within the regime. In the case of Mexico and South Korea, domestic private capital played a heavy role in exerting political pressure.

As mentioned above, liquidity needs in the aftermath of financial crises seem to be the most obvious explanation of selling domestic banks to foreign investors.¹⁰ The classic case of this pattern is Argentina, which privatized a sleuth of provincial banks to MNFIs in the aftermath of the 1995 crisis.¹¹ In the case of China, due to its enormous foreign exchange reserve, it is able to recapitalize banks with relative ease, almost eliminating its need of foreign capital.¹² A close examination of banking policy in Mexico after the 1994 Tequila Crisis and in Korea after the Asian Financial Crisis, however, reveals that these governments did not hold a “fire-sale” of domestic banks to foreigners to meet liquidity needs. Rather, the government first expended enormous amount of public money to write-off non-performing loans and to recapitalize troubled banks before selling banks to domestic capital and MNFIs.

One alternative hypothesis is that the US historically exerted greater influence over Mexico and Korea than over China, giving US MNFIs greater access to the political elite in these countries. While there is some indication of this in the Mexican case, MNFIs still ran into enormous difficulties without the help of domestic capital. For

Incentives and Reform Stagnation in Chinese Financial Policies," *Comparative Political Studies* 2007, no. 10 (forthcoming).

¹⁰ Maxfield implies that the need to attract foreign capital drove financial policies in many Latin American countries. See Sylvia Maxfield, *Gatekeepers of Growth the International Political Economy of Central Banking in Developing Countries* (Princeton, N.J.: Princeton University Press, 1997).

¹¹ Lee J. Alston and Andres A. Gallo, "Banking System under Convertibility: The Roles of Crises and Path Dependence," in *NBER Working Paper*, ed. NBER (Cambridge, MA: NBER, 2000).

¹² China Economic Quarterly, "Understanding China's Bank Bailout," *china Economic Bulletin* 2004, no. 1 (2004).

example, when the Mexican deposit insurance agency repaid Citibank ahead of schedule, causing a reduced profit of 300 million US dollars, Citibank's Robert Rubin, the former secretary of treasury who engineered a major US bailout of the Mexico in 1994, could not reach top level officials for days.¹³ In contrast, with the help of domestic capital, Citibank was able to acquire Banamex in a matter of weeks.

Mexico

Despite severe bank liquidity problems, MNFIs did not acquire Mexican banks at fire-sale prices in the aftermath of the Tequila Crisis in 1994. Rather, these banks were acquired after enormous public money was spent to re-capitalize them. Without a doubt, the main beneficiaries of the sale of Mexican banks were a small group of domestic financiers, who were highly motivated to lobby for public bailouts and were at the same time crucial actors in the Mexican political system.

The post-war Mexican financial system underwent several rounds of liquidity crises due to prolonged Partido Revolucionario Institucional (PRI) strategy to use state fiscal and financial resources to buy political support from politically threatening groups, including the urban poor, domestic capital, and the urban middleclass.¹⁴ Up to the late 70s, the PRI had balanced the interests of the urban poor and that of the major conglomerates, but with the increasing ease of capital mobility which increased the possibility of capital flight, the PRI regime began to pay closer attention to the demands

¹³ Peter Fritsch, "Going South: How Citibank's Deal to Buy Mexican Bank Turned into a Standoff," *Wall Street Journal*, 9/20 2000.

¹⁴ Kessler, *Global Capital and National Politics: Reforming Mexico's Financial System*.

of domestic capital.¹⁵ Although the de la Madrid Administration did not reverse bank nationalization implemented at the end of the Portillo Administration, the PRI compensated increasingly organized domestic capital with high yield government bond and control over brokerages, the combination of which guaranteed the buyers of government bonds-- the newly privatized brokerages-- high margins.¹⁶

Into the Salinas administration, increasing electoral threats from rival parties forced the PRI to privatize the banks in order to raise cash to implement a generous redistribution program to appease the urban poor, who had voted for the opposition in the 1988 election.¹⁷ The privatization was unusually transparent for a developing country, beginning with the evaluation of bank value by international consulting firms to establish base-line prices of these banks.¹⁸ Nonetheless, only domestic capital was allowed to bid, and some 30 or so domestic outfits, mostly cash-rich brokerage houses, bid on some 18 banks.¹⁹ Again, contrary to the portrait of insider privatization, private capital bid aggressively, resulting in a large wind-fall for the PRI. Banamex and Bancomer, the two largest banks in Mexico at the time, drew winning bids of around 9 billion pesos each, or over 2 billion USD each at the prevailing exchange rate.²⁰ Again, the PRI compensated

¹⁵ Although the convention explanation of increasing power of capital is increasing ease of capital flow, capital account convertibility is itself endogenous to the success of capital lobbying. Maxfield, *Governing Capital: International Finance and Mexican Politics*.

¹⁶ Kessler, *Global Capital and National Politics: Reforming Mexico's Financial System.*, pp. 55.

¹⁷ Timothy Kessler, "Political Capital: Mexican Financial Policy under Salinas," *World Politics* 51, no. 1 (1998).

¹⁸ Haluk Unal and Miguel Navarro, "The Technical Process of Bank Privatization in Mexico," in *FIC Working Papers*, ed. Wharton Financial Institutions Center (Philadelphia, PA: Wharton School of Business, 1999).

¹⁹ *Ibid.*

²⁰ *Ibid.*

aggressive bidders with protectionist policies to limit foreign competition, which drove up domestic interest rates and bank profit.²¹

Newly energized with enormous bank assets and easy access to foreign capital, these newly privatized banks went on a borrowing binge to take advantage of the relatively low international interest rates. When international capital lost confidence in Mexico in 1994, the country was plunged into a financial crisis, involving rapid devaluation, high inflation, and recession. Despite a 20 billion dollar credit from the US, the meltdown continued as interest rates shot upward.²² Ordinary Mexicans suddenly found themselves owing much more than they had borrowed originally, thus driving up the default rate to over 33%.²³ Instead of a fire-sale of domestic financial institutions, the government set up an expensive scheme to recapitalize the banks. To be sure, during the crisis, few but the most daring foreign investors would have willingly invested money in Mexican banks, but low prices might have enticed some investors.

Instead of a fire-sale, in June 1995, the Bank Deposit Protection Fund (Fobaproa—its acronym in Spanish) swapped bank non-performing loans (NPLs) for Fobaproa bonds which were backed by the government but paid no yield. After the swap, Fobaproa delegated the task of recovering these loans to the banks themselves, and once these loans were digested, Fobaproa and the banks would split the realized losses from the NPLs.²⁴ Within months, 12 banks swapped their non-performing loans for some 67 billion pesos worth of Fobaproa bonds, instantly converting non-performing assets into

²¹ Kessler, "Political Capital: Mexican Financial Policy under Salinas."

²² Kessler, *Global Capital and National Politics: Reforming Mexico's Financial System.*, pp. 122

²³ Ibid.

²⁴ Bank of Mexico, *Financial Support Programs for the Banking System and Its Debtors* (2006 [cited 5/1 2006]); available from <http://www.banxico.org.mx/gpublicaciones/mexicaneconomy/mexecon96/m96iv2.html>, Brian Caplen, "A House Built on Sand," *Euro money* 98, no. 351 (1998).

“performing” assets.²⁵ After the swap, an additional relief was granted to the banks. Instead of being forced to recover NPLs within a time frame, banks themselves decided when to recover the non-performing loans, in effect allowing them to decide when to realize the book losses of the NPLs. This became an enormous problem for Fobaproa in subsequent years because banks essentially had no incentive to realize the losses and did little to recover NPLs on behalf of Fobaproa.²⁶

After the Tequila Crisis, the ceiling on foreign ownership of banks was raised for smaller banks, and Spanish and American MNFIs came in aggressively to acquire domestic banks. Instead of a fire-sale by domestic capital to foreign capital, the government stepped in to bail out these banks, allowing domestic capital to sell them at a much higher price to MNFIs. For example, before Citibank agreed to pay 200 million dollars for Banco Confia, Grupo Abaco, the owner of Confia, persuaded Fobaproa to take over some $\frac{3}{4}$ of Confia’s loan portfolio and to give Confia Fobaproa bonds. Unlike the other swaps, where the bank and Fobaproa shared the book losses of NPLs, Fobaproa was persuaded to take the entire loss itself.²⁷ The 200 million price was only slightly less than the 212 million that Grupo Abaco paid for Confia in 1991.²⁸

In 1998, President Zedillo, which oversaw a legislature dominated by the opposition, pushed for an even more costly scheme to bail out the privately owned banks. In 1998, there was roughly 18 billion dollar worth of Fobaproa notes held by Mexican banks. Instead of zero coupon bonds, Zedillo wanted to convert these notes into interest-bearing treasuries. Although there was technical merit to this scheme, such as increasing

²⁵ Bank of Mexico, *Financial Support Programs for the Banking System and Its Debtors* ([cited]).

²⁶ Caplen, "A House Built on Sand."

²⁷ Fritsch, "Going South: How Citibank's Deal to Buy Mexican Bank Turned into a Standoff.", Kessler, *Global Capital and National Politics: Reforming Mexico's Financial System.*, pp. 126

²⁸ Unal and Navarro, "The Technical Process of Bank Privatization in Mexico."

liquidity in the banking system, this scheme would have quickly increased the deficit from 28% of GDP to 42% of GDP.²⁹ Despite an initial fury of outcry from the public and from opposition legislators, PRI and opposition Partido Acción Nacional (PAN), both of which received extensive business support, formed a coalition to convert much of the Fobaproa notes into treasuries.³⁰

After this enormous public bailout, Mexican banks became prime real estate for MNFIs acquisitions. The race to conquer the Mexican banking market culminated to Citibank's 12.5 billion purchase of Banamex in 2001. In total contrast to the tortuous path of selling banks to foreigners in China, the deal was struck in five weeks.³¹ While Robert Rubin, former secretary of Treasury and vice-chairman of Citigroup, might have helped push the deal along, pressure from domestic capital was likely the decisive factor in paving the way for the Banamex deal. For one, the Banamex deal made major shareholders fabulously rich. Over 1/3 of the 12.5 billion sale ended up in the pockets of three individuals: Alfredo Harp, Roberto Hernandez and Jose G. Aguilera. Hernandez, the largest shareholder, received 0.38% ownership over Citigroup, as well as nearly 1 billion USD.³² This constitutes a nearly six-fold return for Hernandez and company as the group of financiers behind Accivals, the brokerage owned by Hernandez and his partners, originally paid 2.3 billion USD for the bank in 1991.³³

What explains the pattern of Mexican banking policy, which involves costly public bailout before selling to MNFIs for relatively high prices? First, economic

²⁹ Caplen, "A House Built on Sand.", Kessler, *Global Capital and National Politics: Reforming Mexico's Financial System*.

³⁰ Kessler, *Global Capital and National Politics: Reforming Mexico's Financial System.*, pp. 134.

³¹ Tim Weiner, "After a Bailout, a Wedding," *New York Times*, 5/27 2001.

³² El Economista, "Hernandez, Harp and Aguilera Laughing All the Way between Banks," *El Economista* 2001.

³³ Richard Jacobsen, "Citibank, Banacci Roots Tangled in Mexican History," *Reuters*, 5/17 2001.

nationalism fails to explain the trajectory of banking policies, since much of the banking sector ended up in the hands of the MNFIs anyway. Looking beyond ideational explanations, domestic capital has long been important players in the political arena. The Monterrey financiers helped found the opposition PAN in order to threaten PRI dominance, which in effect forced PRI to implement more pro-capital policies.³⁴ Moreover, Mexico has a tightly knitted elite who comes from a selected group of families and attends a handful of private schools and universities. This further increases the density of communication and mutual influence between the government and business elite.³⁵ Furthermore, after the Salinas privatization gave control of banks to a handful of domestic financial groups, the owners of these banks had high incentive to influence government policies in order to maximize the profit of these entities. They lobbied for liberalization of international financial flow to take advantage of the arbitrage, and when the financial crisis hit, they lobbied for public bailouts so as to minimize losses, if not to make a fabulous profit at the public's expense.

Although the influence of MNFIs doubtless facilitated the sale of domestic banks, available evidence suggests that foreign influence did not approach the importance of domestic pressure. In 2000, the Mexican government repaid 2.5 billion USD in converted Fobaproa notes held by Banco Confia, costing Citibank some 300 million in lost interest. Citibank's Vice-Chairman Robert Rubin, who had engineered a US bailout of the Mexican government in 1995, was soon on the phone trying to reach top Mexican

³⁴ Kessler, *Global Capital and National Politics: Reforming Mexico's Financial System.*, pp. 52.

³⁵ Ben Ross Schneider, "Big Business and the Politics of Economic Reform: Confidence and Concertation in Brazil and Mexico," in *Business and the State in Developing Countries*, ed. Sylvia Maxfield and Ben Ross Schneider (Ithaca, NY: Cornell University Press, 1997), Ben Ross Schneider, "The Career Connection: A Comparative Analysis of Bureaucratic Preferences and Insulation," *Comparative Politics* 25, no. 3 (1993).

officials. However, he reportedly spent days calling old contacts with little success.³⁶ In contrast, after Banamex chairman Hernandez approached Citibank about a possible sale, he guided the deal through Mexico's complex political terrain and bureaucratic red-tapes. In addition to arranging meetings between Citibank management and top Mexican officials, Hernandez also persuaded his old college roommate, President Fox, to give public endorsement of the deal.³⁷ The deal, the biggest in Mexican history, was completed within five weeks. Without highly motivated and influential domestic capital, the sale of domestic banks to MNFIs would have been much more difficult.

Korea

Although MNFIs initially succeeded in purchasing Korean financial institutions due to post-crisis IMF pressure, the Korean government's attitude against MNFIs soon hardened, and the government clearly revealed a preference for domestic ownership of banks. The *chaebols'* enormous clout in politics throughout post-war era, as well as their low stakes in Korean banks before the crisis, likely made MNFI acquisition of domestic banks extremely difficult.

In the aftermath of his successful coup, Park Chung-hee made a show of fighting corruption by arresting the heads of large *chaebols* and by nationalizing all four of Korea's private banks.³⁸ Thus began an era of government directed credit to promote

³⁶ Fritsch, "Going South: How Citibank's Deal to Buy Mexican Bank Turned into a Standoff."

³⁷ Associated Press, "Some See Fruits of Globalization, Some Us Domination, in Citibank's Mexican Buyout," *Associated Press Newswires*, 8/3 2001.

³⁸ Byung-sun Choi, "Financial Policy and Big Business in Korea: The Perils of Financial Regulation," in *The Politics of Finance in Developing Countries*, ed. Stephan Haggard, Chung H. Lee, and Sylvia Maxfield (Ithaca, NY: Cornell University Press, 1993). *Chaebols* are large industrial conglomerate headed by a flagship company, which acts as a holding company. For further details, see Stephan Haggard, Wonhyuk

industrial polices.³⁹ Moreover, state directed credit gave rise to a crony capitalism in which *chaebols* benefited from soft loans from the government and, in return, gave cash kickbacks to Park's political machinery and his personal trove.⁴⁰ In addition to domestic loans, the Park government also gave connected *chaebols* government guarantees to foreign loans. Given the spread between international and domestic interest rates, *chaebols* with loan guarantees made an automatic profit from the spread, which encouraged accelerated foreign borrowing by these *chaebols*.⁴¹ Not surprisingly, high foreign borrowing eventually led to debt crisis where many highly leveraged firms were on the verge of defaulting on their foreign loans. Initially, the government prevented an attack on the won by preemptively devaluating the won, which further increased dollar-dominated debt owed by *chaebols*.⁴² In response to the growing crisis, Park simultaneously placed a moratorium on all loans, converted many short-term loans to either long-term loan or equity ownership of the firms, and blocked capital account convertibility.⁴³ This introduced an era of highly repressed financial allocation for the remainder of the 70s. However, the government ensured that connected *chaebols* received enormous amount of state loans for the heavy industry and chemical drive, thus

Lim, and Euysung Kim, *Economic Crisis and Corporate Restructuring in Korea: Reforming the Chaebol*, *Cambridge Asia-Pacific Studies* (Cambridge, UK; New York: Cambridge University Press, 2003).

³⁹ Chung H. Lee and Stephan Haggard, "Introduction: Issues and Findings," in *Financial Systems and Economic Policy in Developing Countries*, ed. Chung H. Lee and Stephan Haggard (Ithaca, NY: Cornell University Press, 1995).

⁴⁰ Choi, "Financial Policy and Big Business in Korea: The Perils of Financial Regulation.", Kang, *Crony Capitalism: Corruption and Development in South Korea and the Philippines*.

⁴¹ Choi, "Financial Policy and Big Business in Korea: The Perils of Financial Regulation.", Wonhyuk Lim, "The Emergence of the Chaebol and the Origins of the Chaebol Problem," in *Economic Crisis and Corporate Restructuring in Korea: Reforming the Chaebol*, ed. Wonhyuk Lim, Stephan Haggard, and Euysung Kim (New York: Cambridge University Press, 2003).

⁴² Choi, "Financial Policy and Big Business in Korea: The Perils of Financial Regulation."

⁴³ Ibid.

intensifying *chaebol* reliance on state resources and concurrently state dependency on *chaebols* to generate growth and employment.⁴⁴

In the Chun Doo-hwan Administration, banks were slowly privatized, but each *chaebol* could only hold at most 8% share in a bank. Furthermore, the Office of Banking Supervision regulated how much banks could lend to large *chaebols*.⁴⁵ In the short and medium run, *chaebol* financing was limited by the latter policy, which forced expanding firms to seek financing through alternative channels: the capital market, non-bank financial institutions (NBFIs) and foreign credit. By 1990, NBFIs accounted for roughly the same share of corporate financing as banks.⁴⁶ Because there were no regulations on *chaebol* ownership of NBFIs, the conglomerates soon formed numerous NBFIs to organize finance for the groups. Coupled with loose regulations on borrowing from abroad, these NBFIs borrowed heavily from abroad on behalf of the *chaebols*, planting the seeds for the Asian Financial Crisis (AFC).⁴⁷ A longer term implication of Chun's banking policies is that influential *chaebols* could not acquire large stakes in major banks, which after the Asian Financial Crisis, gave them much weaker incentive to seek the sale of Korean banks to cash-rich MNFIs than Mexican financiers.

In the fall of 1997, the currencies of Asian countries toppled in succession, and Korea was forced to float the won in December.⁴⁸ The devaluation of the won immediately created massive liquidity problems in the system. Highly leveraged NBFIs,

⁴⁴ Lim, "The Emergence of the Chaebol and the Origins of the Chaebol Problem."

⁴⁵ More research is needed to discern why chaebols did not succeed in gaining greater control over banks, given their powerful clout. Joon-ho Hahm, "The Government, the Chaebol and Financial Institutions before the Economic Crisis," in *Economic Crisis and Corporate Restructuring in Korea: Reforming the Chaebol*, ed. Wonhyuk Lim, Stephan Haggard, and Euyung Kim (New York: Cambridge University Press, 2003).

⁴⁶ Ibid.

⁴⁷ Stephan Haggard, *The Political Economy of the Asian Financial Crisis* (Washington, DC: Institute for International Economics, 2000), pp. 35-36.

⁴⁸ Ibid., pp. 1.

many of which were owned by the *chaebols*, suddenly faced much higher debt because their debt was denominated in dollar. Thus, they were unable to provide financing to *chaebols*, which by that time had a debt-equity ratio of 519%, compared with an average of 154% in the US.⁴⁹ This in turn caused a massive wave of defaults, creating high non-performing loans and illiquidity in many of the major banks in Korea.

As in 1972, the government intervened massively to stabilize the financial system. However, because the Korean government received IMF facilities to prevent a further devaluation of the won, it also had to make a show of complying with IMF demands during the bailout. The 1998 bailout of Korean financial institutions totaled some 123 trillion won, or roughly 123 billion USD.⁵⁰ 48 billion dollars was used for bank recapitalization, while 42 billion was earmarked for buying NPLs from distressed banks. Finally, another 19 billion USD was used for deposit insurance claims.⁵¹ To finance this costly undertaking, the government issued 104 billion USD in bonds through Korea Deposit Insurance Corporation (KDIC) and Korea Asset Management Corporation (KAMCO).⁵² This was well over 10% of Korea's GDP in 1998.

Unlike Mexico, however, big businesses pressured the government to bailout banks not so much to restore the value of the banks, but to ensure the flow of credit to *chaebols*. To be sure, the Korean government forced many *chaebols* to undergo “work out” programs in which banks imposed conditions on distressed debtors before

⁴⁹ This figure is for the top 30 chaebols. Joseph Bisignano, "Precarious Credit Equilibria: Reflections on the Asian Financial Crisis (Bis Working Paper No. 64)," (Basle, Switzerland: Bank for International Settlements, 1999).

⁵⁰ This assumes a won-dollar exchange rate of 1000, although the won was much weaker at the beginning of 1998.

⁵¹ Kyung-Gon Ro, "Banking Industry Consolidation in Korea," in *BIS Working paper*, ed. Bank for International Settlement (Basel: BIS, 2001).

⁵² *Ibid.*

restructuring loans or extending more liquidity.⁵³ Nonetheless, massive government bailout of the banks greatly decreased bank incentive to put pressure on *chaebols* to truly restructure, which meant that many “work out” programs amounted to little more than debt forgiveness.⁵⁴ With relatively low ownership of banks, *chaebols* did not seem to care that some 8 banks were nationalized by the government, as long as banks received enough liquidity with which to bail out the troubled *chaebols*. They also did not press the government to sell Korean banks to MNFIs after the recapitalization of these banks. If anything, they probably opposed it since foreign ownership would end the cozy relationship between banks and business conglomerates.

However, because Korea had to make a show of complying to IMF conditionality, the government sold substantial stakes of some 6 national-level banks in the aftermath of the crisis. However, absolute majority share was only sold in one case (Korea First Bank) to US-based private equity firm Newbridge Capital.⁵⁵ When HSBC asked for controlling stake of Seoul Bank, however, the government rejected the deal, opting for continual state control over the bank.⁵⁶ After the sale of KFB to Newbridge, the Korean government, under pressure from the public and from the *chaebols*, halted the sale of banks to MNFIs. In order to escape IMF conditionality, Korea repaid its IMF loans early in 2000.⁵⁷ Subsequently, the government committed an additional 40 billion dollars into bank restructuring.⁵⁸

⁵³ Kyung Suh Park, "Bank-Led Corporate Restructuring," in *Economic Crisis and Corporate Restructuring in Korea: Reforming the Chaebol*, ed. Wonhyuk Lim, Stephan Haggard, and Euysung Kim (New York: Cambridge University Press, 2003).

⁵⁴ Ibid.

⁵⁵ Chungwon Kang, "From the Front Lines at Seoul Bank: Restructuring and Reprivatization," in *IMF Working Paper*, ed. International Monetary Fund (Washington, DC: IMF, 2003).

⁵⁶ Ibid.

⁵⁷ Ibid.

⁵⁸ Ibid.

Instead of selling restructured banks to MNFIs at a high premium, the government began to place banks either under permanent state ownership or engineered their sales to large domestic financial conglomerates. The Ministry of Finance, now operating under President Kim Dae-jung, pushed for a banking act that would eliminate the limit for Korean business groups to hold bank shares if they were classified as "specialized financial groups"⁵⁹ After this law passed in 2002, both domestic and foreign financial conglomerates could bid on banks, and the first test case was that of Seoul Bank. Both US-based Lonestar Capital and Hana Bank, a domestic bank with minority foreign shareholders, bid on Seoul Bank, but government regulators expectedly gave Hana control over Seoul Bank, even though Lonestar offered more up-front cash than Hana did.⁶⁰ The tide against MNFIs turned further when the government pressured Kookmin Bank, a bank where Goldman Sachs had acquired controlling stakes, to merge with government controlled Housing Credit Bank. After the merger, Goldman became the second largest holder with 6.86% of the shares, while the Korean government became the largest shareholder at 9.64% of the shares.⁶¹

Regardless of what one believes about the source of spectacular growth in post-war Korea, historical evidence suggests a rather explicit exchange between the major *chaebols* and the military dictators (both Park and Chun) in which the government agreed to provide financial and fiscal subsidies in exchange for campaign financing and bribes.⁶² Again, without taking a stand on why this form of corruption never got out of hand, it

⁵⁹ Ibid.

⁶⁰ Kang, "From the Front Lines at Seoul Bank: Restructuring and Reprivatization."

⁶¹ Kookmin Bank, *Major Shareholders of New Kookmin before and after Merger* (2001 [cited 5/5/2006]); available from <http://inf.kbstar.com/quics?page=A001193&cc=a005049:a005049>.

⁶² Kang, *Crony Capitalism: Corruption and Development in South Korea and the Philippines*, James Schopf, "An Explanation for the End of Political Bank Robbery in the Republic of Korea: The T & T Model," *Asian Survey* XLI, no. 5 (2001).

seems fairly clear that large *chaebols* constituted important members of the electorate for much of post-war South Korea.⁶³ Even under the Park dictatorship, his party, the Democratic Republican Party, spent some 43 million USD annually while some 40 million USD was spent to buy votes in the 1967 election alone.⁶⁴ Without corporate sponsorship, such extravagant spending would have been impossible, and Park would have been under greater political threat.

With the introduction of democracy in Korea, money politics became even more important as politicians scrambled to raise sufficient funds to win competitive elections. The 1992 National Assembly election, for example, cost an estimated 5.1 trillion won (roughly 5.1 billion USD), whereas the 1981 election cost between 266-400 million dollars.⁶⁵ Between 1994 and 1998, Samsung in all likelihood contributed over one billion USD to politicians, while Hyundai and LG both gave well above half a billion USD each.⁶⁶ Besides *chaebols'* enormous impact on campaign finance, there was frequent social and policy interaction between business leaders and officials. This “embeddedness” stemmed partly from the common practice of *amakudari* in the Korean bureaucracy which placed early bureaucratic retirees in various *chaebols*.⁶⁷

As a result of their political contribution and their dense interaction with officials, *chaebols* influenced financial policies throughout Korea’s post-war history. For example, when President Kim Young-sam set up a commission on financial reform, the *chaebols*

⁶³ On why corruption never got out of hand in Korea, there are at least two versions: mutual hostage and embedded autonomy. See Alice H. Amsden, *Asia's Next Giant: South Korea and Late Industrialization* (New York: Oxford University Press, 1989), Evans, *Embedded Autonomy: States and Industrial Transformation*, Kang, *Crony Capitalism: Corruption and Development in South Korea and the Philippines*.

⁶⁴ Kang, *Crony Capitalism: Corruption and Development in South Korea and the Philippines*., pp. 100.

⁶⁵ Ibid.

⁶⁶ Ibid., pp. 162

⁶⁷ Ibid. pp. 72. Evans, *Embedded Autonomy: States and Industrial Transformation*.

sent their representatives and blocked stricter regulatory measures over merchant banks and NBFIs.⁶⁸ Although the precise channels through which *chaebols* exerted influence on post-crisis banking policies remain unclear, past experience strongly suggests that they had a hand in the generous government bailout and hardening attitude against foreign acquisitions. Like in Mexico, the influence of private conglomerates can clearly be felt in the political arena. However, due to low *chaebol* ownership of major banks and, concurrently, diverse *chaebol* holdings across numerous sectors, their main goal after the crisis was to use public resources to continue the flow of soft loans to the conglomerates, rather boosting the market value of Korean banks.

China

In contrast to Korea and Mexico, non-state private conglomerates have no political leverage over the senior leadership. Even large state conglomerates have weak incentive and ability to influence elite decision. Thus, MNFIs seeking to gain controlling stakes in Chinese banks can find no powerful allies that can influence an outcome. Thus, relative to Korea or Mexico, internal political dynamics play a much greater role in setting the trajectory of banking policies in China.

Although there was no apparent banking crisis in China in the aftermath of the Asian Financial Crisis, the Chinese banking system had long exceeded the threshold for

⁶⁸ Byung-kook Kim, "The Politics of Chaebol Reform: 1980-1997," in *Economic Crisis and Corporate Restructuring in Korea: Reforming the Chaebol*, ed. Wonhyuk Lim, Stephan Haggard, and Euysung Kim (New York: Cambridge University Press, 2003), Wonhyuk Lim, Stephan Haggard, and Euysung Kim, "Introduction: The Political Economy of Corporate Restructuring," in *Economic Crisis and Corporate Restructuring in Korea: Reforming the Chaebol*, ed. Wonhyuk Lim, Stephan Haggard, and Euysung Kim (New York: Cambridge University Press, 2003).

technical insolvency by 1997. Non-performing loan ratio was estimated at 40%.⁶⁹ Taking the opportunity of the AFC, Premier Zhu Rongji centralized the banking system. Furthermore, because the central bureaucracy played up the financial problem, he also orchestrated an impressive bailout scheme of Chinese banks. Taking a cue from Korea, Zhu formed state-owned asset management companies (AMCs) to take over some 175 billion dollars (1.4 trillion RMB) in NPLs from the Big Four Chinese banks. Similar to both the Korean and the Mexico bailouts, the AMCs issued government backed notes in the same amount to the banks, instantly transforming NPLs into performing assets.⁷⁰ Although China did not face an attack on the RMB due to its relatively strict capital control, minutes of the PBOC Monetary Committee reveal that top policy makers were worried about the integrity of the RMB in the midst of the AFC.⁷¹ Thus, a fire-sale of Chinese banks in the aftermath of the AFC was not completely inconceivable from a liquidity stand-point.

Despite the enormous bailout in 1998, Chinese banks were still in poor shape at the end of Zhu's tenure in 2003. By that time, however, China's foreign exchange reserve had grown several fold, and the new leadership found a new way with which to bailout the major state banks: injections from the foreign exchange reserve. Within months of taking power, the Wen Jiabao Administration suddenly announced that the government would inject 45 billion dollars from the foreign exchange reserve to China

⁶⁹ Laurence W. Berger, George R. Nast, and Christian Raubach, "Fixing Asia's Bad-Debt Mess: A Banking Crisis Crippled Asia's Economies in 1997. A Bad Debt Crisis Threatens to Do So Again Unless Governments and Banks Crack Down on Nonperforming Loans," *McKinsey Quarterly* 2002, no. 139 (2002).

⁷⁰ Victor Shih, "Dealing with Non-Performing Loans: Political Constraints and Financial Policies in China," *The China Quarterly* (2005).

⁷¹ PBOC Monetary Policy Committee, "Zhongguo Renminyinhang Huobi Zhengce Weiyuanhui Diwuci Huiyi Jiyao (Summary of the Fifth Meeting of the PBOC Monetary Policy Committee)," in *Zhongguo Renmin Yinhang Huobi Zhengce Weiyuanhui Huiyi Jiyao (a Summary of Meetings of the PBOC Monetary Policy Committee)*, ed. PBOC Monetary Policy Committee (Beijing: China Finance Publisher, 2000).

Construction Bank and the Bank of China, the two state banks in the best condition.⁷² A further 15 billion dollar was later injected into the Industry and Commerce Bank of China, in combination with a 15 billion dollar allocation from the treasury.⁷³ In exchange for these funds, equity in the three banks was shifted to the Central Huijin Company, a state-owned holding company jointly run by the central bank and the ministry of finance (MOF).⁷⁴

After over 200 billion dollars in bailout, the technocrats pushed for listing the healthiest state banks in the international equity market in order to increase discipline in these banks. However, Chinese policy makers never contemplated ceding control over these banks either to the stock market or to MNFIs. While Chinese technocrats realized that limited cooperation with MNFIs was necessary to drum up interest in the IPOs, they made it clear from the beginning that MNFI ownership of Chinese banks would be tightly regulated. Under current regulations, no foreign bank can own more than 20% of a Chinese bank, and combined foreign ownership of a Chinese bank is restricted to below 25%. Although Newbridge Capital was able to gain de facto control over Shenzhen Development Bank (SDB) in 2003 by becoming the largest shareholder, SDB remains a relatively minor lender, and the Chinese government has shown no sign of allowing another such bid to succeed. Even after successful listing in Hong Kong, Temasek and Bank of America, the two strategic partners of China Construction Bank (CCB), held less than 15% of CCB shares. Besides these major cases, MNFIs have managed to acquire small stakes in a handful of small regional banks.

⁷² Haiyan Hu, "Zhongyang Huijin Gongsì Jinrong Bantu Qiemi (Unveiling the Secret Design of the Central Huijing Company)," *Zhongguo Qiyejia (Chinese Entrepreneur)*, 7/7 2005.

⁷³ China Economic Quarterly, "Understanding China's Bank Bailout."

⁷⁴ Victor Shih, "Beijing's Bailout of Joint-Stock and State-Owned Banks," *China Brief* 5, no. 18 (2005).

In December 2005, a consortium led by Citibank shocked the Chinese financial world by placing a bold 3 billion USD bid for some 85% of Guangdong Development Bank shares. The Guangdong Development Bank (GDB) had been a troubled mid-size regional bank that even State Council technocrats realized required inventive methods of recapitalization.⁷⁵ With the encouragement of both the Guangdong Provincial government and some central bureaucrats, Citibank placed a bid that well surpassed the existing limit on foreign ownership. Although the consortium included both foreign and Chinese entities, the bid called for 40% ownership by Citibank and 9.9% ownership by the other foreign partner, the Carlyle Group, which sums to an unprecedented 49.9% foreign ownership.⁷⁶ Citibank was by no means unaware of the unusual nature of its bid. It strategically invited a major Chinese state conglomerate to join the consortium, presumably to provide some political clout, and it asked former President Bush to write a letter to the Chinese government.

Although the China Banking Regulatory Commission (CBRC) gave preliminary approval in early 2006, the regulatory process bogged down with the annual meeting of the National People's Congress (NPC), where NPC delegates voiced complaints that bank assets were sold to foreigners "too cheaply."⁷⁷ When asked about the GDB deal at a March 12th NPC press conference, Premier Wen answered that the state should continue

⁷⁵ China Financial Net, *Lao Bushe Lijian Huaqi Yinhang Guangfahang Jinggou Zhizheng Yuelaiyue Weimiao (Senior Bush's Lobbying on Behalf of Citibank in the Bid for Guangdong Development Bank Brought About Interesting Development)* (cited).

⁷⁶ Yuan Li, "Huaqi Yinhang De Zhongguo Jinrong Zhanlue (Citibank's China Strategy)," *Jingji Cankaobao*, 2/6 2006, Yanzheng Lu, "Guangfa Feichang Congzu, Dianfu Zhongguo Shangye Yinhang Yinzi Chongzu Moshi (the Unusual Restructuring of Gdb Scambles the Usual Mode of Recapitalization and Restructuring in the Chinese Commercial Banking Sector)," *Caijing*, 10/5 2005.

⁷⁷ Kathy Chen, "Foreigners Face Backlash in China --- in an Echo of Beijing's Problems in the West, Criticism Grows of Overseas Investors' Influence on Its Home Turf," *Asian Wall Street Journal*, 4/3 2006.

to hold majority control in the process of “commercial banking reform.”⁷⁸ His wording indicated government unwillingness to cede majority control to foreign hands even for a bank like GDB. In official banking lexicon, “state-owned commercial banks” (*guoyoushangye yinhang*) refers to the Big Four state banks, while “commercial banks” (*shangye yinhang*) refers to all commercial banks in China. Soon after Wen’s comments, the Bush letter was leaked, and the CBRC circulated a memo stating that the government would not alter the rule governing foreign ownership in the case of GDB, in effect rejecting Citibank’s bid.⁷⁹

If examined in isolation, an outside observer might conclude that Chinese unwillingness to cede control over domestic bank stems from its enormous store of foreign exchange and its rapidly growing economy. With so much money, why does it need to place banks on the auction block. However, a comparison with banking policies in Mexico and Korea reveals that money is by no means the decisive factor. In the case of China, government elite has little incentive to sell domestic banks to MNFIs. First, senior officials in the party have a strong incentive to maintain control over the banking system in order to channel loans toward various political and policy demands.⁸⁰ Whether the selectorate is the Central Committee or just the Politburo, control over the banking sector allows top leaders to buy political support by disbursing preferential credit. Bank managers and bureaucrats who oversee the banks are junior officials in the party hierarchy and must obey the wishes of the Standing Committee. Although they can influence the agenda by providing information and policy alternatives, they have little

⁷⁸ Ibid.

⁷⁹ Xia, "Guangfahang Jinggouzhan: Yinjianhui Wuyi 'Puoxian' Huaqi Huo Gaifang'an."

⁸⁰ Shih, "Partial Reform Equilibrium, Chinese Style: Political Incentives and Reform Stagnation in Chinese Financial Policies."

direct leverage over senior officials. Outside of the party selectorate, no societal actor can threaten the leadership to nearly the same extent, at least relative to societal actors in Mexico and Korea.

Furthermore, although MNFIs often partnered with state owned financial institutions or large state-owned enterprises in their bids for Chinese banks, their Chinese partners at most have weak incentive to lobby for the sales, especially if the deals call for surpassing existing regulations. State-owned enterprises rely on the central government for a host of other subsidies in order to survive. They are thus reluctant to outright dispute the wishes of the State Council. Even if major SOEs are junior members of the elite selectorate, they have at most weak incentive to promote the sales, and they lack the leverage over national politicians that large conglomerates in Korea and Mexico have. Beyond that, MNFIs, which want to gain a toe-hold in China's financial market, have no political leverage against the Chinese government since they remain completely outside of the political system.

This is not to say that there is no impetus in the Chinese bureaucracy to push for increasing foreign participation in the Chinese financial market. First, some technocrats in the central government have long argued for a more competitive banking market, and they over time shifted the debate toward more foreign participation. The stronger impetus comes from the system of portfolio responsibility at the highest reaches of the regime. Essentially, every member of the Standing Committee of the Politburo is assigned a portfolio to oversee. They are vested with ultimate responsibility for the performance of that portfolio. Thus, holder of a given portfolio has an incentive to push for policy innovations in that portfolio to increase its significance and to bolster his or her

standing in the Standing Committee. However, even this incentive for policy innovation is balanced against the desire of the other Politburo members, each of whom is a member of the elite selectorate. One possible reason for the failure of the GDB deal is that the main elite proponent of banking reform, Vice-Premier Huang Ju in charge of banking reform, fell ill just before the NPC meeting, leaving banking policies in the hands of Premier Wen Jiabao. However, even if Huang had not fallen ill, he would not have risked Wen's anger by pushing for the deal. Without strong financial or factional interests at stake, triggering a dispute over such a minor issue would have made little political sense.

Conclusion

It is obviously not a novelty to use domestic selectorate or the structure of domestic capital to explain policy outcomes. Combining the two, however, yields some counterintuitive explanations about a country's willingness to sell banks to MNFIs. First, while large domestic capital in Mexico and Korea has a say over policies because they are members of the selectorate, private capital is excluded from the elite selection process in China. Thus, there is a sharp contrast between the composition of the selectorate in China and in Mexico and Korea, where voters, labor organizations and domestic capital loom large in the elite selection process. Although domestic Chinese capital is increasingly able to make its voice heard through lobbying, its exclusion from the selectorate renders its voice weaker than counterparts in the other two countries. As a

result, banking policies diverge further away from the ideal policies of domestic private capital in China than in the other two cases.

To the extent that industrial or financial interests are represented in the selectorate through Central Committee membership, they represent state owned entities with much weaker profit incentive than their private counterparts in Mexico and Korea. Instead, they are motivated by a mix of performance and political incentive. Moreover, in order for SOEs to do well they need a host of government subsidies and preferential policies.⁸¹ Although some CEOs of large state conglomerates are members of the Central Committee, the position hardly affords them political leverage vis-à-vis the senior leadership, who decides on their appointment in the first place. At most, they have access to the senior leadership and can lobby for a deal. However, this access is a far cry from the direct leverage that *grupos* and *chaebols* can exert on the political leadership in Mexico and Korea. Thus, even if MNFIs partnered with large state conglomerates in their bids for Chinese banks, the Chinese partners have weak incentive—and even weaker ability—with which to influence elite decision.

The structure of domestic capital also explains the varying outcomes between Mexico and Korea. Because bank ownership is concentrated in Mexico, it gives owners incentive to lobby for massive government bailouts in the aftermath of a financial crisis, with the goal of restoring the values of the banks and possibly selling them to MNFIs for a high price. In contrast, because major conglomerates only have small stakes in Korean banks, they lobby for government bailouts for an entirely different reason, to continue the flow of soft loan to large industrial conglomerates. Thus, although there is great political

⁸¹ Edward S. Steinfeld, *Forging Reform in China: The Fate of State-Owned Industry* (Cambridge, UK; New York: Cambridge University Press, 1998).

pressure for bank bailouts in Korea, there is much weaker impetus for selling banks to MNFIs. In this framework, the difficulty of foreign entry into China and Korea stems from two entirely different reasons. In the case of Korea, *chaebol* opposition probably played an important part. In the case of China, the continual dominance of the party hierarchy both in the higher reaches of the government and in the largest banks and industrial conglomerates excludes outside actors from the political process.

Beyond banking policy, the combination of political selectorate and business structure might explain policy outcomes in a wide range of areas, especially in privatization and regulatory policies. In order to explore its explanatory power, this framework needs to be fully fleshed out and tested on a wider range of cases. For example, further development of this approach requires a better classification of business structure and more rigorous thinking about how various conceptions of business structure, e.g. ownership type and ownership concentration, affects policy outcomes. In the mean time, MNFIs should not be surprised if Chinese technocrats are inaccessible. Their main job is to appease their political superiors, and until that changes, directly influencing Chinese policies will remain a difficult proposition for outsiders.

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