The Unlikely Revolutionary

Hyun-Sung Khang profiles Korean crusader **Jang Hasung**

JANG HASUNG'S crusade against the opaque accounting practices of Korean big business was almost derailed in its infancy by a fainthearted young lawyer. In 1998, Jang and his supporters filed a class action lawsuit against the Korean industrial powerhouse Samsung Electronics, accusing it of making illegal political donations and unlawful subsidies to a failing subsidiary. With limited funds, Jang was forced to use the services of a fellow activist—a recently minted young lawyer—to champion his cause. Samsung, for its part, had hired the best: "the king of litigation," as he was known in local legal circles. So, in a strongly Confucian culture in which seniority automatically confers additional authority, the plaintiff's young counsel faced the disadvantage of both youth and inexperience.

After the first hearing, the young lawyer approached Jang in despair and said, “This is an impossible game. The judges and other lawyers treat me like a child.” Jang, now dean of the business school at one of the country’s most prestigious education establishments, Korea University, laughs at the memory: “Such a huge imbalance!” he recalls, but then suddenly turns serious. Confronting defeatism before the case had even been heard, “I told him, ‘Look! *You* do it for the cause—justice. *He* does it for the money. That’s a huge difference. You have commitment. He just has incentive. So don’t worry.’”

Jang and his counsel went on to win that case: one of Korea’s first-ever lawsuits on behalf of minority shareholders against the directors of the industrial giant. The ruling marked a milestone in Korean corporate legal history. And the young attorney? “His name is in the law books now,” says Jang.

The same conviction and optimism Jang exhibited in 1998 have sustained him over more than a decade of campaigning for shareholder rights and better corporate governance when he faced threats to his safety, the loss of friends alienated by his activism, and accusations of selling out to foreigners.

The path to activism

Jang, 56, is an unlikely revolutionary, and his life could have been very different. After earning a Ph.D. in finance from the Wharton School of Business at the University of Pennsylvania, he could have disappeared into academic obscurity or a secure job for life at one of Korea’s leading industrial groups—the targets of his later activism. But on his return from the United States, he discovered a major lesson he had learned from his studies—that the primary aim of firms to increase value for their shareholders—did not, in his view, hold true for the giant industrial conglomerates that dominated Korea’s economy. Instead, these “chaebol” (see box) were run as personal fiefdoms by the company’s founders, without transparency or accountability.

“Everything was centered on one controlling person, whom they called ‘chairman’; sometimes they called him ‘owner.’ But if you look at the ownership structure, he is not the owner. He’s only a small, small minority shareholder, and that applied to most of the chaebol,” says Jang. “Where does his uncontested power come from? And why the abuse of this controlling power for his private benefit? [At the time] no one was raising the issue,” he recalls.

So Jang launched a crusade for greater accountability and transparency in the giant family-run conglomerates, which still dominate much of Korea’s economy. The action was organized under the auspices of a grassroots civic group Jang helped found—People’s Solidarity for Participatory Democracy (PSPD)—which is now one of the country’s leading nongovernmental organizations. Their weapon of choice: the class action minority shareholder lawsuit. The PSPD pushed for the appointment of outside directors, forced light onto opaque accounting practices, and demanded consideration for shareholders’ interests.

At the beginning of his activism, Jang describes himself as a “gadfly” on the elephantine body of the chaebol. The notion of shareholder rights barely existed in Korea at the time, nor was there an adequate translation of the term “corporate governance.” The law—which then required shareholders to own 5 percent of a company before bringing a motion to a shareholders meeting—created a huge barrier to challenging the might of the chaebol. The firms dismissed his early attempts to hold them accountable. A struggle with Korea First Bank stalled when the bank refused him access to board minutes, company papers, and shareholder registers. Unable to identify the atomized equity holders, Jang and his supporters took to the streets. Armed with placards, they marched in front of brokerage houses, calling on shareholders to make contact.

Jang’s campaign baffled many of his friends, relatives, and peers. In Korea’s close-knit society, many of them worked in the very companies he was challenging, and they pressured him to stop his rabble-rousing. He was branded antibusiness, anti-Korean, perhaps even communist—an accusation guaranteed to provoke suspicion and scorn.

Market believer

Far from being a communist, Jang holds an unconditional faith in markets, which he combines with a desire to promote the public good. “I love to make money,” he says. “There is nothing wrong with making money in a market system. If everyone involved is making money—shareholder, employees, society—and we make the company better and make society better, it’s a win-win-win game.”

The promotion of the public good may be a central motivation for Jang, but it is stripped of any ethical or moral language. Rather, his indignation lies in his belief that corruption in Korean firms is preventing market forces from functioning properly. Jang’s colleague John Lee describes the crusader as a “Western-style capitalist.” Lee says of his friend, “His view is that money is a driving force for change. It is not a justice kind of thing. It’s a belief that companies should make money and that the chairman should make money for the company.”

Jang has also benefited from being the right person in the right place at the right time. Certainly, the Asian financial crisis of 1997–98 came at the right time for Jang’s campaign. As his activism was taking off, the crisis shone an unprecedented spotlight on the accounting and management practices of the country’s chaebol and their role in precipitating the worst downturn in Korea’s modern history. It focused attention on the tangled web of cross holdings between the chaebol’s parent company and its subsidiaries, used to hide the unsustainability of subsidiaries and protect them from hostile takeovers. These subsidies and murky cross holdings had also given rise to unsustainable debt and conflicts of interest.

At the depth of the Asian slump, Jang targeted a plan by Samsung Electronics to provide debt guarantees to its ailing car manufacturing subsidiary. It was one issue of many that he and his followers wanted to raise during Samsung Electronics’ annual meeting in 1998—an event that has attained near totemic status among Korean civic activists involved in corporate governance. On that day, for more than 13 hours Jang and his supporters heckled and interrogated company directors more used to shareholder meetings as a rubber-stamping forum. The activists failed to resolve the Samsung Motors problem on that occasion, but Jang's wider actions and those of the PSPD triggered the beginnings of a move by some of Korea's family-run chaebol, such as SK Group and LG, to start separating their holding companies from their operating units.

Inevitably there have been setbacks: defeat in the courts, public incomprehension, and charges that the activists were undermining confidence in the Korean economy. But the gains of Jang and his supporters have been as much about changing corporate norms and public education as legal victories and defeats. The Asian crisis also helped precipitate the change in public opinion—many who had looked askance at Jang came to the slow realization that the chaebol must change or be forced to change. The liberal administration of Kim Dae-jung, voted into office in the early days of the crisis, embraced a swathe of corporate reforms, which continued under a second left-of-center administration. Those reforms included lowering the threshold to bring a motion to a shareholders meeting to 1 percent of shareholders then to 0.01 percent, establishing a requirement that one-quarter of directors be appointed from outside the company, a new securities law favoring minority shareholders, and tighter rules on disclosure, accounting, and board selection.

A history of fight

Given Jang's background, it is perhaps unsurprising he has fire in his belly. His family roots lie in the southern city of Kwanju—well known in Korea for its history of protest. One close family member died in the landmark 1980 mass demonstrations in his hometown against the military dictatorship of the time. The academic boasts an impressive pedigree. During Japanese colonization, his grandfather fought for Korean independence, while his grandfather's brother was involved in the military campaign against Japanese rule. As well as being a scion of a wealthy and well-educated family—"all his family members are Ph.D.s," a friend jokes—public service also runs in the family. An uncle and sister have held high government office, and he shoulders the responsibility conferred in Confucian culture on the eldest son.

Jang's own declared battle for the public good has transformed him from a protester on the sidelines to a respected public figure. But that growing respect again took a beating as he turned his fire away from the chaebol toward small and medium-sized companies. Jang credits the shift in his focus to an exchange with a European financier who spoke to him in a language they both understand—that of the market. The financier, whom Jang does not identify, told his Korean friend: "You seem to have a strategy to capitalize on undervalued assets. There are clearly assets [in Korea] which are mispriced,

The Republic of Chaebol

A Korean could spend an entire day living in the world of Samsung. In the morning, he might leave his Samsung-constructed apartment and drive to the office in his Samsung (Renault)-manufactured car while speaking on his Samsung cell phone. He might purchase lunch from a Samsung-owned department store and eat food produced and distributed by Samsung (Cheil Jedang), heated up in his Samsung-produced microwave while watching his Samsung television.

Such is the penetration of the chaebol in Korea that few aspects of life in this northeast Asian country have been left untouched by the sprawling influence of Korea's giant, family-founded corporations. The Samsung Group is just the largest and most powerful of them, accounting for about 20 percent of Korea's gross domestic product, earning it the moniker "the Republic of Samsung."

The chaebol are the channel for Korea's rapid economic development. Under the military dictatorship of Park Chung-hee in the 1970s and 1980s, the government provided the blueprint for industrial expansion; the chaebol carried it out. Under this system of guided capitalism, the government selected companies for industrial projects, fueled by low-interest loans from state-controlled banks. The reach of chaebol grew to include a broad range of industrial and service businesses protected from foreign competition and enjoying implicit government risk sharing and guarantees. Economically profitable activities wound up in the hands of a limited number of conglomerates.

Chaebol's highly centralized, autocratic management systems revolved around powerful founding chairmen and their immediate family members. The fate of these chaebol families—the nearest thing Korea has to royalty—is a source of endless public fascination. In several cases, the mantle of chairman is now being passed down to a third generation. The founding chairman's family typically maintains control of the business through cross ownership, even though its economic stake in the major group companies may have dwindled over time to less than 10 percent in many cases.

By the late 1980s, chaebol dominated Korea's industrial sector and were especially prevalent in manufacturing, trading, and heavy industry. They had started making strides into global markets, financed through cheap government credit and excessive leveraging. In 1997, on the eve of the Asian financial crisis, the debt-to-equity ratio of the top 30 chaebol exceeded 530 percent, often on short-term loans.

But that level of debt proved too much for many of them. The crisis heralded the demise of about half of the top 30 conglomerates. The surviving firms have drastically reduced their overall short-term and long-term debt financing, and, among the top 30 groups, new intragroup guarantees are no longer permitted and existing ones have been eliminated.

Koreans are deeply ambivalent about these homespun engines of growth. The egalitarian instincts of Koreans mean they have a deep suspicion of the controlling family's accumulation of wealth, but they also remain proud of the global success of the chaebol. They recognize that the fate of the country's export-driven economy hinges on the fate of the giant conglomerates—to such an extent that threats to rein in their influence and power are regularly met with warnings of dire consequences for the economy.

undervalued, and which are never capitalized. One of those undervalued assets is you." The financier challenged Jang to put his money where his mouth was and enter the private sector. "In this capitalistic market, unless you make money and show results, there is no persuasion power," he told the academic.

The seed was planted, but again Jang benefited from the fortuitous collision of right man, time, and place. While Jang was marching outside brokerage houses and appealing to small shareholders to come forward, he caught the attention of Lee, then an asset manager working in the United States. Intrigued by the activist, Lee made contact, and their friendship ensued. Lee supported Jang's campaign by delegating his voting rights to Samsung to give the campaigner a voice at shareholder meetings.

Making up the discount

A decade or so later, Lee, then with Lazard Asset Management, helped launch the company's Korea Corporate Governance Fund (KCGF) with an initial capitalization of about $35 million, according to Jang, who was recruited as its special advisor. That capitalization has now increased, he says, to $250 million, and so great is his brand recognition that the fund is known locally as the Jang Hasung fund. Its mandate: to unlock the value of small and medium-sized companies by improving the quality of their corporate governance and reversing the traditional undervaluation of Korean stocks, commonly described as the "Korea discount."

Korean stocks are widely thought to trade below their true value because of the higher risk investors assume to enter the country's stock market. This is frequently illustrated by the low price-earnings ratios of Korean stocks, compared with those in other markets. The discount is attributed to factors ranging from the risk posed by neighboring nuclear North Korea, to overleveraging at firms, to inefficiencies in the market. Jang thinks poor corporate governance is largely responsible. Improve a firm's governance, do away with the discount, and you reap benefit from the increased value of the company, his thinking goes.

KCGF's first investment was a 5.1 percent stake in a small textile company, Daehan Synthetic Fiber. The purchase was soon followed by demands that the company appoint outside directors, sell idle assets, and disclose transactions with affiliates. The fund requested access to the firm's shareholder register six times, and six times the firm refused. Finally, a court order forced the firm to capitulate.

Once labeled antibusiness, ironically, Jang's involvement with KCGF has forced him to deny accusations of profiteering. Jang protests, saying that he is committed to increasing the value of companies for the long term, even though the price of a company's stock can soar on the simple announcement of a share purchase by KCGF. Minutes after news of the purchase of Daehan equity, stocks in its parent company, Taekwang Industrial, hit their permitted daily ceiling, while the price of Daehan shares doubled in five days. Jang chalks up the rise to herd behavior. "In the space of a few minutes, what changes do you think we could make? Nothing changed on the company side. We only said, 'OK, we will work with the company.' Yesterday, today—it's the same company. It will take a number of days, months, even years to bring even a slight change."

In KCGF's short history, change has already involved considerable litigation as well as accusations of hostile and aggressive involvement in the operations of companies in which the fund buys shares. And despite the involvement, there is no guarantee of success. After buying shares in a local construction material firm, Byucksan, KCGF lost a shareholder vote and, against its wishes, saw the reinstatement of the chairman and auditor. KCGF later sold its holdings in the firm. "We gave up," says Jang. "There are companies where we want to bring changes and use all the weapons, including criminal cases or civil cases or any way we can that the law allows us. But by doing that, sometimes it destroys the value."

Jang is committed to increasing the value of companies for the long term.

The chaebol and the Korean business establishment have often charged Jang with being a conduit for opportunistic foreign predators more interested in making a quick profit than in corporate reform. Ninety-five percent of KCGF's investors are from overseas, but Jang says he deliberately avoids marketing the fund to local institutions, because their investment horizon is too short to allow him to meet the fund's objectives. Whereas investors in the West often look to accrue value over years, in Korea the average holding time for an institutional investor is months. "They would call me every week, every month, asking about profits," he says. For local investors Jang has this message: "If you are not patient enough, don't follow me, because over the short term nothing will change. It will take days, months, perhaps years."

Patience is a quality Jang has been forced to develop throughout his career as a crusader. Legal cases brought by Jang and his supporters have dragged on through numerous appeals and counterappeals, many lasting years. The original class action that Jang, his young lawyer, and the PSPD filed in 1998 against Samsung Electronics was not decided until 2001 by the district court, which awarded them damages of more than $72 million. Two years later, the court of appeals concurred with the lower court, but reduced the award to $16 million. Both the PSPD and Samsung appealed and the case went to the Supreme Court. The highest tribunal in the land backed the original decision and found in favor of Jang and his allies. The Supreme Court ruling in 2005 came seven years after the filing of the original suit. In this instance at least, Jang's conviction and optimism had finally paid off. ■

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