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Office Memorandum

To Ms Tseng

June 30, 1998

From J R Dodsworth *JD*

Subject **Background information for Supplementary Budget**

I have received the attached data from MOFE staff indicating the disaggregation of the revenue shortfall compared with the projection of the last mission. Also attached is a breakdown of unemployment related expenditures that shows implementation performance under the various programs through 27th of June.

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'98 National Tax Revenue Projection

(In trillion won)

	'97 11 (1st Prog)	'98 2	'98 4 (2nd QR)	'98 4 (3rd QR)
Total Tax Revenue	79 2	76 1	75 6	70 9
1 Internal Tax	57 5	55 3	55 7	51 9
① Income Tax	15 9	16 6	17 4	16 8
② Corporation Tax	8 5	6 1	6 1	8 8
③ Inheritance Tax	1 5	1 3	1 3	0 8
④ Asset Revaluation Tax	0 2	0 1	0 1	0 3
⑤ VAT	22 4	23 1	21 9	18 2
⑥ Special Consumption Tax	4 4	3 9	3 8	2 5
⑦ Liquor Tax	2 0	1 7	2 1	1 9
⑧ Telephone Tax	0 9	0 9	0 9	0 9
⑨ Securities Transaction Tax	0 3	0 3	0 3	0 2
⑩ Stamp Tax	0 4	0 4	0 4	0 3
⑪ Others	1 0	0 9	0 9	1 0
2 Transportation Tax	7 3	6 7	6 3	7 2
3 Customs Duties	6 5	6 8	6 8	5 5
4 Education Tax	6 7	6 2	6 2	5 3
5 Rural Development Tax	1 2	1 1	1 1	1 1

실업대책 추진실적(6.27 현재)

구분	Target			Implementation			비고	
	목표	실적	진도	목표	실적	진도		
합계	84,615	22,895	27.1	2,247	656.2	29.1		
Job Keeping	고용유지	17,536	8,126	46.3	444	200	45.0	
avoid lay-off	해고회피 노력지원	5,586	531	9.5	444	200	45.0	
credit guarantee	신용보증확증	1,000	500	50.0	-	-	-	235,500억 출연 (2023.08.08.까지)
housing	주택신용보증확증	3,000	3,000	100	-	-	-	(235,452억 보증)
extending maturity	외화대출 만기연장	7,950	4,095	51.5	(1,300개)	(555개)	(42.7)	환자순 무담환과
Job Creation	고용창출	19,444	8,224	42.3	270	75	27.8	
public work	공공근로사업	5,444	1,380	25.5	270	75	27.8	전일 참가인원 36천명(우천)
Kepto	한전 송배전시설 투자확대	6,000	6,000	100	-	-	-	송인액 기준
Venture business	벤처기업창업지원 등	1,000	844	12.1	-	277개	-	창업지원 772억 대체지원 72억
	SW벤처기업 지원	1,000		접수	6,227	73		
Training	직업훈련과 취업알선	7,634	2,502	32.8	339	133.1	39.3	
unemployed	실업자 직업훈련 등	5,255	2,245	42.7	282	130.3	46.2	
workers training	재직자 고용유지훈련	1,919	52	2.7	57	2.8	4.9	
Job matching	구인 구직 연계제제 확충	460	205	44.6	-	-	-	고용안정센터(22) 인력은행(8) 증설
Social care	실업사 생활보호	40,001	4,043	10.4	1,194	248.1	20.8	
unemployed benefit	실업급여지급	17,001	2,702	15.9	513	198	38.6	
lending	실직자 내부	20,800	443	2.1	370	7	1.9	
(bond)	(고용안정채권 발매)	(16,000)	(2,954)	(18.5)	-	-	-	실직자대부사업 지원
	지소득실직자생계보호	2,000	667	33.4	310	41.8	13.5	
lending to those who want to return to rural areas	귀농자 영농창업지원	200	231	115	1	13	130	농기업경영자금 200억 포함
	(국민연금 대부)	(10,000)	(3,049)	(30.5)	(250)	(90)	(36.0)	비에산사업

national pension loans to unemployed

The data in parentheses are not included in the total



Office Memorandum

To Mr Severino

June 29, 1998

From Hubert Neiss 

Subject **Korea Bank-Fund Collaboration**

A Fund mission will be in Seoul on July 8-22 to conduct the discussions for the Third Quarterly Review and to negotiate a new letter of intent. Since the Bank is taking the lead in some key areas which also impact the Fund-supported reform program, there needs to be close collaboration between our staffs regarding the commitments (and timeframe) we will be seeking from the authorities. The three main areas of focus for this review are financial sector restructuring, corporate restructuring and the social safety net.

To ensure close and effective collaboration, we have requested Bank staff to provide input to the letter of intent on financial sector and corporate restructuring. At a coordinating meeting on June 19 between Messrs Schweitzer, Aghevi, and Ms Tseng, Fund staff requested, and Bank staff agreed to provide, a matrix of measures and timing that could be incorporated in to the Fund's letter. However, this matrix was not provided by the promised date and we were told subsequently that it would not be possible to supply a matrix at this stage or even later (July 11) in the field, by the time the Fund expects to start the negotiations on the LOI. Bank staff have indicated that they would keep the Fund mission fully informed on their discussions with the authorities and that some input in broad terms would be possible towards the end of the Fund mission. The Bank team is working toward a SAL in early October.

I would stress that this review is important for the Fund, particularly because the market have been skeptical of the authorities efforts at corporate restructuring so far and are expecting some significant actions soon to restructure the chaebols. There is a serious risk that market sentiment will deteriorate further if a framework for debt work outs is not in place shortly along with a concrete plan for restructuring the debt of the largest chaebols. President Kim has also been keen to move ahead quickly and has been pressing the bureaucracy and the chaebols for actions. Given market expectations and the authorities' own need to show results, I am concerned that the Bank's time table is too slow.

In light of these considerations, it is of critical importance that a World Bank staff member join the mission and be in position to provide input to the letter of intent on (i) financial sector restructuring, (ii) corporate restructuring, and (iii) the social safety net. I would like to extend this invitation and hope you will be able to meet our request.

✓HN
cc. WT
KMM
Div. 5



Office Memorandum

To Ms Coorey
Mr Gordon

June 27, 1998

From J R Dodsworth *(JD)*

Subject **Korea Credit Guarantee Fund**

Attached some data on KCGF operations which may be useful

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1. 신용보증업무현황

(Credit Guarantee Performance)

단위: 백만원

in million won

연월말 End of	기본재산 Total Capital funds	보증승낙 Acceptance of guarantee		보증해지 Invalid guarantee		보증잔액 Guarantee outstanding	
		건수 Cases	금액 Amount	건수 Cases	금액 Amount	건수 Cases	금액 Amount
		1979	111,995	16,683	678,832	15,350	386,170
1980	134,029	34,936	1,701,670	27,921	1,200,623	23,062	1,265,236
1981	137,566	38,856	1,841,597	35,132	1,552,599	27,388	1,357,618
1982	112,278	34,449	1,549,028	33,893	1,735,643	27,942	1,357,615
1983	161,552	31,757	1,385,980	33,684	1,434,380	26,015	1,310,218
1984	198,933	31,613	1,649,129	30,515	1,409,397	27,113	1,649,950
1985	255,150	33,982	1,870,701	29,518	1,525,125	31,577	1,895,526
1986	304,675	40,215	2,236,469	34,015	1,811,633	37,777	2,320,362
1987	387,908	38,470	2,371,191	30,762	1,912,013	45,448	2,779,540
1988	473,719	44,722	2,726,555	33,747	2,225,771	56,423	3,280,324
1989	578,344	47,227	3,047,786	35,270	2,466,617	62,490	3,969,499
1990	622,546	56,278	4,522,433	40,656	3,148,298	79,112	5,230,628
1991	680,452	62,392	5,221,522	45,909	3,857,046	95,595	6,595,104
1992	578,906	63,569	5,419,065	56,507	4,854,173	102,657	7,169,996
1993	504,276	65,633	6,386,694	55,956	5,002,621	132,400	8,244,170
1994	549,224	55,015	4,441,991	64,200	5,221,244	123,221	7,664,817
1995	528,079	69,521	5,727,332	65,790	5,201,168	126,952	8,190,981
1996	687,834	92,080	6,755,202	74,785	5,699,660	144,247	9,246,523
1997	705,283	95,857	8,314,662	72,421	6,232,565	167,892	11,328,620
1997							
1		2,574	268,467	2,546	289,082	144,455	9,226,007
2		7,789	566,488	4,829	368,925	147,615	9,425,140
3		10,839	858,269	6,273	505,556	157,181	9,777,853
4		10,714	988,752	5,359	698,749	156,536	10,167,656
6		0,480	003,363	6,300	610,000	159,006	10,462,150
6		2,777	327,989	7,200	744,451	162,100	10,709,698
7		7,663	649,428	5,576	496,212	164,253	10,853,914
8		7,003	592,537	4,382	410,143	166,874	11,036,308
9		7,791	618,254	6,178	497,711	168,487	11,156,851
10		7,225	549,697	7,691	663,616	168,031	11,122,032
11		7,252	649,176	6,099	492,807	169,184	11,179,300
12		6,780	778,253	8,077	628,922	167,892	11,328,620
1998							
1		6,460	640,707	4,370	390,220	169,974	11,563,107
2		11,774	1,067,363	6,488	642,410	175,200	12,110,120
3		11,478	931,880	7,881	625,018	178,857	12,416,982

* 1970년 7월 1일 기준 합계
 순계기본재산 28,722백만원
 순계보증신액 101,623백만원
 98년 3월말 현재까지 보증잔액 중 중소기업(중견기업 포함)분은 178,650천에 12,350,415백만원임

3. 보증종류별 (Credit Guarantee)

연월일	총 계		대출보증		지급보증의보증		사채보증		납세보증		
	Total		Guarantees for loans		Guarantees for payment guarantees of banks		Guarantees for bond issues		Guarantees for tax and duty payments		
	건수 Cases	금액 Amount	건수 Cases	금액 Amount	건수 Cases	금액 Amount	건수 Cases	금액 Amount	건수 Cases	금액 Amount	
1985	31,511	1,895,528	28,314	1,264,227	231	33,717	545	39,887	403	5,730	
1986	37,777	2,320,362	33,485	1,621,096	151	43,311	627	428,935	826	9,366	
1987	45,148	2,779,540	40,554	2,059,485	123	18,661	637	413,884	557	6,368	
1988	58,423	3,280,324	51,182	2,532,762	136	14,301	618	381,081	18	1,486	
1989	63,490	3,856,493	58,067	3,045,660	128	13,902	615	394,050	14	1,139	
1990	79,117	5,230,628	73,052	4,240,434	137	15,783	689	428,656	5	683	
1991	95,595	6,595,104	89,723	5,436,185	129	19,278	548	444,682	10	1,145	
1992	102,657	7,169,896	95,108	5,870,585	140	20,949	539	438,052	71	935	
1993	132,406	8,544,070	124,603	7,235,544	120	17,136	600	411,540	6	1,475	
1994	123,221	7,664,817	115,937	6,478,273	142	17,457	449	364,107	4	1,341	
1995	126,962	8,190,981	118,443	6,973,118	191	25,413	386	299,936	3	1,052	
1996	144,247	9,246,523	134,597	7,982,468	203	28,734	324	255,499	10	1,409	
1997	107,892	11,328,620	154,887	9,756,383	271	40,093	301	236,043	15	1,992	
7	164,253	10,867,914	152,331	9,311,697	231	32,531	311	248,694	10	1,477	
8	166,814	11,030,308	154,732	9,541,700	233	33,316	307	246,338	13	1,956	
9	168,407	11,156,851	166,098	9,646,355	234	35,066	309	247,632	11	1,567	
10	168,031	11,122,932	155,411	9,602,251	232	34,830	305	243,680	13	1,694	
11	169,184	11,179,300	159,351	9,648,225	232	34,793	305	242,130	13	1,919	
12	167,892	11,328,620	164,887	9,756,383	221	40,093	301	236,043	15	1,992	
1998	1	169,974	11,595,167	156,670	9,981,427	221	39,813	205	233,370	18	2,836
2	173,260	12,110,120	161,339	10,442,607	219	42,413	299	232,178	26	5,233	
3	178,857	12,410,982	164,442	10,725,642	211	41,101	291	229,808	29	5,542	

신용보증현황

(Performance by Type)

in million won

어음보증 Guarantees for bills		제2금융보증 Guarantees for loans for nonbanking financial institutions		시설대여보증 Guarantees for leases		이행보증 Guarantees for performance		무역어음인수 담부부족 Guarantees for acceptance of trade bills		End of
건수 Cases	금액 Amount	건수 Cases	금액 Amount	건수 Cases	금액 Amount	건수 Cases	금액 Amount	건수 Cases	금액 Amount	
441	61,832	750	65,098	737	81,207	158	5,848	—	—	1985
562	75,485	883	74,394	989	77,024	265	9,791	—	—	1986
1,145	95,879	988	86,310	1,220	92,456	224	9,493	—	—	1987
1,329	120,272	1,587	130,608	1,351	92,827	203	7,980	—	—	1988
1,364	141,103	1,766	149,398	1,390	101,349	156	9,194	1	100	1989
1,459	177,014	2,085	206,867	1,630	152,020	163	8,520	12	1,651	1990
1,588	211,720	2,600	270,708	1,840	211,004	142	15,408	15	1,092	1991
1,592	220,998	3,297	351,254	1,859	247,381	83	8,902	18	2,140	1992
1,750	254,279	4,466	561,974	1,863	257,509	48	8,818	14	1,795	1993
1,831	261,540	5,000	300,094	1,818	243,768	21	7,763	11	1,474	1994
2,613	361,889	7,074	317,347	1,891	219,898	16	6,983	5	480	1995
3,702	404,787	8,900	343,271	1,441	174,126	67	10,842	3	298	1996
5,700	642,345	5,357	454,055	1,318	170,608	36	17,681	2	450	1997
5,056	598,666	4,817	419,469	1,406	161,325	88	19,506	3	550	I
5,179	607,953	4,917	424,892	1,395	159,252	96	20,453	2	450	A
5,286	610,341	5,047	434,038	1,380	158,265	110	23,137	2	450	B
5,439	620,585	5,139	442,013	1,379	155,151	111	22,278	2	450	C
5,562	630,921	5,243	448,846	1,356	152,928	109	20,988	3	550	N
5,700	642,345	5,352	454,955	1,318	170,608	36	17,681	2	450	D
5,831	656,940	5,530	472,771	1,294	177,064	113	20,396	2	450	I 1998
6,156	682,819	5,831	508,533	1,273	172,937	117	22,520	0	0	F
6,427	687,681	6,070	525,032	1,245	168,479	135	23,637	1	100	M

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4. 금액별 신용보증현황

(Credit Guarantee Performance by Amount)

in million won

연월말	총계		5천만원 이하		1억원 이하		3억원 이하		
	Total		50million won or less		100million won or less		300million won or less		
	업체수	금액	업체수	금액	업체수	금액	업체수	금액	
	No. of firm	Amount	No. of firm	Amount	No. of firm	Amount	No. of firm	Amount	
1990	43,098	5,230,628	33,688	904,509	4,693	393,361	3,951	777,824	
1991	52,280	6,595,104	36,421	1,129,324	9,014	530,956	4,947	999,158	
1992	55,129	7,159,998	37,169	1,241,834	7,969	649,145	5,364	1,048,751	
1993	76,160	8,544,070	55,405	1,985,483	9,061	809,244	6,011	1,182,056	
1994	10,129	7,664,817	50,427	1,795,850	9,138	828,414	5,505	1,081,514	
1995	76,439	8,190,901	52,688	1,896,785	12,243	1,103,659	6,561	1,299,571	
1996	93,519	9,248,523	65,195	2,392,272	14,641	1,323,141	9,650	1,702,295	
1997	107,808	11,328,820	70,883	2,095,323	18,631	1,708,116	12,161	2,353,820	
	8	107,517	11,036,308	71,694	2,709,912	18,132	1,661,351	11,878	2,279,988
	9	108,501	11,156,851	71,671	2,768,304	18,688	1,672,129	11,893	2,327,986
	10	108,207	11,122,932	71,275	2,717,384	18,875	1,676,285	11,959	2,340,717
	11	100,689	11,179,300	77,472	2,748,868	18,977	1,693,938	12,086	2,353,248
	12	107,808	11,328,820	70,883	2,095,323	18,531	1,708,116	12,161	2,353,820
1998	1	108,485	11,585,167	69,705	2,711,530	18,785	1,721,534	12,542	2,440,110
	2	108,042	12,110,120	69,397	2,752,482	18,424	1,781,469	13,315	2,590,002
	3	111,214	12,416,982	70,004	2,706,683	20,332	1,823,789	13,823	2,685,027

연월말	5억원 이하		10억원 이하		15억원 이하		15억원 초과		
	50million won or less		1 billion won or less		1.5 billion won or less		1.5 billion won or more		
	업체수	금액	업체수	금액	업체수	금액	업체수	금액	
	No. of firm	Amount	No. of firm	Amount	No. of firm	Amount	No. of firm	Amount	
1990	1,591	657,329	1,561	1,128,288	485	613,635	353	756,684	
1991	1,680	768,044	1,853	1,225,985	748	981,597	411	902,036	
1992	2,052	834,997	1,930	1,396,340	809	1,032,392	436	956,539	
1993	2,166	881,588	2,176	1,561,474	837	1,055,090	504	1,092,135	
1994	1,974	804,804	1,943	1,338,208	756	949,858	306	806,159	
1995	1,819	741,230	1,972	1,423,305	830	1,044,542	226	682,859	
1996	1,909	807,071	2,001	1,446,921	785	985,560	298	609,273	
1997	2,692	1,118,826	2,494	1,853,283	709	999,053	338	693,199	
	8	2,568	1,053,898	2,448	1,816,759	688	877,106	311	624,286
	9	2,583	1,071,297	2,474	1,838,154	678	865,282	310	629,310
	10	2,608	1,082,541	2,474	1,838,601	675	864,835	301	611,789
	11	2,607	1,081,931	2,477	1,848,782	685	860,818	305	603,935
	12	2,692	1,118,826	2,494	1,853,283	709	899,053	338	693,199
1998	1	2,818	1,173,083	2,500	1,917,991	735	925,619	341	694,294
	2	3,064	1,276,965	2,712	2,018,095	772	970,582	358	720,525
	3	3,193	1,331,057	2,772	2,060,133	784	984,709	366	735,596

5. 지역별 신용보증 현황

(Credit Guarantee Performance by Province)

in 100 million won

단위: 억원											
연월일	전국	서울	인천 경기	부산 경남	대구 경북	광주 전남	강원	충북	대전 충남	전북	제주
End of	Total	Seoul	Incheon & Kyonggi	Pusan & Kyong Nam	Taegu & Kyong Buk	Kwangju & Jeon Nam	Kang Won	Chung Buk	Taegu & Ching Nam	Jeon Buk	Jeju
1989	38,565	10,561	12,052	5,965	4,137	1,473	714	844	1,821	1,056	142
1990	52,300	13,426	16,610	8,035	5,716	1,990	1,031	1,183	2,552	1,507	257
1991	69,951	16,551	20,436	10,238	7,380	2,688	1,386	1,730	3,302	1,835	375
1992	71,500	18,216	21,910	10,821	7,648	3,024	1,601	2,068	3,756	1,893	465
1993	85,441	22,278	25,230	12,371	9,913	3,705	1,802	2,458	4,284	2,328	622
1994	76,648	20,848	22,825	10,742	8,717	3,203	1,640	2,151	3,865	2,096	561
1995	81,910	22,658	24,546	11,647	9,046	3,357	1,533	2,094	4,303	2,156	576
1996	92,165	26,088	27,713	12,857	10,779	3,890	1,790	2,180	4,682	2,386	656
1997	113,786	33,308	33,206	15,814	12,155	5,129	2,041	2,671	5,265	2,912	791
1998											
10	92,556	26,170	27,734	12,896	10,779	3,869	1,751	2,229	4,865	2,358	665
11	92,764	26,271	27,669	12,889	10,332	3,866	1,781	2,198	4,687	2,417	655
12	92,466	26,088	27,713	12,857	10,223	3,890	1,790	2,180	4,682	2,386	656
1997											
1	92,260	26,081	27,623	12,802	10,271	3,800	1,803	2,156	4,659	2,352	654
2	94,251	26,709	28,241	13,113	10,438	3,895	1,847	2,182	4,793	2,392	641
3	91,178	27,789	29,442	13,514	10,772	4,073	1,907	2,257	4,898	2,464	682
4	101,679	29,210	30,681	14,913	11,074	4,260	1,922	2,350	5,035	2,539	689
5	104,522	30,073	31,409	14,302	11,348	4,467	1,966	2,435	5,180	2,641	731
6	107,007	30,655	32,055	14,721	11,568	4,672	2,049	2,574	5,241	2,724	748
7	108,539	31,283	32,499	14,867	11,663	4,731	2,083	2,634	5,248	2,766	767
8	110,369	31,895	33,032	15,076	11,841	4,883	2,122	2,644	5,314	2,816	780
9	111,569	32,120	32,853	15,230	11,961	4,976	2,113	2,666	5,320	2,837	793
10	111,228	32,882	32,610	15,403	11,958	5,014	2,080	2,601	5,204	2,877	776
11	111,793	33,144	32,467	16,566	11,842	5,085	2,081	2,645	5,189	2,890	784
12	113,286	33,308	33,206	15,814	12,166	5,173	2,041	2,671	5,265	2,912	791
1998											
1	115,852	33,841	34,087	16,202	12,477	5,221	2,055	2,722	5,409	2,959	799
2	121,101	35,411	35,824	16,737	13,137	5,420	2,072	2,808	5,608	3,069	819
3	124,170	36,202	36,536	17,010	13,399	5,626	2,115	2,926	5,888	3,210	858

FUND

Industrial Bank of Korea

The Korean Development Bank

Abusing and commercial Bank

(Credit Guarantee The export-import Bank of Korea)

단위 백만원

연월일	총계 Total	특수은행						장기신용은행
		기업은행	국민은행	한국산업은행	한국주택은행	수출입은행	Specialized Bank	
1989	3,059,551	689,468	446,306	23,301	8,879	22,316	122,681	
1990	4,256,211	864,780	600,117	26,524	16,721	55,828	129,023	
1991	5,455,556	1,073,200	817,936	55,911	34,878	73,658	123,664	
1992	6,893,876	1,088,408	955,560	94,036	41,100	84,688	109,892	
1993	7,254,483	1,485,302	1,405,157	67,708	44,943	77,166	115,281	
1994	8,497,204	1,239,849	1,327,414	57,891	34,390	81,578	105,263	
1995	8,998,991	1,215,231	1,635,594	66,191	38,461	57,429	108,510	
1996	7,991,500	1,548,969	1,799,561	51,751	42,725	50,943	92,194	
1997	4,795,906	2,128,144	1,882,124	73,267	76,408	94,656	97,397	
8	9,575,466	1,981,691	1,980,323	66,645	62,252	62,888	101,768	
9	9,681,923	2,009,868	1,974,940	66,883	63,899	84,828	99,256	
10	9,638,028	2,031,318	1,884,845	65,471	67,561	66,816	98,148	
11	9,724,269	2,072,413	1,878,435	65,070	71,001	67,905	99,755	
12	9,795,906	2,128,144	1,887,124	73,267	76,406	94,656	97,397	
1998	1	9,854,052	2,183,378	1,927,305	69,937	83,725	92,273	
2	10,480,887	2,312,717	2,044,009	69,142	92,093	88,791	91,494	
3	10,762,836	2,403,912	2,107,941	61,196	98,003	85,581	90,425	

Korea long-term credit bank

연월일	Hanmi	Donghae	Daegu	Daegu	Hankook	Daegu	Daegu	Daegu	Daegu	Daegu
	하이은행	동화은행	내곡은행	동남은행	하나은행	보림은행	정파은행	부산은행	충청은행	Changhaeng Bank
1989	40,776	6,235	2,135	6,678	-	-	-	58,661	21,774	
1990	69,614	52,023	54,126	34,753	-	-	-	86,379	39,824	
1991	80,775	80,677	65,515	58,113	-	-	-	122,156	53,372	
1992	101,032	92,481	67,271	82,105	24,023	13,873	-	134,378	52,328	
1993	120,761	89,149	90,450	120,207	50,828	22,238	-	144,489	57,892	
1994	126,098	75,401	92,641	115,005	62,616	27,765	24,482	126,831	65,212	
1995	141,349	11,561	141,307	127,867	85,855	40,457	23,678	139,252	76,617	
1996	158,160	84,968	201,240	173,696	107,366	52,459	36,517	149,787	86,800	
1997	209,354	122,088	297,462	251,148	135,938	76,435	53,648	180,112	106,090	
8	199,034	119,939	270,264	244,220	133,083	70,826	36,938	180,582	106,750	
9	203,914	123,461	282,261	250,153	132,646	72,064	61,668	179,085	111,080	
10	204,116	124,250	281,240	257,534	133,459	74,129	53,775	181,871	110,105	
11	209,101	125,190	298,969	259,113	135,547	76,095	53,900	179,632	109,052	
12	209,354	122,088	297,462	251,148	135,938	76,435	53,648	180,112	106,090	
1998	1	207,466	120,054	288,402	262,502	130,217	78,211	185,667	104,045	
2	215,675	121,516	300,409	275,214	141,562	79,576	61,641	193,416	114,333	
3	211,571	119,122	305,242	279,561	143,703	85,904	64,666	197,810	116,240	

주: 내국보증과 지급보증의 보증 및 무역어음인수납보증 등이 한계임

신용보증현황

Performance by Bank

the commerce bank of Korea
Cheil Bank
Hanil Bank
Seoul Bank
Foreign Exchange Bank of Korea
Shinhan Bank

Nation wide Commercial Banks							End of
Chohenny	시	중	은	행			
조흥은행	한국산업은행	제일은행	한일은행	서울은행	한국외환은행	신한은행	
201,934	165,027	202,771	166,001	212,350	160,078	122,423	1989
275,477	235,154	288,348	209,981	282,274	192,254	198,499	1990
303,809	298,450	373,491	259,766	298,796	227,455	217,928	1991
312,601	288,354	424,844	279,277	286,240	260,364	323,280	1992
341,012	298,719	509,005	334,124	287,951	320,197	392,528	1993
297,731	263,109	473,840	319,792	240,848	285,664	372,888	1994
313,978	257,436	485,524	341,135	221,743	298,076	370,238	1995
304,146	295,917	512,241	367,461	232,414	323,620	401,148	1996
448,034	347,513	584,233	403,089	264,758	353,875	479,400	1997
479,305	313,894	578,688	421,874	275,646	368,963	445,187	A
482,875	379,431	584,839	422,121	279,113	370,007	440,702	S
485,479	382,279	580,663	418,758	278,626	370,833	447,432	O
495,960	388,187	579,803	423,375	278,994	374,000	452,259	N
501,527	388,026	569,259	410,690	276,070	373,748	452,063	D
517,286	386,425	555,948	417,050	271,440	378,044	460,168	J
552,864	415,874	580,038	440,492	271,819	397,553	495,194	F
580,594	429,431	578,528	451,313	268,244	402,755	519,112	M

Local Banks								외국은행	End of
방	주	주	전	간	간	충	대	Foreign Banks in Korea	
안주은행	제주은행	경기은행	전북은행	강원은행	경남은행	충북은행	대구은행		
35,594	6,374	93,075	14,968	16,140	66,746	11,909	100,486	17,531	1989
58,591	12,536	160,834	25,546	27,834	99,369	18,480	140,366	22,523	1990
71,730	15,796	259,150	30,230	38,155	136,280	25,245	167,558	31,837	1991
79,290	15,802	233,091	30,772	49,227	144,836	28,780	170,027	25,534	1992
99,411	20,295	223,775	37,747	56,094	184,143	29,949	209,983	42,244	1993
87,657	20,741	169,491	34,938	50,327	135,238	24,285	175,586	13,734	1994
94,606	22,735	165,431	34,008	45,166	147,922	26,832	178,240	12,753	1995
112,714	23,218	188,100	38,731	52,894	161,285	28,588	208,752	7,129	1996
137,747	26,204	224,302	43,462	60,627	184,755	33,175	240,002	7,684	1997
145,319	27,845	231,540	45,320	72,663	189,001	35,545	252,509	5,948	A
160,330	29,294	233,058	47,805	72,787	191,416	35,202	254,267	7,279	S
160,236	29,279	231,061	48,251	72,961	192,803	36,025	254,167	6,449	O
164,521	28,879	231,935	46,838	74,057	192,451	35,487	255,089	5,949	N
167,485	29,704	231,177	40,780	71,123	192,446	35,051	255,343	5,949	D
161,647	30,202	234,420	47,892	70,404	195,832	34,329	273,701	5,849	J
172,175	30,169	267,886	48,724	74,271	201,475	33,938	294,678	5,649	F
182,828	32,832	283,881	52,823	74,982	206,053	33,919	298,724	5,649	M

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WT
KMM
Div. 5



Office Memorandum

June 27, 1998

To Ms Conroy
Mr Gordon

From I R Dodsworth *IRD*

Subject **Korea Credit Guarantee Fund**

Attached some data on KCGF operations which may be useful This is the most recent data which was published on June

98 JUN 29 10 31 AM '98

1. 신용보증업무현황

(Credit Guarantee Performance)

in million won

연월말 End of	기본재산 Total Capital funds	보증승낙 Acceptance of guarantee		보증해지 Invalid guarantee		보증잔액 Guarantee outstanding	
		건수 Cases	금액 Amount	건수 Cases	금액 Amount	건수 Cases	금액 Amount
1979	111,995	18,683	678,832	15,350	386,170	16,645	700,788
1980	134,629	34,938	1,761,070	27,921	1,206,623	23,662	1,255,235
1981	137,566	38,856	1,841,597	35,132	1,552,599	27,386	1,357,618
1982	112,278	34,149	1,549,078	33,893	1,735,643	27,942	1,357,615
1983	161,582	31,757	1,385,980	33,684	1,433,390	29,015	1,319,210
1984	192,933	31,813	1,649,129	30,515	1,409,397	27,113	1,549,950
1985	232,150	32,982	1,079,701	39,519	1,575,125	31,611	1,852,526
1986	304,675	40,215	2,236,469	34,015	1,811,633	37,777	2,320,362
1987	387,908	38,470	2,371,191	30,762	1,912,013	45,448	2,779,540
1988	479,710	44,722	2,726,555	33,747	2,225,771	66,423	3,280,324
1989	578,344	42,337	3,042,786	35,270	2,466,617	63,490	3,884,493
1990	622,546	56,278	4,522,433	40,658	3,149,299	79,112	6,239,628
1991	680,452	62,392	5,221,622	45,909	3,857,048	95,595	6,595,104
1992	578,906	63,569	5,419,085	56,507	4,854,173	102,657	7,159,996
1993	504,278	85,633	6,386,694	55,956	5,002,621	132,406	8,544,070
1994	549,224	55,015	4,441,991	64,200	5,221,244	123,221	7,664,817
1995	528,079	69,521	5,727,332	65,790	5,201,168	126,952	8,190,981
1996	687,834	92,080	6,755,202	74,785	6,699,660	144,247	9,248,523
1997	705,283	95,857	8,314,662	72,421	6,232,565	167,892	11,328,620
1997	1	3,574	268,467	3,546	788,983	144,455	9,226,007
	2	7,789	665,468	4,829	366,335	147,615	9,425,140
	3	10,639	858,269	6,273	506,556	162,181	9,777,853
	4	10,714	988,752	6,359	598,749	156,536	10,167,856
	5	9,460	903,363	6,300	619,089	159,696	10,462,160
	6	9,767	992,999	7,326	744,451	162,166	10,700,698
	7	7,883	649,428	5,576	496,212	164,253	10,853,914
	8	7,003	592,537	4,382	410,143	166,874	11,036,308
	9	7,791	618,254	6,178	497,711	168,487	11,156,861
	10	7,225	549,697	7,681	583,616	168,031	11,122,932
	11	7,252	549,175	6,099	492,807	169,184	11,179,300
	12	6,780	778,263	8,072	628,933	167,892	11,328,620
1998	1	6,460	649,767	4,378	393,220	169,974	11,585,167
	2	11,774	1,067,363	6,488	542,410	175,260	12,110,120
	3	11,478	931,880	7,881	625,018	178,857	12,416,982
	4	11,028	991,193	9,763	882,030	180,122	12,546,145

주 1976년 7월 1일 기준 창립시
 순계기본재산 28,722백만원
 순계보증잔액 101,623백만원
 • 98년 4월말 현재의 보증잔액 중 중소기업(중견기업 포함)분은 179,931건에 12,487,152백만원임

2 업 종 별 신

(Credit Guarantee Performance)

단위 백만원

연월일	총 계		광 업		소 계		제 조					
	Total		Mining & quarrying		Sub-Total		음식료품		섬유제품		의복 및 모피제품	
	업체수	금 액	업체수	금 액	업체수	금 액	업체수	금 액	업체수	금 액	업체수	금 액
1992	55,729	7,159,998	764	46,291	36,815	6,291,323	1,428	312,346	3,817	535,097	2,438	252,360
1993	76,180	8,544,070	278	45,937	49,328	6,319,201	1,649	342,183	5,255	644,866	3,257	297,879
1994	70,129	7,664,817	221	41,307	45,407	5,691,183	1,395	285,621	4,888	814,618	2,908	276,996
1995	76,439	8,190,981	200	38,452	49,738	5,860,465	1,395	284,858	5,171	621,055	2,848	275,628
1996	93,519	9,245,523	218	44,467	56,070	6,744,780	1,469	298,341	5,458	588,494	3,174	288,506
1997	107,808	11,328,620	207	50,632	60,748	7,102,514	1,594	316,937	6,558	821,769	3,364	324,355
9	108,601	11,156,851	313	50,830	61,606	7,072,245	1,677	319,730	6,721	821,036	3,462	331,538
10	108,207	11,122,332	305	49,688	61,238	6,993,351	1,619	318,202	6,658	800,074	3,401	328,771
11	108,889	11,179,308	214	50,037	61,429	6,986,051	1,616	313,618	6,646	802,237	3,420	327,407
12	107,808	11,328,620	207	50,632	60,748	7,102,514	1,594	316,937	6,558	821,769	3,364	324,355
1998 1	106,486	11,685,167	217	51,041	61,072	7,241,099	1,606	321,046	6,572	826,404	3,375	325,891
2	109,042	12,114,170	214	55,946	62,330	7,545,604	1,648	338,445	6,689	845,014	3,438	341,870
3	111,274	12,416,882	217	58,351	62,671	7,713,624	1,686	348,963	6,546	848,066	3,419	347,170
4	116,446	12,545,145	233	54,530	63,119	7,750,561	1,722	354,074	6,576	848,600	3,416	345,255

연월일	Manufacturing											
	고 구 및 플라스틱제품		비금속 광물제품		제 1 차 금속산업		조 림 금속제품		타 리 분류되지 않은 기계및장비		기 타 제조업	
	업체수	금 액	업체수	금 액	업체수	금 액	업체수	금 액	업체수	금 액	업체수	금 액
1992	2,304	300,216	1,811	350,788	1,250	304,743	4,049	572,231	5,999	609,716	7,755	1,113,062
1993	3,162	427,711	1,982	398,800	1,582	336,273	6,041	693,889	8,083	778,328	10,439	1,354,521
1994	2,903	382,064	1,741	345,447	1,436	298,194	5,712	591,952	7,923	723,287	9,425	1,105,296
1995	3,065	406,776	1,624	322,962	1,508	296,614	6,388	652,539	10,628	897,691	10,135	1,237,361
1996	3,581	445,658	1,582	319,123	1,625	311,175	7,347	719,112	12,508	1,041,718	11,630	1,328,262
1997	3,877	496,894	1,669	366,337	1,719	349,658	8,091	874,890	14,673	1,283,222	11,842	1,477,807
9	4,254	496,135	1,716	361,889	1,704	342,766	8,427	828,654	14,093	1,107,738	12,059	1,577,293
10	3,914	479,281	1,704	360,895	1,746	340,657	8,452	827,293	14,204	1,180,140	12,134	1,564,315
11	3,909	478,911	1,695	359,965	1,745	339,007	9,192	839,278	13,804	1,197,916	11,957	1,627,480
12	3,877	486,884	1,669	365,337	1,719	349,658	8,091	874,890	14,673	1,283,222	11,842	1,477,807
1998 1	3,898	500,337	1,685	371,043	1,734	380,742	8,087	861,498	14,812	1,328,748	11,904	1,508,944
2	3,967	520,925	1,732	387,477	1,772	375,547	8,211	894,047	15,103	1,377,178	12,205	1,577,219
3	4,013	539,121	1,764	394,846	1,791	389,443	8,265	907,413	15,128	1,404,216	12,320	1,610,757
4	4,056	547,399	1,780	397,727	1,801	393,349	8,328	903,807	15,280	1,408,972	12,379	1,627,664

• 92년도 이후는 한국표준산업 분류의 개칭 시행에 따라 재 편제한 농계임

3. 보증종류별 (Credit Guarantee)

단위: 백만원

연월합	총 계		대출보증		지급보증의보증		사채보증		납세보증		
	Total		Guarantees for loans		Guarantee for payment guarantee of bank		Guarantees for bond issues		Guarantees for tax and duty payments		
	건수 Cases	금액 Amount	건수 Cases	금액 Amount	건수 Cases	금액 Amount	건수 Cases	금액 Amount	건수 Cases	금액 Amount	
1985	31,577	1,895,526	28,314	1,264,277	231	33,717	545	397,887	403	5,730	
1986	37,777	2,320,362	33,485	1,621,056	151	24,311	621	429,935	825	9,368	
1987	45,448	2,779,540	40,554	2,059,489	123	16,001	637	413,084	657	6,368	
1988	68,423	3,780,324	51,182	2,532,762	135	14,301	618	380,081	18	1,485	
1989	63,490	3,856,493	58,067	3,045,650	128	14,902	615	394,658	14	1,139	
1980	79,112	5,230,626	73,032	4,240,434	137	16,783	509	428,656	5	683	
1991	96,695	6,595,104	88,723	5,436,186	129	18,278	548	422,882	10	1,145	
1992	102,657	7,159,996	95,108	5,870,585	140	20,949	639	436,662	21	935	
1993	132,408	8,544,070	124,603	7,235,544	126	17,130	500	411,540	6	1,475	
1994	123,221	7,664,817	116,937	6,478,273	142	17,457	449	353,107	4	1,341	
1995	128,952	8,190,981	118,983	6,973,118	191	26,413	386	299,936	3	1,062	
1996	144,247	9,246,523	134,597	7,962,460	203	28,734	324	255,488	10	1,400	
1997	167,892	11,328,620	154,887	9,755,363	221	40,093	301	236,043	15	1,992	
8	168,874	11,038,308	154,732	9,541,700	233	33,316	307	246,336	13	1,956	
9	169,487	11,156,851	156,008	9,646,355	234	35,066	309	247,632	11	1,587	
10	169,031	11,172,932	155,411	9,602,751	232	34,830	305	243,680	13	1,694	
11	169,184	11,179,300	155,351	9,648,225	232	34,793	305	242,130	13	1,919	
12	167,892	11,319,620	154,887	9,755,363	221	40,093	301	236,043	15	1,892	
1998	1	169,974	11,585,167	156,670	9,981,427	221	39,913	295	233,370	18	2,836
2	173,260	12,110,120	161,339	10,442,887	219	42,413	299	232,178	26	5,233	
3	178,857	12,416,882	164,442	10,725,642	211	41,101	297	229,808	29	5,542	
4	180,122	12,546,145	165,235	10,821,976	205	42,388	291	225,058	28	5,885	

신용보증현황

(Performance by Type)

in million won

어음보증		제2금융보통		시설내여보증		이행보증		무역어음인수 담보보증		Kind of
Guarantees for bills		Guarantees for loans for nonbanking financial institutions		Guarantees for leases		Guarantees for performance		Guarantees for acceptance of trade bills		
건수	금액	건수	금액	건수	금액	건수	금액	건수	금액	
Cases	Amount	Cases	Amount	Cases	Amount	Cases	Amount	Cases	Amount	
441	61,832	750	65,098	737	61,207	156	6,848	—	—	1985
552	75,485	883	74,394	989	77,024	255	9,791	—	—	1986
1,145	95,879	988	88,310	1,220	92,466	274	9,493	—	—	1987
1,329	120,272	1,547	130,806	1,351	92,827	203	7,990	—	—	1988
1,364	141,103	1,755	149,398	1,390	101,349	156	9,194	1	100	1989
1,459	177,014	2,085	206,867	1,630	162,020	163	9,620	12	1,651	1990
1,598	211,720	2,600	276,708	1,840	211,604	142	15,489	15	1,092	1991
1,592	220,998	3,297	351,254	1,859	247,381	83	9,902	18	2,140	1992
1,790	268,779	3,466	351,974	1,863	267,609	48	9,818	14	1,795	1993
1,831	261,540	3,008	300,094	1,818	241,768	21	7,163	11	1,414	1994
2,603	361,868	3,074	312,342	1,691	209,000	16	6,980	5	460	1995
3,702	463,787	3,900	343,271	1,441	174,126	67	16,947	3	298	1996
5,100	642,345	5,352	454,955	1,318	179,698	96	17,681	2	460	1997
5,179	607,053	4,017	424,802	1,305	150,272	96	20,453	2	450	A
5,286	610,341	5,047	434,098	1,290	159,265	110	23,137	2	450	S
5,439	620,585	5,139	442,013	1,379	155,151	111	22,278	2	450	O
5,562	630,921	5,243	446,046	1,366	152,920	109	20,888	3	560	N
5,700	642,345	5,352	454,955	1,318	179,698	96	17,681	2	450	D
5,831	666,940	5,530	472,771	1,294	177,064	113	20,395	2	450	J 1998
6,156	682,610	5,831	500,533	1,273	172,037	117	22,520	0	0	Γ
6,427	697,691	6,070	525,037	1,245	168,429	135	23,637	1	100	M
6,703	714,348	6,314	547,056	1,202	162,762	142	26,572	1	100	A

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4. 금액별 신용보증현황

(Credit Guarantee Performance by Amount)

다위 백만원

in million won

연월말	총 계		5천만원 이하		1억원 이하		3억원 이하		
	Total		50million won or less		100million won or less		300million won or less		
	업체수 No. of firm	금액 Amount	업체수 No of firm	금액 Amount	업체수 No of firm	금액 Amount	업체수 No. of firm	금액 Amount	
1990	46,098	5,230,628	33,568	904,509	4,693	383,361	3,951	111,824	
1991	62,280	6,596,104	36,477	1,128,324	6,014	630,958	4,047	968,158	
1992	55,729	7,159,998	37,169	1,241,834	7,989	649,145	5,364	1,048,751	
1993	76,160	8,544,070	55,405	1,965,483	9,081	808,244	6,011	1,182,056	
1994	70,129	7,664,917	50,427	1,795,880	9,138	828,414	6,606	1,081,614	
1995	76,439	8,190,961	52,668	1,895,766	12,243	1,103,689	6,561	1,299,571	
1996	93,519	9,246,523	65,185	2,392,272	14,641	1,323,141	8,060	1,702,285	
1997	107,808	11,328,620	70,883	2,695,373	18,531	1,708,116	12,181	2,383,820	
9	108,501	11,156,861	71,671	2,758,304	18,888	1,672,129	11,893	2,322,366	
10	108,207	11,122,932	71,276	2,717,384	18,876	1,676,286	11,999	2,340,717	
11	104,689	11,174,300	72,572	2,748,868	18,977	1,693,938	12,086	2,353,248	
12	107,808	11,328,620	70,883	2,695,323	18,531	1,708,116	12,181	2,383,820	
1998	1	106,486	11,595,167	69,705	2,711,530	18,765	1,721,534	12,542	2,440,116
2	108,042	12,110,120	69,397	2,752,482	19,424	1,781,489	13,315	2,590,002	
3	111,274	12,416,987	70,004	2,796,688	20,332	1,823,783	13,823	2,665,027	
4	116,446	12,546,145	75,424	2,786,252	19,875	1,832,955	14,139	2,749,717	

연월말	5억원 이하		10억원 이하		15억원 이하		15억원 초과		
	500million won or less		1 billion won or less		1.5billion won or less		1.5billion won or more		
	업체수 No. of firm	금액 Amount	업체수 No. of firm	금액 Amount	업체수 No. of firm	금액 Amount	업체수 No. of firm	금액 Amount	
1990	1,597	667,329	1,551	1,128,286	486	613,636	353	755,684	
1991	1,880	788,044	1,863	1,339,986	748	961,697	411	902,036	
1992	2,052	834,997	1,830	1,396,340	809	1,032,392	436	956,639	
1993	2,166	881,688	2,176	1,561,474	837	1,055,090	504	1,082,136	
1994	1,974	804,804	1,943	1,398,208	758	948,858	386	806,159	
1995	1,819	741,720	1,972	1,423,305	830	1,044,542	328	682,959	
1996	1,969	807,071	2,001	1,446,921	766	966,660	298	609,273	
1997	2,692	1,118,826	2,494	1,853,283	709	896,053	338	693,199	
9	2,583	1,071,297	2,474	1,838,154	678	865,262	316	629,319	
10	2,608	1,082,541	2,474	1,838,601	678	864,636	301	601,769	
11	2,607	1,081,931	2,477	1,846,762	666	860,618	306	603,936	
12	2,692	1,118,826	2,494	1,853,283	709	896,053	338	693,199	
1998	1	2,818	1,173,083	2,580	1,917,991	735	920,619	341	694,284
2	3,064	1,276,965	2,712	2,018,095	772	970,582	358	720,626	
3	3,193	1,331,057	2,772	2,080,133	784	984,703	366	735,596	
4	3,235	1,350,349	2,828	2,106,730	775	971,835	370	747,812	

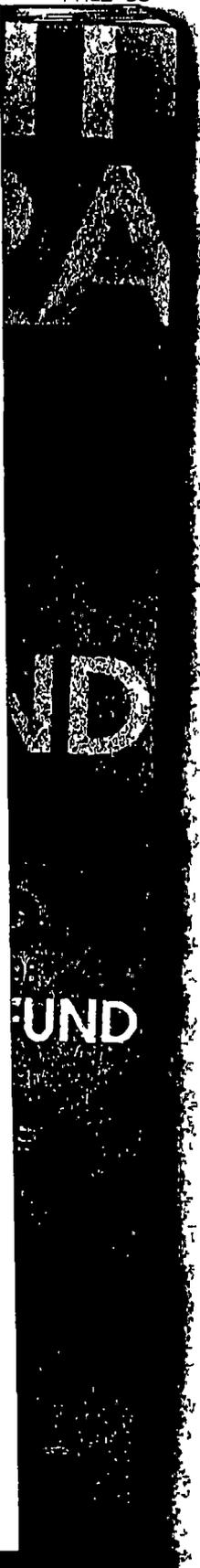
5. 지역별 신용보증현황

(Credit Guarantee Performance by Province)

단위: 억원

in 100 million won

연월	전국	서울	인천 경기	부산 경남	대구 경북	광주 전남	김천 경원	충북	대전 충남	전북	제주
of	Total	Seoul	Incheon & Kynggi	Pusan & Kyng Nam	Daegu & Kyng Buk	Kwangju & Jeon Nam	Kang Won	Chung Buk	Taegon & Chung Nam	Jeon, Buk	Jeju
3	38,566	70,561	12,057	5,965	4,137	1,473	714	844	1,821	1,056	142
4	52,306	13,426	16,810	8,036	5,716	1,990	1,031	1,183	2,652	1,507	257
5	69,951	16,651	20,436	10,238	7,380	2,888	1,386	1,730	3,332	1,836	375
6	71,600	18,216	21,910	10,821	7,848	3,024	1,601	2,066	3,756	1,803	465
7	85,441	22,278	25,230	12,371	9,913	4,706	1,802	2,458	4,284	2,328	622
8	76,648	20,848	22,825	10,742	8,717	3,203	1,640	2,161	3,865	2,096	561
9	81,910	22,659	24,546	11,642	9,046	3,357	1,533	2,084	4,303	2,156	576
10	92,466	26,088	27,713	12,857	10,223	3,890	1,790	2,180	4,082	2,366	656
11	113,286	33,308	33,206	15,814	12,155	5,123	2,041	2,671	5,265	2,912	791
12	92,704	26,271	27,659	12,889	10,332	3,865	1,701	2,198	4,681	2,417	655
1	92,466	26,088	27,713	12,857	10,223	3,900	1,790	2,180	4,682	2,366	656
2	92,280	26,081	27,629	12,807	10,271	3,860	1,803	2,155	4,659	2,352	654
3	94,251	26,709	28,241	13,113	10,438	3,896	1,841	2,182	4,793	2,392	641
4	97,778	27,789	29,442	13,514	10,772	4,073	1,907	2,257	4,898	2,484	602
5	101,679	29,210	30,687	13,913	11,074	4,260	1,922	2,350	5,036	2,539	689
6	104,522	30,073	31,409	14,302	11,348	4,461	1,966	2,436	5,160	2,641	731
7	107,007	30,656	32,055	14,721	11,568	4,672	2,049	2,571	5,241	2,724	748
8	109,539	31,283	32,499	14,867	11,663	4,731	2,083	2,634	5,248	2,766	761
9	110,363	31,895	32,032	15,026	11,841	4,893	2,122	2,644	5,314	2,816	780
10	111,569	33,120	32,653	15,230	11,961	4,976	2,113	2,566	5,320	2,837	793
11	111,229	32,862	32,510	15,403	11,958	5,014	2,080	2,601	5,204	2,822	775
12	111,793	33,144	32,467	15,566	11,942	5,085	2,081	2,045	5,189	2,890	784
1	113,286	33,308	33,206	15,814	12,155	5,123	2,041	2,671	5,265	2,912	791
2	115,852	33,841	34,087	16,202	12,477	5,221	2,055	2,722	5,489	2,959	799
3	121,101	35,411	35,824	16,737	13,137	5,420	2,072	2,806	5,806	3,069	819
4	124,170	36,202	36,936	17,010	13,399	5,626	2,116	2,926	5,868	3,210	858
5	126,461	36,478	37,338	17,089	13,418	5,863	2,122	2,958	5,971	3,296	942



6. 은행별

(Credit Guarantee

연월일	총계 Total	Specialized Bank					
		기업은행 Industrial Bank of Korea	국민은행 Citizen Bank	한국산업은행 The Korean Development Bank	한국주택은행 Housing and Commercial Bank	수출입은행 The Export-Import Bank of Korea	장기신용은행 Korea long term Credit Bank
1989	3,059,551	689,468	445,305	23,301	6,879	22,316	122,594
1990	4,256,217	864,200	600,117	26,524	16,721	55,828	128,023
1991	5,455,556	1,073,225	817,936	55,911	34,878	71,658	127,664
1992	5,893,676	1,088,408	955,580	94,036	41,100	84,688	104,892
1993	7,264,483	1,485,302	1,405,157	67,708	44,943	77,166	116,281
1994	6,497,204	1,238,849	1,327,414	67,891	34,390	61,678	105,283
1995	6,999,991	1,215,234	1,635,594	66,191	38,467	57,429	106,510
1996	7,991,600	1,546,969	1,799,567	61,751	42,726	58,943	92,194
1997	9,796,900	2,120,144	1,882,124	73,267	76,406	54,656	97,397
9	9,681,923	2,008,868	1,974,940	68,893	63,899	64,628	89,256
10	9,634,028	2,031,318	1,884,845	66,471	61,561	65,816	88,148
11	9,724,259	2,072,413	1,878,435	66,070	71,001	67,905	89,755
12	9,795,806	2,128,144	1,882,124	73,267	76,406	94,656	97,397
1998 1	9,654,052	2,183,378	1,927,305	69,937	83,725	92,273	95,187
2	10,480,887	2,312,717	2,044,609	69,142	92,093	88,791	91,484
3	10,782,836	2,403,912	2,107,941	61,198	98,003	85,587	90,425
4	10,862,890	2,489,754	2,080,154	57,116	95,239	89,070	86,745

연월일	한미은행	동화은행	대동은행	중앙은행	하나은행	보림은행	경희은행	부산은행	지창은행
	1989	49,726	5,235	2,135	6,678	—	—	—	58,567
1990	69,014	52,023	54,126	34,753	—	—	—	89,379	38,624
1991	80,775	88,677	85,515	59,113	—	—	—	122,156	53,372
1992	101,032	92,481	67,271	82,105	24,023	13,873	—	134,378	62,528
1993	120,761	98,149	80,456	120,287	50,828	22,238	—	144,460	57,602
1994	126,096	75,401	92,541	115,005	62,616	27,766	24,482	126,831	55,212
1995	147,349	77,561	141,307	127,867	85,855	40,457	29,678	136,252	75,517
1996	159,161	94,968	201,240	173,696	107,366	52,459	38,517	149,787	86,800
1997	208,354	122,080	297,462	257,148	135,938	76,435	54,846	180,112	106,090
9	203,914	123,461	282,261	250,153	132,646	72,064	51,588	179,085	111,080
10	204,116	124,250	291,240	257,534	133,459	74,129	53,775	181,871	110,106
11	200,101	125,190	289,969	258,113	135,547	75,095	53,900	179,632	109,052
12	209,354	122,086	297,462	257,148	135,938	76,435	54,846	180,112	106,090
1998 1	207,466	120,054	288,462	262,592	139,212	78,211	53,988	185,661	104,046
2	216,675	121,516	300,409	275,214	141,582	79,576	57,541	193,416	114,330
3	217,577	119,122	305,242	279,561	143,703	85,984	54,666	197,810	116,240
4	219,306	113,846	305,394	281,041	142,401	88,921	54,821	193,397	118,258

수 대출보증과 지급보증의 보증 및 무역어음인수담보보증을 합계임

신용보증현황

Performance by Bank

Chohung *The commercial Bank of Korea* *Cheil* *Hanil* *Seoul* *The Foreign exchange bank of Korea* *Shinhan Bank*

in million won

Nation-wide Commercial Banks							End of
조흥은행	한국상업은행	제일은행	안림은행	서울은행	한국외환은행	신한은행	
201,934	166,521	202,771	166,881	212,360	169,078	122,423	1989
275,477	235,154	288,348	209,981	262,274	192,264	198,499	1990
303,809	298,450	373,491	250,766	296,796	227,465	271,928	1991
312,601	288,354	424,844	279,272	285,240	260,364	323,280	1992
341,012	298,719	509,006	334,124	287,951	320,197	392,578	1993
297,731	263,109	473,840	318,782	240,848	285,664	374,888	1994
313,978	257,438	485,524	341,136	221,743	208,076	370,238	1995
384,146	295,917	512,241	367,461	732,414	323,620	401,148	1996
448,034	347,513	584,233	403,089	264,758	363,625	428,400	1997
482,875	379,431	684,839	422,121	278,113	370,687	448,702	S
464,419	382,279	680,663	419,756	278,626	370,833	447,432	O
495,900	388,187	679,803	423,375	278,994	374,000	452,259	N
501,527	388,026	660,260	410,090	278,070	373,748	452,063	O
517,286	396,425	655,948	417,060	271,448	378,944	469,168	J
552,864	415,874	684,038	440,492	271,819	397,653	496,194	F
580,584	429,431	678,528	461,313	268,244	402,785	518,112	M
600,097	445,927	682,166	455,311	268,330	412,937	521,628	A

Daegu *Cheju* *Kyungso* *Cheong* *Bankwon* *Local Banks* *Daegu* *Foreign Banks in Korea*

대구은행	제주은행	경기은행	전북은행	강원은행	충남은행	충북은행	대구은행	외국은행	End of
35,594	6,374	99,075	14,988	16,140	68,746	11,909	100,486	17,531	1989
58,591	12,538	160,934	25,546	27,834	99,359	19,480	140,365	22,523	1990
71,730	15,796	259,160	30,230	30,155	135,280	25,245	167,668	31,831	1991
79,298	15,802	333,691	30,772	49,277	144,836	28,760	170,627	25,534	1992
99,411	20,285	223,775	37,747	58,094	164,143	24,949	208,983	42,244	1993
87,657	20,741	169,491	34,939	60,377	135,238	24,285	175,686	13,734	1994
94,606	22,735	165,431	34,008	46,165	147,822	26,897	178,240	12,763	1995
112,714	23,218	188,100	38,731	52,094	101,285	28,588	208,762	7,129	1996
137,747	26,204	224,302	43,462	69,677	184,755	33,176	240,662	7,684	1997
160,330	29,204	233,050	47,806	72,787	191,416	36,202	254,267	7,279	S
164,235	28,279	231,061	48,252	72,961	182,903	36,025	254,167	5,449	O
160,821	29,879	231,935	46,838	74,057	192,451	35,487	255,089	5,949	N
181,485	29,704	231,177	49,780	71,123	192,446	35,051	258,343	5,849	U
161,647	30,202	234,420	47,892	70,404	195,897	34,329	273,701	5,849	J
172,176	30,169	267,886	48,724	74,271	201,475	33,938	294,678	5,649	F
182,628	32,632	283,881	52,823	74,981	206,053	33,019	298,324	5,049	M
193,951	38,559	287,458	54,415	74,060	207,210	33,857	296,238	5,449	A



Office Memorandum

To Mr Neiss

June 26, 1998

From James Gordon *JG*

Subject **Korea—State Department Conference**

I attended a U S State Department Conference on June 22 on Korea (schedule attached), where I presented an overview of the current economic situation. The conference was off the record and I spoke candidly. Besides describing the severity of the downturn, I noted

- President Kim Dae-Jung's push for reforms faced opposition from key interest groups (including the bureaucracy). The recent "death list," which did no little more than give the appearance of reform, illustrated these difficulties,
- Japan was the biggest source of risk to the growth forecast because Japanese and Korean exports compete so closely. If the yen was to remain weak, and exports were not to lead recovery in Korea, fiscal stimulus would have to be considered,
- The "costs" of Korean unification had increased significantly relative to the South's ability to borrow (spreads on the sovereign bond over U S Treasuries were currently 450–460 basis points, compared to pre-crisis levels of 50–100 basis points)

After my presentation, I stayed on for the rest of the morning session. There was a general sense among participants that President Kim Dae-Jung represented an unprecedented opportunity for improving inter Korean relations. The financial crisis seemed to be having indirect effects on the North e.g., Southern tourists had stopped travelling to the Chinese border areas. In addition, Jeff Frankel of the CEA made the following remarks

- Given the crisis in South Korea, it was fortunate that unification was not occurring now. Not only was the South weak, but the national angst it was experiencing might confuse North Koreans about market economics,
- Korea was unlikely to be able to choose the starting date for unification, but it could influence its speed and sequencing. Professor Frankel advocated a 5-year transition period during which there would be free flows of trade and capital, but not of labor, and an opportunity for North Koreans to assimilate market economics.

Attachment

cc Ms Tseng, Ms Kelly, Mr Collyns, Ms Coorey

Bureau of Intelligence and Research
Office of Research
U S Department of State
National Intelligence Council

PRELIMINARY AGENDA

THE TWO KOREAS PROSPECTS FOR ECONOMIC EXCHANGE AND ECONOMIC INTEGRATION

System Planning Corporation
30th Floor, USA Today Building
1000 Wilson Boulevard
Arlington (Rosslyn), Virginia 22209
(703) 351-8200

MONDAY, JUNE 22, 1998

- 8 30 a m **Registration and Coffee**
- 9 00 a m **Opening Remarks**
John Gannon, National Intelligence Council
William Brown (Chairperson and Moderator), National Intelligence Council
- 9 30 a.m **Overview of Economic Situation**
South Korean Economic Situation
North Korean Economic Situation
James Gordon, International Monetary Fund
- 10 00 a m **Panel Discussion**
- 10 20 a m **Break**
- 10 30 a m **Applying Economic Integration Theory to Korea's Future**

What are the theoretical and practical economic issues involved in opening the two Koreas to economic exchanges and eventual economic integration? What gains and challenges present themselves? What are some analogies—compare Hong Kong-China NAFTA, EU, Israel-Jordan? Do corporations act in regional or pan-national interest? Competition issues Must the North and South have compatible economic systems (WTO-like or much tighter EU-like) for orderly integration to occur? What are the policy issues and economic considerations associated with gradual integration versus shock unification—i.e., South Korean takeover?

Jeff Frankel, Council of Economic Advisors

ALL REMARKS ARE OFF THE RECORD AND NOT FOR ATTRIBUTION

11 00 a m **Panel Discussion**

11 20 a m **Assessing the Current Status of Economic Exchange**

How is South Korea organizing itself for integration/unification? New government's new policies How does Pyongyang respond? What is the nature and extent of North-South trade? What trends, commodities, rules and regulations are typical of current trade practices? What is the nature of South Korean and Chaebol investment interests in North Korea? How does North Korea's debt problem affect such transactions?

Scott Snyder, U S Institute for Peace

✓ 12 00 p m **Working Lunch -- Council on Foreign Affairs Report on North Korea**

Robert Manning, Council on Foreign Affairs

Afternoon Sessions David Gordon (Moderator) National Economic Council

1.15 p m **Economic Cost and Benefits of Unification**

Compare shock unification versus gradual integration

Marcus Noland, Institute for International Economics

1 45 p m **Break**

1 55 p.m **Economic Forces for Integration-What Should we Watch, What Can We Do?**

Are there ways to measure the pressure, i e , relative price differences, comparative advantages, rate of return on capital, infrastructure, i e , cross DMZ electricity, oil pipelines, etc ?

Nicholas Eberstadt, American Enterprise Institute

2 10 p m **Break**

2 20 p m **Historical/Cultural Forces For/Against Economic Integration**

Pre-1945 economic relationship, i e , industrial north agricultural south, land ownership issues, regionalism—are there cross cutting rivalries/coalitions, i e , far SW—far NE versus Seoul? Education issues, religious issues, divided family issues

David Steinberg, Asia Foundation (TBC)

✓ 2 45 p m **Panel Discussion**

ALL REMARKS ARE OFF THE RECORD AND NOT FOR ATTRIBUTION

3 20 p m Break

3 30 p m China, Japan, and Russia Perspectives

Will Japanese firms compete with South Korea for North Korean resources, labor? Potential for landbridge—China/South Korea Russia/South Korea, Russia/EU-Japan? Integrated Korea a threat or an advantage to C/J/Russia, or don't care?

Katy Oh, Institute for Defense Analysis

4 00 p m Panel-US Policy, How (and how not) to Work for Korean Integration

Discuss—food aid, KEDO nuclear power project KEDO heavy fuel oil, sanctions, IMF/World Bank, market developments in North Korea leverage on North Korea, leverage on South Korea, leverage on China

William Brown, National Intelligence Council
K A Namkung, The Atlantic Council
John Merrill, U S Department of State (Discussant)
Joseph Winder, Korean Economic Institute (Discussant)

4 45 p m Adjournment

Confidential

APD
ECO/EDR(98)12



Organisation de Coopération et de Développement Economiques
Organisation for Economic Co operation and Development

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19 Jun 1998
24 Jun 1998

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ECONOMICS DEPARTMENT
ECONOMIC AND DEVELOPMENT REVIEW COMMITTEE

ECO/EDR(98)12
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PARIS

1997-1998 ANNUAL REVIEW - KOREA

The attached draft Economic Survey of Korea is submitted to the Economic and Development Review Committee for consideration

The Annual Review of Korea by the Economic and Development Review Committee has been arranged for 10 July 1998. The examining countries are Australia and Germany

The tables, figures, the annexes and the statistical annex will be circulated separately

It should be noted that the Korean authorities did not have the opportunity to comment on this draft before it was circulated

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Document complet disponible sur OLIS dans son format d'origine

FONDS MONETAIRE INTERNATIONAL
64/66, Avenue d'Iéna
75116 PARIS

Or En



Office Memorandum

cc FOSS
RM
SC
DS

To Mrs Tseng

June 26, 1998

From Sean Hagan ~~SH~~ (LEG)

Subject **Korea—Briefing Paper for the Third Quarterly Review Under the Stand-By Arrangement**

The Legal Department's only comment is marked on the attached page

Attachment

cc FAD, MAE PDT, RES, STA, and TRE
Messrs Schweitzer, Scott, Lierberman, Qureshi, World Bank

98 JUN 25 PM 11 36

Box 2 Deleveraging of Large Corporations

Reducing debt equity ratios of the large corporations is an essential element of corporate restructuring. At end 1997 debt equity ratios of the top 30 chaebols stood at 604 percent (including financial affiliates) compared with industrial country norms of about 100–200 percent. The magnitude of the effort needed to reduce debt equity ratios to these levels is demonstrated by an illustrative exercise prepared by the World Bank. Under favorable assumptions the standard restructuring options would reduce the debt equity ratio to only about 340 percent in two years. Reduction of debt equity ratios beyond this level requires some form of additional restructuring in the form of debt/equity swaps, debt write down, or equity injections.

Options for Reducing Debt Equity Ratios of the 30 Largest Chaebols

	Debt (W bil)	Equity (W bil)	Debt Equity Ratio	Assumptions
Stock at end-1997	456.3	75.6	604	
Standard options				
Increase in retained earnings		3.7		Based on 1996 financial performance
Domestic equity issues 1/	8.3	8.3		Based on issuance during 1989–96 and stock market capitalization of W 100–W 120 trillion
Offshore equity issues 1/	5.3	5.3		Based issuance over past year
Debt/equity conversions by banks	16.0	16.0		Banks hold equity up to legal limit (15 percent)
Chaebols under court supervision	48.6	1.9		Debt and equity of these chaebols are excluded
Foreign investment/asset sales 1/ ~	12.0			Based on transactions to date during 1998
Subtotal	366.1	106.9	343	

Source: World Bank.

1/ All proceeds used to retire debt.

liberalization of short-term capital movements, the mission will discuss the possibilities for bringing forward prudential regulations on short-term foreign borrowing and foreign exchange exposures, and on monitoring and reporting requirements. It will also review progress on the authorities' efforts to strengthen the reporting of off-balance sheet foreign currency-denominated exposure of financial institutions and to submit legislation to improve corporate sector external debt data reporting. The mission will also review the progress in developing an early warning system based on external vulnerability indicators.

The mission will also ensure that the proposed law is consistent with Korea's obligations under Article VIII of the Fund's Articles



Office Memorandum

98 JUN 25 PM 4:48

cc: FOSS
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To: Ms. Tseng

June 26, 1998

From: J. Ferran (PDR)

Subject: **Korea--Briefing Paper for the Third Quarterly Review Under the Stand-By Arrangement**

While we agree on the need to adjust the program, we have serious concerns about the proposed floor for the fiscal deficit and the monetary policy stance, as well as some questions about the extent of the downward revision to the output forecast.

Fiscal Policy Issues

1. While it may be inevitable to accept a widening in the fiscal deficit, we think the brief goes too far in actually recommending a *floor* on the deficit. I personally feel strongly that it is not our business to tell the authorities to go for a fiscal deficit higher than the one they themselves seem to consider appropriate. I am really concerned about the effect on our credibility with markets if we persist in this kind of advice. It may very well be that the recent stability in the Won, notwithstanding the volatility elsewhere in the region, reflects a positive effect on investors' sentiment resulting from the relatively strong fiscal position. Would it not be logical to think that investors would view the strength of the fiscal position as a positive factor counterbalancing the expectation of further upward revision of financial sector restructuring costs? This could give them comfort that there is margin for the use of public money, if necessary, to capitalize the banking system, without jeopardizing the medium-term sustainability of fiscal and balance of payments positions. Furthermore, if we insist on a larger fiscal deficit, shouldn't we be ready to provide additional Fund resources to finance the excess at our regular (i.e., not SRF) interest rate? Some clarification of the actual increase in the deficit that is being proposed would, in any case, be in order; while the text indicates that the staff will propose a deficit of 4 percent of GDP, Tables 2 and 3 indicate a target of 3.5 percent of GDP.

Monetary policy and interest rates

2. It may well be that real interest rates at 15 percent (however the uncertainty of these calculations, related in part to the projection of expected inflation), are substantially higher than in the rest of the region. Whether this is an argument for lowering interest rates substantially is not clear, however. The primary objective of monetary policy should remain the stabilization of the exchange rate, and the measure of the real interest rate, in and of itself, does not provide much guidance for the conduct of monetary policy at this time. It would be preferable, therefore, to suggest that the reduction in rates be implemented only gradually.

during the next several months, in order to avoid the need for reversals. In addition, a further decline might not be consistent with the increase in the fiscal deficit that is being proposed.

3 We are uncomfortable with maintaining the monetary program unchanged from the last review given the proposed substantial downward revision in economic activity. While we realize that some of this reflects that the much larger than expected decline in velocity evidenced through March, it is not evident that we should expect further decline for the rest of the year. We think that some tightening of the monetary program would be consistent with the nominal GDP revision and, in light of the magnitude of the overperformance to program targets to date, it would still provide room for a decline in interest rates.

Other principal comments

4 We appreciate the difficulties in forecasting the magnitude of the economic downturn, but we would caution against overdoing the downward revisions -- from having been persistently too optimistic, we should avoid moving to excessive pessimism. The projection of minus 5 to 7 percent is much weaker than the consensus forecast of minus 3 ¾ percent, and to justify it, the staff should present the underlying analysis, including an account of the carryover effects of where we are now (as evidenced by the existing data).

5 Given the rapid accumulation of usable reserves to date (Chart 1b), and the further rapid increase forecast for 1999 (notwithstanding net repurchases to the Fund of nearly \$9 billion), we think the authorities may wish to consider turning this arrangement into a precautionary one. Remaining purchases are relatively small compared to the stock of Korea's reserves and, in any case, they would continue to be available to the authorities. An announcement that the program has become precautionary could be expected to have a positive signaling effect.

6 Does the staff have a view which would be the better way to proceed with corporate debt restructuring? Does it favor the centralized (World Bank favored) approach or the decentralized (favored by the authorities) approach? We think the decentralized approach could work better, with the World Bank providing technical assistance to help the banks overcome some of the weaknesses in their relationship with Chaebols (as identified by the World Bank). It is not clear to us why government officials would be better equipped than commercial banks in dealing with these matters.

7 Is there room for some further reform of the bankruptcy law? We understand that notwithstanding the revision earlier this year, there remain problems in this area.

Specific comments

- The brief is missing a work program
- Regarding the recent liberalization of short-term capital, we would attach high priority to bringing forward the issuance of prudential regulations on short-term foreign borrowing and the associated reporting requirements. This is particularly important against the background of a weak banking system and the dangers that managers will “gamble for resurrection”
- On other structural policies, the mission could also review the progress made, as mentioned in the 1998 Article IV report, in several aspects of corporate restructuring, including the strengthening of corporate governance, the prohibition of cross guarantees for new borrowing, and the easing of restrictions on merges and acquisitions
- Is there scope for including trade reform measures that go substantially beyond what had been agreed under the program, as had been suggested in the brief for the second quarterly review?
- The mission should review the authorities’ progress in meeting trade policy commitments under the program, including the following (i) liberalization by July 1998 of an additional 40 items presently covered by the Import Diversification Program, (ii) the review of existing import certification procedures, and preparation of a plan to streamline them and bring them in line with international practice, by August 15, 1998, and (iii) progress in rationalizing all existing subsidy programs
- The brief could also clarify whether the proposal to shift the distribution of revenue between central and local governments would be accompanied by a parallel shift in expenditure between central and local governments
- The penultimate sentence of para 20 seems to be incomplete
- What is the timetable for the “implementation of the diagnostic reviews of the remaining” financial institutions (para 19)?,

cc FAD, LEG, MAE, RES, STA, and TRE



Office Memorandum 36

93 JUL 25 PM 4

~~RES~~
CC FUSS
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To Ms Tseng

June 26, 1998

From Charles Adams (RES)

Subject **Korea—Briefing Paper for the Third Quarterly Review Under the Stand-By Arrangement**

While we broadly agree with the staff's position on fiscal policy, we have reservations on the idea to convert the fiscal deficit targets into floors, rather than ceilings. On monetary and exchange rate policy, we are not sure the brief strikes the proper balance between exchange rate appreciation and easing monetary policy. We also have serious concerns about the lack of progress in corporate debt restructuring, as explained below. Progress in this area is essential to lift Korea out of the crisis. As a more detailed discussion of approaches to corporate debt restructuring may be warranted, it may be helpful to meet to discuss this issue.

Monetary and Exchange Rate Policy

The brief states the intention to indicate to the authorities that "there is scope for continued easing of interest rates, provided the foreign exchange market remains stable", and proposes to leave the monetary targets in the program unchanged in order to "give the authorities room to lower interest rates" (para 15). However, we are not sure that, in the current environment, there is room for significantly lower interest rates. As the brief notes in the first paragraph, in recent weeks there has been an erosion in market sentiment, negative repercussions from continued weakness in the Japanese economy and the value of the yen, and a virtual halt in portfolio capital inflows, to which we would add the sharp increase in the spread on EXIM global bonds in the last month (Chart 1b). This does not suggest that there is much scope for lowering interest rates. In fact, the argument for lowering interest rates seems to be that, if the current drop in inflation holds, real interest rates in Korea will be higher than in other Asian countries.¹ The problem is that, while the current level of interest rates may not be desirable from the point of view of the banking and corporate situation or the economic recovery, it may be the level necessary to defend the exchange rate. As we argue below, other policies should be implemented to deal more aggressively with banking and corporate debt problems, which ultimately hold the key to the economic recovery. Certainly nothing good can come out of losing the degree of exchange rate stability that has been gained.

¹ But note that real interest rates in Korea are **much lower** than in countries that have (so far) successfully defended the exchange rate (e.g. Russia or Brazil). Also, we wonder how sensitive the estimates are to the degree of optimism in the inflation projections for the different countries.

More generally, it does not seem that the brief strikes the right balance between easing monetary policy or allowing some exchange rate appreciation. The current strength in the balance of payments seems to come from the current account, rather than from the capital account. From this perspective, the current level of the exchange rate still seems overdepreciated. Even allowing for cyclical effects, a current account surplus equivalent to 10 percent of GDP is difficult to accept as an optimal level.

It seems highly inappropriate to leave the **ceilings on monetary aggregates** unchanged. The current program ceilings allow a 40 percent increase in reserve money between May and December of 1998 and, in fact, a nearly 33 percent increase from May to June alone, with lots of room for increases in NDA through September. Clearly the Bank of Korea cannot use all that room in the program without seriously undermining exchange rate stability. While, given the difficulties in accurately projecting the demand for the various different aggregates, it is understandable that a divergence arise between program targets and the actual evolution of monetary aggregates, there is no reason not to adjust the program ceilings in view of current developments. We also note that although the recent drop in reserve money seems unusual (the reasons for it are not discussed in the brief) the broader monetary aggregates have remained broadly in line with projections. This suggests that an increase in reserve money as in the program targets would result in a sharp easing of monetary conditions. In addition, the brief could explain other monetary developments in more detail. For example, what explains the large increase in the money multiplier at a time when banks are allegedly reluctant to extend credit?

Fiscal Policy

It seems quite awkward to convert the indicative ceiling on the fiscal deficit to a floor. Would the mission really not conclude a review if the deficit is too low? Would this prompt the authorities to immediately go on a spending binge to meet the program target? While the deficit target seems appropriate, the only valid strategy seems to be to convince the authorities of the desirability of a moderate easing of fiscal policy.

GDP Projection

As a matter of principle, we want all area department projections to represent their best judgement. We are definitely not comfortable with the idea that economic projections should be adjusted for political reasons. While the adjustment in this case seems small (from -6 percent to -5 percent) it would still constitute a dangerous precedent.

Corporate Debt Restructuring

We are not convinced that the approach described in the brief will yield significant results in the foreseeable future. When the FSC unveiled a "death list", its limited coverage was viewed as disappointing by markets. For example, some chaebols are rumored to have used creative

accounting to window-dress the financial health of their affiliates and have avoided being put on the list. Even for the companies on the list, the process may be very slow. Creditor banks will reportedly cut off new loans but will not call in outstanding loans until liquidation plans are finalized by the corporates. This delay will reduce the urgency of restructuring of corporates, and chaebols in particular.

We are of the view that a more comprehensive approach, possibly requiring an active involvement by the government, will be required to resolve the corporate debt problem and allow the normal credit mechanism to resume functioning. It is clear that debt for equity swaps by banks cannot be the full answer, as after the conversion the banks will still have weak balance sheets. These operations may also be problematic from the corporate governance perspective. Several alternative approaches, which will not use public funds to bail out corporates, can be envisaged, including the setting up of special purpose vehicles (SPVs) to restructure corporate debt using private international capital. We would welcome further discussion within the Fund on a concrete plan on corporate debt, which will also help speed up the restructuring of bank balance sheets. We are of the view that the present approach using an arbitration committee and bank creditor committees is slow and inadequate and will exacerbate the output contraction.

cc Mr. Mussa
Heads of Departments
FAD, LEG, MAE, PDR, STA, TRE

Contributors
Mr. Borensztein
Mr. Chen
Mr. Lee
Mr. Lall



Office Memorandum

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93 JUN 25 FILE 36

To Ms Tseng

June 26, 1998

From Peter S Heller (FAD)

Subject **Korea—Draft Briefing Paper for the Third Quarterly Review Under the Stand-By Arrangement**

This well-written brief presents a clear picture of developments and the mission's proposed policy stance. While we agree that the authorities should be urged to consider loosening the deficit, we would prefer the program to contain a specified deficit target rather than a deficit floor. Our comments explain our reservations about the deficit floor, and list further considerations that should be taken into account to determine the appropriate level of the target.

The deficit floor

On balance, we would caution against introducing a deficit floor, despite some attractive aspects. The main contra-argument is that a floor would leave fiscal management vulnerable to both upside and downside uncertainties. Suppose, for instance, that the authorities raise spending abruptly, but then revenues collapse (see below). A deficit target would provide guidance on the tolerable limits to the consequent fiscal gap, while a deficit floor would not. On the other hand, if the authorities' projections are right, and the slump is shallower than the mission expects (so that, *inter alia*, revenue remains buoyant), the interpretation of the deficit target as a floor could lead to an expenditure effort which is larger than needed for the recovery.¹

More generally, market reaction to the deficit floor and the consequences for public relations may not be unambiguously positive. There is no obvious mechanism by which a deficit floor would contribute to easing financial strains. Rather, the market is likely to worry about the additional pressures on financing needs and interest rates, and the higher band of uncertainty surrounding them. And the public expects the Fund to be, above all, prudent.

The deficit target for 1998

While there appears to be a strong case for a fiscal stimulus, the 3½-4 percent of GDP deficit target should be substantiated before it is included in the program, by clearing up several outstanding issues during the mission.

¹The likelihood of waste would be exacerbated by the concentration of the spending in the second half of the year since the fiscal deficit has been significantly below target so far this year.

- As discussed in my May 21 note to Mr Fischer, FAD has reservations about the estimates of the cyclical impact on the deficit (paragraph 9) Since then, we have made some progress towards developing the methodology, but have been stymied by the unavailability of details on the budget The mission should put high priority on receiving sufficiently disaggregated budgetary projections to allow it to calculate the line-by-line budgetary impact of changes in key parameters, with a view to establishing firmer projections of the no-policy-change budget
- This baseline should form the starting point for articulating a more pointed fiscal strategy for lessening the recession The appropriate deficit target could be achieved by adjusting the no-policy-change deficit by, say, a tax reform which is less-than-revenue-neutral (at least in the short-term), and other transparent and non-discretionary tax cuts New expenditures could focus on items which would boost employment
- It would be important for the mission to address up-front the financing implications of the higher deficit, it is not immediately clear how much could be financed, given the near-term constraints in the market Further, it may be rash to base the case for expansion on the argument that Korea's debt ratio is low, unless information is available on the debt of other parts of government and public enterprises, and on firm projections of the near-term costs of bank restructuring (paragraph 10)
- The suggestion in paragraph 8, that the mission may have to use an unrealistically high GDP projection in the program, exacerbates our previous concerns that the revenue projections may be too optimistic (despite the recent nominal revision, which does not take into account the shift in composition of GDP away from traditional tax bases) Since budgets and fiscal targets cannot respond agilely to rapidly changing assumptions, it would be important for the revenue projections to be based from the outset on the most conservative GDP projection, rather than depending on "frequent adjustments to the projections"

The social safety net

Box 1 is very useful The only proposal that might be questioned is the suggestion to shift eligibility to a minimum employment, rather than contribution, period, this would be unusual, and is not a viable long-term strategy It would be preferable to establish it as a temporary measure, valid for the next six months (until those newly eligible catch up with contributions) This would appear to be in line with World Bank views on needed reforms More generally, it would be important for the mission to identify and reconcile possible differences with the Bank in policy recommendations in this area

If, despite all these amendments, a large share of the labor force remains outside the safety net, the elaboration of some self-targeting schemes is probably called for Public works, and the free distribution of lower-grade foods, are traditional examples

cc LEG, MAE, PDR, RES, STA, TRE, Mr Tsibouris

Contributors J Davis, A Cheasty, L Perez, W Mahler, S Barnett, M Verhoeven



Office Memorandum

CC Foss
KM
SC
DS

To Mrs Tseng

June 26, 1998

From Sean Hagan ~~AS~~ (LEG)

Subject **Korea—Briefing Paper for the Third Quarterly Review Under the Stand-By Arrangement**

The Legal Department's only comment is marked on the attached page

Attachment

cc FAD, MAE PDT, RES, STA, and TRE
Messrs Schweitzer, Scott, Lierberman, Qureshi, World Bank

98 JUN 25 11 4 36

Box 2 Deleveraging of Large Corporations

Reducing debt equity ratios of the large corporations is an essential element of corporate restructuring. At end 1997 debt equity ratios of the top 30 chaebols stood at 604 percent (including financial affiliates) compared with industrial country norms of about 100–200 percent. The magnitude of the effort needed to reduce debt equity ratios to these levels is demonstrated by an illustrative exercise prepared by the World Bank. Under favorable assumptions, the standard restructuring options would reduce the debt equity ratio to only about 340 percent in two years. Reduction of debt equity ratios beyond this level requires some form of additional restructuring in the form of debt/equity swaps, debt write down, or equity injections.

Options for Reducing Debt Equity Ratios of the 30 Largest Chaebols

	Debt (W bil)	Equity (W bil)	Debt Equity Ratio	Assumptions
Stock at end-1997	456.3	75.6	604	
Standard options				
Increase in retained earnings		3.7		Based on 1996 financial performance
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Subtotal	366.1	106.9	343	

Source: World Bank.

1/ All proceeds used to retire debt.

liberalization of short-term capital movements, the mission will discuss the possibilities for bringing forward prudential regulations on short-term foreign borrowing and foreign exchange exposures, and on monitoring and reporting requirements. It will also review progress on the authorities' efforts to strengthen the reporting of off-balance sheet foreign currency-denominated exposure of financial institutions and to submit legislation to improve corporate sector external debt data reporting. The mission will also review the progress in developing an early warning system based on external vulnerability indicators.

The mission will also ensure that the proposed law is consistent with Korea's obligations under Article VIII, of the Fund's Articles.



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Office Memorandum

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To Ms Tseng

June 26, 1998

From Carl-Johan Lindgren *CL* (MAE)

Subject **Korea Briefing Paper for the Third Quarterly Review Under the SBA**

We broadly agree with the thrust of this clear and comprehensive paper. In principle, we agree that a further easing of interest rates would be appropriate, subject to continued stability in the foreign exchange market. As regards, the latter, however, we wonder whether the brief could give further details as to how this proviso would be interpreted in cases where the won comes under pressure because of exchange rate developments elsewhere in the region. Alternatively, should the won appreciate, would the program envisage an immediate interest rate response?

We agree with the mission's positions on financial sector restructuring. In paragraph 20, however, we would prefer a more neutral reference as to the effect of corporate debt restructuring on the timetable for tightening limits on large exposures and on connected lending. The restructuring of corporate debt may well lead to cases in which short-term corporate debt gets transformed into longer-term debt (and in some cases even into equity). Accommodating those cases would most likely delay the tightening of the limits. (A possible way out would be to tighten the limits but allow for them to be exceeded when the excess is linked to corporate debt restructuring cases, other possibilities can be envisaged also.)

It would be appropriate to indicate in paragraph 13 that the fiscal costs related to bank restructuring would include only the interest costs. Similarly, it would be useful if the brief were to clarify that (a) the use of public funds for the purchase of nonperforming loans (paragraph 18) should include the possibility—in line with the May 4 Letter of Intent—of such purchases from sound banks where this is to be done to facilitate mergers, and (b) the proposal to bring forward prudential regulations on short-term foreign borrowing (paragraph 26) refers to measures already included in the May 4 Letter of Intent.

Paragraphs 23 and 24 may need to be updated in light of yesterday's press reports on the functions of the arbitration committee. In paragraph 25, divestiture of assets should be added to the list of alternatives for chaebols to reduce their debt/equity ratios.

Finally, the revision of the Foreign Exchange Management Law (paragraph 26) may involve a number of complex issues. In this context, we note that the Korean authorities have already contacted MAE to provide documentation on a wide range of issues related to capital account

liberalization MAE would be prepared to assist in the assessment of the revision to the law, possibly, if thought appropriate, in the context of a short mission

Editorial

Page 1, Box In the last bullet point, replace “prudential” with “prudent ”

Paragraph 11 “mission” should replace “mss ”

The sentence in the third line from the bottom in paragraph 20 is incomplete

In the Annex on Fund Relations, under X, the first reference (which deals with Mr Nordman’s visit) should be changed from mission to expert visit and the dates should be May 24-30 Also, there should be a reference to Mr Michael Smith’s expert visit, on corporate debt workouts, which took place June 3-10

cc FAD, LEG, PDR, RES, STA, and TRE
Mr Guitian

Contributors

Mr Baliño
Ms Milne
Mr Laurens
Mr Hayward
Mr Musalem

CC FOSS
KM
SC
DJ

From Anna Vahdati
To WTSENG, CCULLATI
Date 6/26/98 1 16pm
Subject KOREA, Briefing Paper - NO COMMENTS FROM STA

The Statistics Department has no comments to offer on your draft paper, for your records the reviewer is Claire Luksila

CC FADREV, LEGREV, MAEREVIEW, PDRCOMMENT, RESREVIEW, TRERE

93 JUL 26 11 4 35



Office Memorandum

cc. WT
Kwon
SC
DJS

To: Mr. Knight

June 25, 1998

From: Okyu Kwon *okwon*

Subject: **Korea**

I would like to thank you for providing the valuable information on foreign exchange systems, which, I believe, could contribute to my authorities' final touch in the amendment process of relevant foreign exchange laws.

However, regarding your suggestion to send a small mission to Korea to discuss this matter, my authorities believe that it is not desirable since the amendment process of relevant laws is in the final stage--waiting for submission to the National Assembly soon. Indeed, my authorities believe that prompt action is very important at this moment since several public hearings were already held for both domestic and international societies, and close consultations were held with staff of the IMF and the World Bank through the Resident Representative office in Seoul. Their opinions seem largely reflected.

I think my authorities appreciated your suggestion even though they could not accept it.

cc: Mr. Aghevli

98 JUN 25 PM 4:39

INTERNATIONAL MONETARY FUND

June 25, 1998

To Peter Hole

Subject **Draft Letter to Financial Times Responding to
Professor Wade**

Thank you for the draft letter I took the liberty to make some changes and take out the second paragraph since the earlier gains in the stock market and exchange rates have been lost

Attachment


Wanda Tseng
(4-320, ext 37182)

June 25, 1998

Editorial Page Editor
The Financial Times
London
United Kingdom

Dear Sir

Professor Robert Wade likens current cautionary monetary policies to “water torture,” but his advice to Asian countries (June 23 article) to “lower interest rates to near zero and step on the monetary gas” in an effort to inflate themselves out of crisis could plunge them into further rounds of destabilizing currency depreciations. Moreover, the situation in Japan illustrates that interest rates near zero are not a panacea for an economy with a structurally weak banking system. It would be equally dangerous to accept Wade’s counsel to jettison the “far-reaching structural reforms,” especially bank capital standards, that Asian countries are implementing at IMF urging. Pretending nothing was wrong with domestic financial systems and corporate governance helped bring on the crisis. Abandoning corrective action and reverting to “channeling credit” would surely make things worse, not better.

Monetary and fiscal policies are already adjusting to mitigate the sharp economic slowdown. Korea’s overnight interest rates have fallen 30 percent at end-1997 to below 15 percent now, and Thailand’s from 25 percent to 17 percent. Larger fiscal deficits are projected to accommodate higher spending on social support costs, the need for which has been consistently emphasized by the International Monetary Fund, as well as weaker revenues. On this evidence, radical course corrections by the countries at the center of the crisis do not seem warranted.

Sincerely,

[APD senior staff or others?]



Office Memorandum

CCI Foss
KMM
SC
DVS
M Stone / Waker
RDR
98 JUN 25 AM 8 47

To Ms Tseng
Mr Balino

June 25, 1998

From J R Dodsworth

Subject **Korea Financial Sector Restructuring Plan**

Over the last few days, I have had discussions with FSC¹ to relay comments from Fund and World Bank staff on the FSC Restructuring Plan that was released on June 19. The authorities' responses may be helpful as input to the next rounds of discussions.

- 1 Under what conditions will public resources be used and how do the authorities plan to meet the LOI criteria that existing or new shareholders should be making a contribution of new capital?

On this question, the authorities recognize that new private capital is an important element in overall financing (W 20 trillion in the May 30 announcement) and that public resources should be used to encourage the shareholders' contribution. In the context of bank restructuring, public resources are expected to be used in two ways:

First, in P&A operations², public resources would be used to (i) fill the financial gap in the weak bank and (ii) reconstitute the capital ratio in the (stronger) receiving bank which will be receiving additional risk assets.³ In P&A operations, there would be no expectation that a shareholders' contribution would be a condition for the use of public resources.

In the second situation, i.e. in promoting an M&A operation, there would be an expectation of a contribution of new capital from the shareholders of the new (merged) bank. The extent and timing of the increase in capital from shareholders would be agreed and included in a MOU prior to the injection of public funds, however, the timing of the capital contribution would be some time after the merger.

¹ I met Chairman Lee, Mr. Won Young Yon, Director General, and Mr. Kang, Director, Financial Sector Restructuring Unit.

² Straightforward liquidations are expected only for nonbank financial institutions.

³ There are two views on the extent to which the receiving bank should be compensated-- FSC believe 100 percent, MOFE believe 50 percent.

has been completed. The expected delay would be six months or less. At this stage, the FSC has not worked out the criteria for setting the amount of new capital that would be expected.

Public resources are also expected to be used in a more general recapitalization of banks which will be pursued separately from the restructuring program. This will be an extension of the earlier program for purchase of subordinated debt. The resources available for this program will be enhanced by W 1-2 trillion in coming months. Individual banks will benefit from the program according to their record of co-operation in rolling over SME debts. The FSC stressed that this was in line with a long-standing political commitment from the President, that the program was separate and not related to the restructuring plan, and that the program would be limited in amount as described above.

- 2 How does the plan ensure that P&A and M&A operations do not financially weaken or deteriorate the cost structure of the sound banks that are participating?

For P&A operations, while the assets and liabilities to be transferred are expected to be balanced--and additional capital will be injected into the recipient bank as indicated above to reconstitute the capital ratio--there is a concern, shared by FSC officials, that the deteriorating trend of the transferred asset portfolio may lead to a worsening of the situation in the sounder bank. It is also not clear what will happen in the P&A operation to fixed assets, workers, and management of the weak bank. While P&A can work like a liquidation and FSC officials maintain that there will be no obligation on the sound bank to take over branches, managers, personnel, etc., there may well be pressures on the sound bank to take over the full operations of the purchased bank, thereby lowering efficiency levels.

The FSC officials stressed that under the current law, P&A has to be voluntarily accepted by the recipient bank with acceptance by at least two-thirds of its shareholders. It is therefore, necessary for the authorities to offer sufficient incentives, including any required restructuring, for the deal to be accepted.

Under a forced merger, the FSC intends to receive a management improvement plan that will be incorporated in a memorandum of understanding from the parties involved. The new merged bank will thus be subject to meeting quarterly benchmarks reflecting the efficiency of its operations, and not just meeting a schedule for minimum capital ratio. Further work is needed in formulating the specific benchmarks to be used, but various cost indications and personnel ratios are being considered.

- 3 What are the authorities plans for obtaining further information and performing additional analysis on the twelve undercapitalized banks, and what are plans for next round?

For the first twelve banks, once the current diagnostic reviews are completed (July 15) there are no plans for further external evaluation of this type, through the remaining banks would be under intensive supervision. The diagnostic reviews on the second twelve banks will need to be completed by end-August and talks will begin soon with accounting firms. The authorities will do their best to get cosigning agreements with international firms, provided the target deadline can be met.

4 Have the fiscal support estimates from May 20 been updated?

The final version of the Financial Sector Restructuring Plan (June 19) contains the same overall fiscal support estimates as the May announcement. The "fiscal cost" of "W 23 trillion" was included in error in earlier versions of the plan. The FSC staff stress that the estimates for bond issuance are very tentative (both in total and in the breakdown between KAMCO and FDIC) given the uncertainties in the situation. The authorities tend toward the view that it will not be possible for the market to completely absorb the bonds required, and that at least part of the issuance should be taken up by the Bank of Korea and thereby monetized.

For the purchase of foreign currency NPLs, KAMCO is expected to raise foreign resources through international bond issue or "asset-backed securities". The second option will, however, only be available if new legislation is passed. Currently, KAMCO is in discussions over a bond issue of DMS billion with Deutsche Morgan Grenfell.

5 Are there plans to ensure that KAMCO purchasing policy does not result in a hidden fiscal cost?

The authorities are aware that determination of a market price for NPLs is very difficult. They point out that in a P&A operation there has to be a firm price, but that as the hole in the balance sheet has to be filled one way or another, the actual price paid is of an accounting nature and does not affect the size of support needed. For M&A, the current plan is still to use a "firm" price system (i.e. no ex post adjustments) and that a percentage to book value would be used (possibly 53 percent). At the same time, KAMCO has not disposed of any of the assets purchased earlier, largely because the market is currently so adverse that losses would be inevitable even after adjustments have been made.

6 What form will capital contributions take?

No final decision has been made, but the authorities believe that at least part of the capital increase will be in the form of preferred stock in order to increase Tier I capital.

7 **Schedule for achieving minimum capital adequacy ratios**

The authorities emphasise that while the time schedule is slightly lengthened from previous commitment, this should be understandable given the adverse conditions in the economy, and the standards have been strengthened for most banks by the inclusion of a 10 percent standard. Also they point out that for banks that do not undertake international business, a minimum capital ratio of 8 percent (the previous goal) is planned by end-2000. For merchant banks, the goal will be to bring up the ratio to at least the level of the internationally operating banks (and possibly more according to Chairman Lee), but the FSC does not wish to announce this intention or set a specific target at this time. This can be further discussed in the coming review.

cc Mr Aiyer

cc, FOSS
KM
SC
D5

Ministry of Finance & Economy

Republic of Korea

427-760 Kwachon-shi, Kyonggi-do, R O K /TEL(82-2-503 6771)/FAX(82-2 503 6772)

Facsimile Cover Sheet

date 24 June 1998

To Ms Tseng
Deputy Director Asia Pacific Department
International Monetary Fund

From Hyung Gun Park, Deputy Director
International Financial Institutions Division

number of pages(2) including cover

fax 1-202-623-4432

Subject Mr Kwon s letter

o Please find the attached letter



MINISTRY OF FINANCE AND ECONOMY
REPUBLIC OF KOREA

23 June 1998

Ms Wanda Tseng
Deputy Director
Asia and Pacific Department
International Monetary Fund

Dear Ms Tseng

I regret that you will no longer be leading the Korean Mission But the Fund needs you for other duties, and I have to respect that decision

My colleagues and I have fond memories of working with you during the trying days of the crisis We appreciate your tireless effort and dedication Your leadership and coordination rendered the last two Quarter Reviews a success

I wish you success in your new job and hope to see you in different occasions

Sincerely,

Tae-Shun Kwon
Deputy Director-General
International finance Bureau

p s Personally I feel sorry that I gave you a little hard time during our negotiation in the second Quarterly Review Please understand that it was not my own intention

CC FOSS
KM
SC
D5

Ministry of Finance & Economy

Republic of Korea

427-760 Kwachon-shi, Kyonggi do, R O K /TEL(82 2 503 6771/FAX(82-2-503-6772)

Facsimile Cover Sheet

date 24 June 1998

To Mr Tseng
Deputy Director, Asia Pacific Department
International Monetary Fund

From Kyung Wook Hur, Director
International Financial Institutions Division

number of pages(2) including cover

fax 1 202-623-4432

Subject letter

o Please find the attached letter

June 24, 1998

Ms Wanda Tseng
Deputy Director
Asia and Pacific Department
International Monetary Fund

First of all, Congratulations on your new job! It would be exciting to work on Chinese economy particularly for you as an expatriate

However it is regretful that we would not see you as often as before I would very much miss your patience sense of balance and humor, and warm heart I will always remember your efforts and dedication to help us get over the current crisis

I wish you all the best and will remember you as one of my friends

With Best Regards,



Kyung Wook Hui

cc FOSS
D5
KM
SC

Ministry of Finance & Economy

Republic of Korea

127 760 Kwachon-shi, Kyonggi do, R O K /TEL(82-2 503 6771/FAX(82-2 503-6772)

Facsimile Cover Sheet

date 24 June 1998

To Ms Tseng
Deputy Director, Asia Pacific Department
International Monetary Fund

From Kyung Wook Hur, Director
International Financial Institutions Division

number of pages(2) including cover

fax 1-202 623-4432

Subject Minister's letter

○ Please find the attached letter



**MINISTRY OF FINANCE AND ECONOMY
REPUBLIC OF KOREA**

19 June 1998

Ms Wanda Tseng
Deputy Director
Asia and Pacific Department
International Monetary Fund
Washington, D C , U S A

Dear Ms Tseng

I regret that you will no longer lead the IMF Mission to Korea, but congratulates you on your new assignment for China and Hong Kong. I appreciate the invaluable service and dedication you have put into helping Korea overcome the difficult times.

As you have expressed, I hope you continue to have keen interest in Korea and support the Korean cause. Thank you very much, and I bid you the best.

Sincerely yours,

Kyu-Sung Lee
Minister of Finance and Economy



Office Memorandum

CC: FOSS
D/S

To Mr Fischer

June 24, 1998

From Wanda Tseng *WT*

Subject Korea Information Note on "Rescue Loans"

For your information, in response to Ms Lissakers' request made during the last Board meeting on Korea, we intend to circulate the attached note on rescue loans to the Board on Friday, June 26

6 25 98

Attachment

cc Mr Munzberg

Ms Tseng
Before circulating this,
please include some indication
of how large W3 trillion is,
in the overall scheme of things -
e.g. as a % of total loans,
as a % of GDP

JF

The problem here is that the
reader has no idea whether
this is a big or a small
issue

98 JUN 26 AM 11 25

OFFICE FUND-

JUN 98 2:45



Office Memorandum

To The Secretary

June 24, 1998

From Wanda Tseng 

Subject **Korea Information Note on "Rescue Loans"**

This note provides information on "rescue loans" requested during the Executive Board meeting on May 29. I would appreciate its circulation to the Board.

Rescue loans are extended by banks to corporations that are experiencing financial problems and have the potential to recover within three to four years. Banking Supervisory Authority rules prescribe that banks (i) inform the Authority in writing of new rescue loans, (ii) review borrower restructuring plans each month, and (iii) report to the Authority every six months on borrower adherence to the plan. Banks can replace borrower management, sell assets of the corporations or the owner, suspend dividend payments to large shareholders, and liquidate the corporation if the restructuring plan is not being followed.

Eleven corporations received rescue loans totaling W 3 trillion during October 1997–May 1998 (Table 1). Most rescue loans were at interest rates (13 percent to 25 percent) which were above the prime rates (9–12 percent) and with maturities ranging from four to twelve months. Some rescue loans were at below market interest rates. Creditor banks can adjust interest rates when corporations implement restructuring plans to recover the cost of reduced interest rates. More than half of the loans were extended by the 12 banks with capital asset ratios less than 8 percent and by Seoul Bank and Korea First Bank (Table 2). Since the beginning of March four rescue loans have been extended.

Banking Supervisory Authority instructed main creditor banks to reach corporate restructuring agreement with borrowers of "rescue loans" on February 13, 1998. Seven of the borrowers are on the list of nonviable firms announced by the authorities last week and are currently preparing group-wide restructuring plans involving the liquidation or merger of their affiliates. The management of the Dong Ah group, which accounts for one-third of the total stock of rescue loans, has been replaced and plans have been announced for disposal of its affiliates with the exception of Dong Ah Construction. In addition, the four borrowers not on the nonviable list are expected to liquidate affiliates according to their restructuring plans.

Mark Stone (Ext 36532) is available to answer technical questions relating to this note.

Attachments (2)

Table 1 Korea Rescue Loans by Borrower

Group	Date	Amount (W bils)	Percent of Total
Dong Ah	10-Jan-98	294 0	
	3-Apr-98	140 0	
	6-May-98	81 5	
	21-May-98	526 0	
	Total	1,041 5	34 8
Hanwha	17-Dec-97	300 0	
	28-Feb-98	442 0	
	Total	742 0	24 8
Kohap	30-Jan-98	278 7	9 3
Haitai	15-Oct-97	54 7	
	13-Nov-97	45 3	
	6-Nov-97	150 0	
	Total	250 0	8 4
Shin Won	11-Feb-98	200 0	6 7
Woo Barg	2-Mar-98	110 0	3 7
Jindo	19-Nov-97	106 0	3 5
Shin Ho	27-Nov-97	80 0	2 7
Hwa Sung	14-Apr-98	80 0	2 7
New Core	21-Oct-97	54 5	1 8
Hanil	31-Dec-97	50 0	1 7
Total		2,992 7	100 0

Source Financial Supervisory Commission

Table 2 Korea Rescue Loans by Bank

Bank	Amount (In billions of won)	Percent of Total
Seoul Bank	523.4	17.5
KEB	401.2	13.4
CBK	350.1	11.7
Hanil	262.2	8.8
KLTCB	218.4	7.3
CHB	180.6	6.0
KDB	151.8	5.1
KFB	132.3	4.4
Hana	121	4.0
Daedong	89.3	3.0
Boram	72.6	2.4
Shinha	71.6	2.4
Kyongnam	67.5	2.3
Daegu	56.3	1.9
Other	294.4	9.8
Total	2,992.70	100.0

Source: Financial Supervisory Commission



Office Memorandum

To Mr Hansen

June 23, 1998

From Wanda Tseng

Subject **Korea—Shipbuilding Industry**

Regarding your memorandum of June 18, 1998 concerning the letter from the Danish shipping company Maersk line to the Danish Ministry of Economic Affairs, I would like to note the following

Many companies in Korea have high debt-equity ratios (averaging about 500 percent for large corporations), and corporate restructuring is an important objective of the IMF-supported reform program in Korea. Reducing overindebtedness is an essential aspect of corporate restructuring. The authorities have announced a target debt-equity ratio of 200 percent within two years to encourage the large conglomerates to restructure. However, specific debt-equity ratios (200 percent nor 400 percent) are not targets under the IMF-supported program. The appropriate debt-equity ratio depends on the circumstances of specific industries and companies. There is, therefore, not an issue of the IMF being asked to relax debt-equity ratios for particular sectors like shipbuilding.

I should add that it is more realistic to expect deleveraging among the large corporations to be a gradual process as corporate restructuring proceeds.



Office Memorandum

CC, FOSS
KM
SC
D5

To Ms Tseng

June 23, 1998

From Deborah E Siegel *DES*

Subject **Korea Questions on Exchange System**

Further to the Korean authorities request, I checked Legal Records for "correspondence" relating to Korea's acceptance of Article VIII. While there are several internal memoranda among Fund staff on the matter of travel restrictions, there is no "correspondence" between staff and the authorities in our files.

These internal staff memoranda indicate that the discussions regarding exchange restrictions centered on creating authority for the Bank of Korea to approve bona fide requests on current international transactions. This was noted in the staff report notifying the Executive Board of Korea's acceptance of Article VIII (attached) ¹

Mr Dodsworth notes that the authorities believe that the issues raised in the questionnaire were resolved at the time of the Article VIII acceptance. While the "prior approval" question was indeed addressed generally, we would appreciate the authorities renewed attention to the particular questions on how the approval process operates because it would continue to apply to certain transactions under the new law (as noted in my memorandum to you of June 8). Concerning travel, for example, the existing rules are quite complex and raise several ancillary questions beside the prior approval point. Also, many of the other questions noted do not concern the prior approval process, such as transfers by non-residents.

Attachment

cc Mr Hagan/Mr Leckow

JUN 23 1 07 PM '98

case you have an electronic means of searching APD's files, the other staff members involved were Chang-Yuel Lim and Ana Maria Jul and Peter Quirk and perhaps one of them had correspondence with the authorities

**IMMEDIATE
ATTENTION**

LEGAL RECORDS
ROOM 8-514

0401

EBD/88/338

November 21, 1988

To Members of the Executive Board
From The Secretary
Subject Korea - Acceptance of Obligations of Article VIII,
Sections 2, 3, and 4

It is not proposed to bring the attached memorandum to the agenda of the Executive Board for discussion unless an Executive Director so requests by noon on Monday, November 28, 1988. In the absence of such a request, the draft decision will be deemed approved by the Executive Board and it will be so recorded in the minutes of the next meeting thereafter.

Att (1)

Other Distribution
Department Heads

INTERNATIONAL MONETARY FUND

KOREA

Acceptance of Obligations of Article VIII,
Sections 2, 3 and 4

Prepared by the Exchange and Trade Relations, Asian
and Legal Departments

Approved by J T Boorman, P R Narvekar,
and François Gianviti

November 18, 1988

In a letter received on November 9, 1988 (attached), Korea has informed the Fund that it has accepted the obligations of Article VIII, Sections 2, 3 and 4 of the Articles of Agreement. The staff has been informed that the effective date was November 1, 1988.

The exchange system of Korea was last described in Korea - Staff Report on the 1988 Article IV Consultation (SM/88/88, 4/20/88) and Korea - Recent Economic Developments (SM/88/101, 5/4/88). On November 1, 1988 Korea's foreign exchange regulations were modified to authorize the Governor of the Bank of Korea to approve exchange applications for the purpose of travel notwithstanding limitations in other parts of the regulations. The staff notes that under current policy and practices, the Governor of the Bank of Korea freely grants approval of any bona fide exchange application for the purpose of making a payment or transfer for any current international transaction, subject only to verification that the application is for the purpose of current international transaction and not for the purpose of transferring capital. Accordingly, the staff notes that Korea now maintains an exchange system that is free of restrictions on payments and transfers for current international transactions.

The following draft decision is proposed for adoption by the Executive Board

The Fund notes with satisfaction that with effect from November 1, 1988 Korea has accepted the obligations of Article VIII, Sections 2, 3 and 4 of the Articles of Agreement.

Attachment

OFFICE OF THE MINISTER

MINISTRY OF FINANCE
REPUBLIC OF KOREA
GWACHUN, KOREA

OCTOBER 31, 1988

MR MICHEL CAMDESSUS
MANAGING DIRECTOR
INTERNATIONAL MONETARY FUND
WASHINGTON, D C , 20431
U S A

DEAR MR MICHEL CAMDESSUS

I WISH TO INFORM YOU THAT THE REPUBLIC OF KOREA, IN ACCORDANCE WITH ARTICLE XIV, SECTION 1 NO LONGER WISHES TO AVAIL ITSELF OF THE TRANSITIONAL ARRANGEMENTS OF ARTICLE XIV, OF THE ARTICLES OF AGREEMENT AND IS PREPARED TO ACCEPT THE OBLIGATIONS OF ARTICLE VIII, SECTIONS 2, 3 AND 4

YOURS SINCERELY,

IL SAKONG
MINISTER OF FINANCE AND
GOVERNOR FOR THE
REPUBLIC OF KOREA

CC Foss
SC
DS



Office Memorandum

To Ms Tscng

June 22, 1998

From J R Dodsworth *(RD)*

Subject **Korea Rescue Loans**

Please find attached the requested information on rescue loans received from MOFE today

98 JUN 22 AM 8 14

1 What is the definition of a rescue loan?

1-1 The rules and regulations of Banking Supervisory Authority (BSA) define a rescue loan as follows

A loan which a group of banks offer to assist recovery of a firm and to minimize the loss of banks by the lead of main creditor bank under the judgement that a firm can be recovered within 3 to 4 years

1-2 Following are measures creditor banks should take before they give a rescue loan according to the rules and regulations of BSA

- o Creditor banks should be delegated property disposal rights and take measures which are needed to secure obligatory rights

- o Creditor banks should establish rules that state how to handle and call in a rescue loan

1-3 The rules and regulations of BSA also prescribe follow-up measures subsequent to offering a rescue loan

- o Creditor banks should file related information on an obligor and make checks every month as to whether an obligor is implementing a self-rescue plan and redemption of debt plans faithfully

- o Creditor banks should analyze financial statements, results of operations, and related reports and use them to review a self-rescue plan at least once a year

- o If a rescue loan recipient does not display a commitment to pursue a turn around or knowingly does not follow a rescue-request of creditor banks, creditor banks can stop offering loans and take actions to liquidate the firm after discussing the matters among themselves

- o Creditor banks should prohibit an obligor from giving dividend to large stockholders until an obligor fully repays its debt or returns to normal condition

o If an obligor follows a self-rescue plan very well, creditor banks can change their rescue plan such as cutting the period of waiver of an obligation, dwindling loans whose interest is waived and changing interest rates ✓

2 Do banks have to report "rescue loans" to the FSC(or how is this information collected)?

2-1 Yes

Creditor banks are required to report to the BSA in writing immediately when they decide to make a rescue loan

Creditor banks are required to report to the BSA in writing how an obligor follows the self-rescue plan every 6 months

3 Is there any further information on the terms (ie interest rates, maturity) and other conditions for these loans? If not, can we say why we don't have these informations?

3-1 regarding whether to violate 'Fair Trade Act'

- It is violation against the Fair Trade Act for creditor banks to offer a rescue loan whose terms such as interest, amount, loan-period are identical, for it restrains commercial banks' competition

- However it does not matter if creditor bank extends a rescue loan with different terms, and any creditor bank can reject the rescue loan if loan terms presented by the firm concerned are unreasonable in its judgement. ✓

3-2 regarding how to handle

- Creditor banks' non-performing loans can be enlarged if a rescue loan is offered without objective criterion of deciding recipients of a rescue loan amount of loan, decision-making procedure etc

- Even though it thoroughly depends on the bank whether it offers a rescue loan, the rescue loan is treated by the bank's internal regulation to minimize the subjectivity
- o And creditor banks are now disclosing the procedures and contents related to the rescue loan for securing transparency
- o In determining which companies a rescue loan will be extended to, creditor banks will consider particular companies that are suffering from temporal financing difficulties have the potential to continue business operations based on objective materials such as its business prospect a self-rescue plan management ability, etc
- o The timing and amount of a rescue loan is determined complying with the firm's request by discussion with creditor banks in order to rehabilitate the firm

3-3 regarding interest rate and loan-period

- The interest rates and period of a rescue loan are determined on a commercial basis by reflecting the characteristics of the firm
- o Creditor bank sets interest rate as prime rate plus spread which can be decided by considering each bank's funding rate, firm's credit grade and contribution to that bank
- * The interest rates of the rescue loan ranged from 13.0% to 24.8% since Oct 1997 which can be divided as 13.0%~22.4% before Nov 1997, 16.0%~24.8% after that.

* The trend of prime rate of creditor banks (Month, %)

97.10	97.11	97.12	98.1	98.2	98.4	98.5
8.5	8.5	9.5-11.75	11.5-11.75	11.5-11.75	11.5-11.75	11.5-11.75

- o Some creditor banks offer a rescue loan with lower interest rates in contrast with normal interest rates but this favorable purpose, or bank's credit policy is to quickly normalize the firm through reducing financial cost burden

- o It is normal for creditor banks to adjust interest rates when the firm has completed or executed its rescue plan to a satisfactory level in order to recover losses incurred due to reduced rates
- o Loan-period to be set somewhere between four months to one year for rescues loans after Oct 1997 is also determined by each bank in proportion to period that the firm needs a rescue loan

3-4 the role of parties concerned for normalization of the firm

- (the responsibilities of owner) In that the owner has the social responsibilities for the insolvent operation, he might dispose of his personal properties for repaying the obligations of the firm concerned (corresponding to execution of his guarantee for the firm's debt to creditor banks) or delegate managing right to professional management.
 - o The owner disposes of or delegates to creditor banks the right of disposal of his own properties excluding properties not appropriate to their disposal such as houses
 - o The owner renounces the right of management.
- (the responsibilities of shareholders) Shareholders have to be ready to suffer losses arising from free issue of new shares, non payment of dividend and drop in their stock price due to disposal of related affiliates, mortgaged assets or other assets to the extent that they neglect their role in monitoring and supervising firm's management.
 - (the responsibilities of management) In general, management involved in the insolvent operation are replaced and other existing management have to suffer wage cuts
- (the role of creditor banks to minimize their loss) Creditor banks admit that insolvent firms repay obligations in lower interest rates than that of normal level until they are recovered

• 81

But creditor banks try to secure obligatory rights by receiving additional collateral and urging them to follow a rescue plan

- o Creditor banks try to take, as security, shares of firms owned by parties concerned such as owner, management. seek for concealed properties and get disposal rights of them
- o Creditor banks play a monitoring and supervising role together with other banks in such as preservation of collateral and monitoring for a fund supply and demand program by sending a managing agency to the firm concerned

4 Other than Dong-Ah Group, can we say whether any of the other groups are restructuring (either on their own or forced by the creditor banks)?

4-1 BSA instructed main creditor banks to make an agreement with each group so as to improve its financial structure on Feb 13 1998

The major contents of that agreement for next 5 years include .

- o plan to reduce the debt ratio of the entire group on a gradual basis
- o self-rescue plan and debt repayment schedule for the entire group
- o restructuring plan for the entire group
- o improvement on corporate governance etc

4-2 Main creditor banks made agreements to the contents of restructuring in free consultation with groups

The ways for major groups' restructuring are as follows

✓

- o debt reduction by way of asset, business and subsidiary disposal
- o expansion of own funds by inducing foreign investment and increasing capital
- o subsidiary liquidation

4-3 For your reference corporate viability assessment committee of each bank reviewed the possibility of normalization of the debt-ridden companies for the acceleration of corporate restructuring and banks announced a list of 55 firms deemed non-viable on June 18 1998

The announcement of the hit list for liquidation will not end this time

4-4 Among 11 groups receiving rescue loans 7 groups such as Hanwha, Dong Ah, Kohap, Haitai, Shinho, New Core and Hanil are expected to set out group-wide restructuring more thoroughly with the liquidation or merger of their affiliates including nonviable companies

- o Especially, Hanil Group is forced to enter into overall group restructuring because Hanil Synthetic Co, its core company, is subject to possible liquidation along with 3 other companies
- o Dong Ah Group has already announced to dispose of its entire affiliates other than Dong Ah Construction Industry Its owner gave up his stock holding and management and further returned his private estates to his group to repay debt
- o Other 4 groups that received rescue loans, that is, Jindo Shinwon, Woubang and Whasung will liquidate some affiliates according to their own rescue-plan

CC - Foss
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Office Memorandum

To Mr Tseng
Mr Balno

June 22, 1998

From J R Dodsworth *JRD*

Subject **Korea FSC Financial Sector Restructuring Plan**

Attached is the public version of the FSC Plan dated June 19, 1998. I have talked to Mi Hun Jae Lee about potential differences between the plan and the previous LOI and will discuss further with FSC staff tomorrow and with the Chairman Lee on Wednesday.

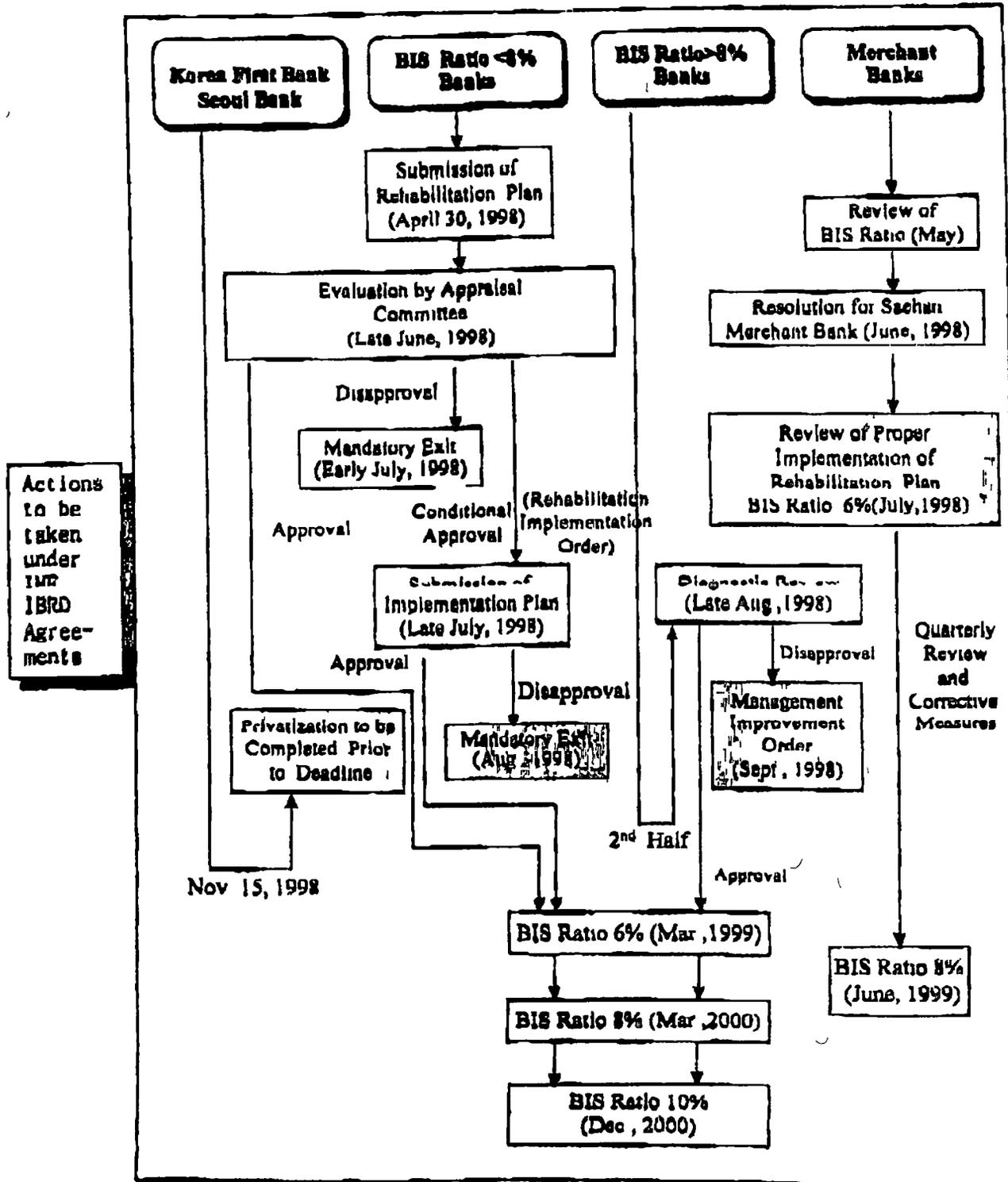
98 JUN 22 AM 8 14

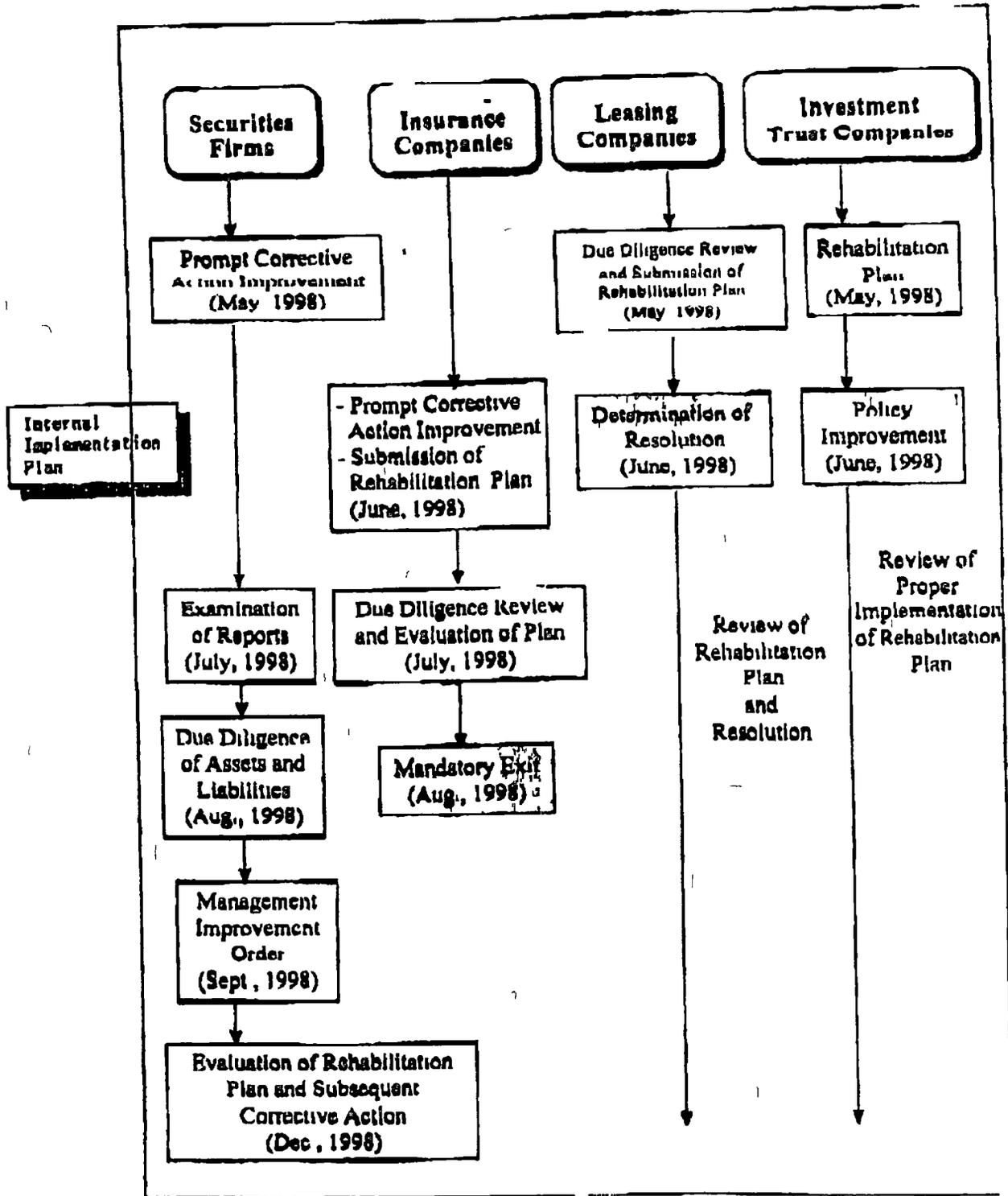
FINANCIAL SECTOR RESTRUCTURING

June 19th, 1998

Structural Reform Planning Unit

Financial Restructuring Plan





1 Bank Restructuring Plan

1 Implementation to-date and future plans

Financial restructuring is being carried out in accordance to the MOUs with IMF and IBRD as well as other previously announced plans

▶ Seoul Bank and Korea First Bank

o Privatization will be pursued in close cooperation with an internationally well-known lead manager, Morgan Stanley

o As the asset due diligence review by a foreign accounting firm (Coopers & Lybrand) is close to completion, the privatization of these two banks will be carried out ahead of the originally planned schedule of November 15, 1998

o If the sell-off to foreign financial institutions is not successful an alternative plan will be put into place

▶ 12 banks that fall short of BIS capital adequacy ratio of 8%

o Upon completion of asset appraisal reviews by respective accounting firms the Bank Appraisal Committee (consisting of 11 outside experts including academics, accountants, lawyers etc) will be formed (June 20, 1998)

o Rehabilitation plans submitted by each bank will be evaluated by this committee and the results of the evaluation will be reported to the Financial Supervisory Commission

o Taking into account the recommendations by the Bank Appraisal Committee, the Financial Supervisory Commission will prepare a corrective scheme for troubled banks

► 12 banks that satisfy the BIS capital adequacy ratio of 8%

- Upon completion of due diligence reviews by the end of August troubled banks will be subject to forceful management improvement orders, such as the change in management or merger with another bank

2. Implementation Scheme

- Restructuring of the banking sector will be pursued in accordance to the following basic principles

- ◇ Subsequent to a realistic assessment of the size of non-performing loans through assets due diligence reviews by respective accounting firms, full provisioning and write-off based on the actual size of NPLs will be pursued and as a result total capital at banks will be reduced leading to the deterioration of BIS ratio

- The additional capital needed to achieve a BIS ratio of 8% will be determined and the regulatory authority will evaluate the feasibility of capital increase to make up for capital deficiency

- However, there are concerns of a liquidity squeeze as banks are expected to call back or suspend loans for the purposes of achieving BIS ratio of 8%. As such, a stage-by-stage approach in achieving BIS ratio over a 2 year period will be allowed

Set the minimum intermediate target for March 1999 at BIS ratio 6% and review the progress of implementation on a quarterly basis in order to encourage an early achievement of such targets

Apply a more lenient set of BIS ratios for regional banks and commercial banks that do not lend in amounts above a set amount (eg, 5 billion won) to an individual corporate and that do not engage in international business

	<u>Mar 31, 1999</u>	<u>Mar 31, 2000</u>	<u>Dec 31, 2000</u>
- banks that engage in international business	6%	8%	10%
- banks that do not engage in international business	4%	6%	8%

◇ The Bank Appraisal Committee will evaluate recapitalization plans after a comprehensive review of adequacy in capitalization asset soundness profitability, liquidity, management expertise and the prospects of future achievement of respective BIS ratios and will make recommendations as to whether a certain bank should be given an approval conditional approval or disapproval classification

□ Measures to be undertaken subsequent to appraisal results

◇ With the input from appraisal results from the Bank Appraisal Committee FSC will closely examine the feasibility of achieving BIS target ratios and arrive at either an approval, conditional approval or disapproval classification for each bank

0 Approval

Mandated to prepare and submit a MOU containing detailed quarterly implementation plans

Implementation of rehabilitation plans will be monitored on a continuous basis and in the event the plan is not being implemented accordingly, management improvement measures such as capital reduction, change in management or merger will be imposed

0 Conditional approval

Submission of implementation plans within one month since the date conditional approval was obtained This plan should contain contents

summarized below

- In the event of disapproval of an implementation plan a mandatory merger order or transfer of business order will be imposed

<Content of Implementation Plans>

- Change in management
- Capital reduction
- Expense reduction through adjustments in organization personnel and compensation schemes as well as improvement in profitability

Maintenance of sufficient liquidity

Plans of recapitalization, such as merger joint venture or rights issue

o Disapproval

Mandatory merger or transfer of business under a purchase & assumption arrangement will be ordered

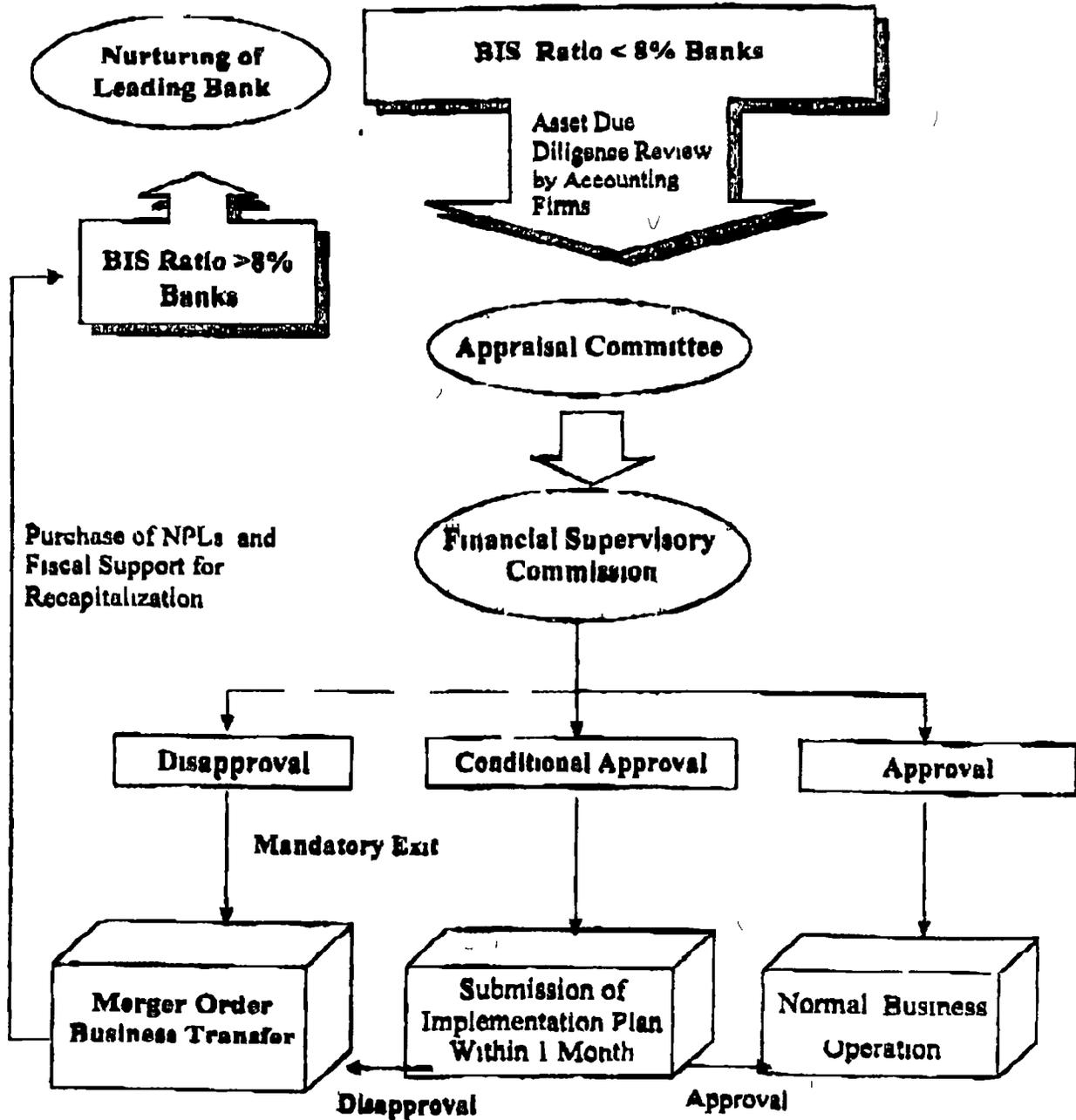
- Banks identified as being conditionally approved or disapproved that voluntarily pursue mergers with sound banks will be exempt from mandatory exit
- In parallel schemes to minimize the possible side effects arising from disruptions to the financial market during the bank resolution process have to be put into place

x Purchase and Assumption Arrangements

- Troubled bank will transfer its good assets and debt to a sound bank

If the failing bank's total liabilities exceed total performing assets the

Resolution for Non-Viable Banks



Korea Deposit Insurance Corporation (KDIC) will cover the discrepancy by injecting capital and etc (examples of providing fiscal support to cover excess liabilities of troubled banks can be found in many foreign countries as well)

3 Fiscal Support for Bank Restructuring

Size of Fiscal Support

- o Fiscal support for financial restructuring through issuance of bonds was set at 50 trillion won at the National Economic Council Meeting on May 20
- o This can be broken down as follows , purchase of non-performing assets 25 trillion won, recapitalization of bank 10 trillion won, deposit payment 9 trillion won

Underlying Principles are to minimize taxpayers' burden, mandate self-rescue efforts that match fiscal support levels, while at the same time establishing a responsible management system through loss sharing of shareholders by way of capital reduction and the removal of incompetent management

Fiscal support to be provided for through the issuance of bonds could either be through KAMC's purchase of NPLs of the troubled bank or through recapitalization provided by KDIC for the purposes of covering the deterioration of BIS ratio upon acquisition of a troubled bank

o Voluntary merger between banks and the inducement of foreign investment will be encouraged through support measures such as the purchase of NPLs and recapitalization

o Details pertaining to support method and criteria will be decided after consultation with the Ministry of Finance and Economy the Planning and Budget Committee as well as other related authorities

4 Supplementary Measures

- Amendments to related Taxation Law and the [Act Concerning the Structural Improvement of the Financial Industry] are necessary for the facilitation of mandatory exit of troubled banks
- Contingency programs to minimize adverse side effects such as disruptions to the financial market as a result of bank restructuring have been devised, in consultation with Ministry of Finance and Economy and the Bank of Korea
- Evaluate the level of support provided to small-to-medium sized enterprises by banks as of the end of June and differentiate the level of support to concerned banks accordingly as a way to encourage support to such enterprises who are likely to receive less attention especially throughout the bank restructuring process

All banks are categorized into one of three categories (A, B, C), where banks categorized as A and B banks will be provided with subordinated loans or capital injection amounting to 1 trillion won on a 2:1 basis.

In addition, subordinated loans etc worth 1-2 trillion won will be provided to banks in accordance to support level to small-to-medium sized enterprises

- Enhancement of prudential regulation through amendment of related regulations
- Adopt transparent accounting principles through mark-to-market accounting and strengthened disclosure requirement for NPIs
- Resolve disproportionate lending practices through the reduction of lending amounts that surpass large exposure limits etc
- Strictly enforce prompt corrective actions for the prevention of and

contraction of problems embedded in the system

- o Strengthen prudent management through amendments to the asset soundness classification standards
- It is important for financial institutions to resolve NPLs to the greatest extent and to eliminate the possibility of additional NPLs especially with bank restructuring moving forward in a more accelerated pace
- o From the point of view of financial institutions, as the borrowing limit toward a business group (chaebol) is to be reduced, further lending to such groups will be difficult
- o In preparation of such a situation each business group should push hard toward corporate restructuring efforts through the reduction of corporate debt ratios

II Non-bank Restructuring Plan

- ◇ Insolvent non-banking financial institutions that emerge as a result of bank restructuring will be subject to mandatory exit
- ◇ As non-bank financial institutions have majority shareholders, self driven rehabilitation through recapitalization will be encouraged under the responsibility of major shareholders. However, if a recovery is deemed unrealistic those institutions will be exited without hesitation
- Leasing Companies
 - o Leasing companies with eroded capital will be encouraged to exit the market. However, if the majority shareholders possess a clear commitment and have the capacity to recapitalize, those leasing companies will continue to operate. Troubled leasing companies will either be liquidated or exited by means of a bridge leasing company (June 1998)
- Merchant Banks

- o Determine a resolution scheme for Saehan Merchant Bank (June 1998) and review the satisfactory implementation of rehabilitation plans of other merchant banks in the event dissatisfactory implementation is revealed additional mandatory exits will be pursued (July, 1998)

Insurance companies

- o After receipt of rehabilitation plans (June, 1998) asset due diligence reviews will be conducted An appraisal committee will be formed and this committee will evaluate rehabilitation plans (July, 1998), after which the exit of troubled insurance companies will be pursued (August, 1998)

Securities Firms

- o After receipt of operational net capital ratio and asset liability ratio reports (July, 1998) asset due diligence review will be conducted Prompt corrective actions are to be imposed upon completion of asset due diligence reviews (September, 1998) and subsequent to review of management improvement plans appropriate measures will be imposed (December 1998)

Investment Trust Companies

- o Submission of rehabilitation plans has been completed (May 1998) and after a review of satisfactory implementation of such plans, management improvement measures will be imposed (September, 1998)
- o Amendment to related rules such as the adoption of mark-to-marketing of bonds and changes to the repurchasing system will be pursued in conjunction with bank trust accounts

The first round of financial restructuring will be completed by September, 1998, whereas restructuring of financial institutions that were not included in the first round will be dealt with after October, 1998



Office Memorandum

cc: FOSS
KM
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D5

To: Mr. Taylor

June 22, 1998

From: Manuel Guitián *ms*

Subject: **Korea—MAE Staff Visit**

A team from the Monetary and Exchange Affairs Department will visit Korea from July 8 to 22, 1998 in conjunction with the third quarterly review under the Stand-By Arrangement. The team will support the work of the APD review mission and focus on technical aspects related to the implementation of the program, especially in the areas of financial sector restructuring, market development, and prudential supervision. The team will comprise Messrs. Peter Hayward, David Woo, and Angel Ubide.

Questions regarding this mission may be addressed to Mr. Hayward (ext. 36616).

cc: Mr. Neiss ✓
Mr. Hayward

98 JUN 23 AM 10:40



INTERNATIONAL MONETARY FUND

Press Information Notice

EXTERNAL
RELATIONS
DEPARTMENT

NEISS, Hubert
ROOM HQ 4-320 0433

Press Information Notice (PIN) No. 98/39
FOR IMMEDIATE RELEASE
June 19, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Korea

On May 29, 1998, the Executive Board concluded the Article IV consultation with Korea¹.

Background

Until the financial crisis in late 1997, Korea had experienced a long period of rapid growth, low inflation, and a sustained improvement in the standard of living. Prudent macroeconomic policies and high domestic savings and investment contributed to the rapid transformation of Korea into an advanced industrial economy in four decades. The government had begun an economic reform program—which gained momentum in 1993-96—to gradually liberalize financial markets and the capital account.

Capital account liberalization, however, was not well sequenced nor accompanied by the necessary reforms and strong prudential supervision of the financial system. The vulnerabilities of the economy to external events stemming from weaknesses in the corporate and financial sectors were not fully recognized. Controls on short-term external borrowing by banks were eased, but controls on medium- and long-term capital remained in place. In 1994-96, Korean conglomerates undertook an aggressive investment drive financed by large increases in borrowing from domestic banks, which, in turn, sharply increased short-term external borrowing. During 1997, an unprecedented number of highly leveraged conglomerates went into bankruptcy as the buildup in capacity proved unviable owing to the depreciation of the yen, a sharply adverse movement in Korea's terms of trade, and the slowing of domestic demand in 1996. The

¹Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

bankruptcies resulted in a severe deterioration in the balance sheets of Korean financial institutions

The onset of the crisis in Thailand in mid-1997 brought Korea's financial and corporate sector problems into sharper focus and increased the concerns of foreign creditors about the soundness of Korea's financial system. With markets already apprehensive, the correction of the Hong Kong stock market in late October 1997 triggered a massive and sudden loss of market confidence. In the weeks that followed, credit lines to Korean banks were cut back severely and usable reserves fell to critically low levels as the Bank of Korea provided emergency foreign exchange support to Korean banks to avoid default. Korea entered into a Stand-By Arrangement with the IMF on December 4, 1997.

The program supported by the Stand-by Arrangement has two main objectives: the restoration of confidence in the basic soundness of the Korean economy, and the fundamental restructuring of the financial and corporate sectors supported by far-reaching market opening to lay the basis for recovery and growth. In the immediate period of the crisis, monetary conditions were tightened in support of the stabilization of the foreign exchange market. With the stabilization of the foreign exchange market, interest rates have fallen substantially in recent months. Fiscal policy has been flexible so as not to aggravate the downturn in economic activity. The program for 1998 envisaged a fiscal deficit of 1.7 percent of GDP, close to the estimated cyclically neutral deficit, and allowed for increased social safety net expenditures. The social safety net has been improved through a widening of the coverage and extension of benefits. Structural reforms have been accelerated. In the financial sector, an autonomous consolidated supervisory agency has been established, the merchant banking sector has been rationalized with the closing of about half the original number of banks and approval of recapitalization plans of the others, and 12 undercapitalized commercial banks have been asked to submit recapitalization plans by end-June. With regard to corporate restructuring, large conglomerates have been required to publish combined financial statements by next year, shareholder rights have been strengthened, and bankruptcy procedures improved. Restrictions on foreign investment in domestic equity, bond, and money markets have been eliminated and foreign direct investment substantially liberalized. In addition, legislation has been passed to increase labor market flexibility.

Substantial progress has been made in overcoming the immediate external financial crisis, and the won has appreciated and stabilized. A debt restructuring agreement with foreign banks was finalized at end-March and in early April, the government issued \$4 billion in a global bond issue. The current account balance has turned into a substantial surplus (some \$14½ billion in the first four months of 1998) and there have also been significant inflows of portfolio capital. Usable reserves have been rebuilt to exceed pre-crisis level—reaching \$34½ billion by end-May.

The impact of the crisis on the real economy, however, has been severe. After growing at 5.5 percent in 1997, real GDP contracted by 3.8 percent in the first quarter of 1998, as the decline in consumption and domestic investment outweighed the strong positive stimulus to growth from net external demand. The unemployment rate reached 6.7 percent in April 1998 (compared with 2.5 percent in 1997). In spite of the won depreciation, inflation has been subdued, reflecting falling domestic demand and the absence of wage pressures.

Executive Board Assessment

Executive Directors commended the authorities for their steadfast implementation of their wide-ranging stabilization and reform program. This had contributed to a rapid rebuilding of usable reserves, the strengthening and stabilization of the won, and Korea's successful re-entry into international capital markets. Directors stressed that international confidence in the authorities' commitment to reforms had been a key factor contributing to these achievements. Nevertheless, they cautioned that confidence remained fragile—as indicated by the more recent weaknesses in the equity market—particularly given the severe downturn in economic activity and the difficult challenges that were widely recognized to remain ahead. Several Directors noted that the weakening of the yen and adverse developments elsewhere in the region were also likely to make Korea's situation more difficult. Directors urged the authorities to persevere with the determined implementation of the reform program, especially as the contraction in output will be sharper than originally anticipated, with unemployment expected to continue rising. Directors stressed the importance for the successful implementation of the program of continued efforts by the authorities to maintain social consensus and stability. In this context, they emphasized the need for an adequate social safety net to protect vulnerable groups in the economy that are adversely affected by the restructuring process. Directors welcomed the initiation of the second-round tripartite committee.

To lay the basis for recovery, Directors urged the authorities to continue to pursue policies to safeguard the gains in confidence, preserve social stability, and decisively address weaknesses in the financial and corporate sectors. In particular, Directors advised the authorities to continue to focus monetary policy on maintaining exchange market stability. Directors saw scope for further gradual reductions in interest rates, provided the exchange market remained stable.

Directors viewed fiscal policy as prudent, and many supported a further widening of the deficit through the operation of automatic stabilizers, should the economic downturn prove to be worse than currently expected. Indeed, in light of the severity of the downturn, many Directors observed that additional social expenditures were desirable to help preserve social consensus, and supported a modest further widening of the fiscal deficit to allow additional social safety net expenditures.

Directors considered decisive action to strengthen the financial system to be imperative in the period ahead. They welcomed the progress made in rationalizing the merchant banks, and emphasized that focus should now shift to creating a sound and more efficient commercial banking sector. In this context, Directors were encouraged by steps taken to prepare two major intervened banks for privatization. They emphasized that the decisions expected shortly on the recapitalization plans of undercapitalized banks should be made with the benefit of a rigorous review of the magnitude of the nonperforming loan problem.

Directors welcomed the authorities' recent efforts to make public a more realistic assessment of the size of the nonperforming loan problem and the commitment of public resources to support financial sector restructuring. They underscored the importance of setting clear conditions on the use of public resources for bank recapitalization. Systemic importance and clear market

indications of viability, as signaled by the willingness of private parties to inject new capital, should be criteria in the provision of such assistance. In this regard, several Directors cautioned against the provision of public funds for nonviable banks. Directors welcomed the authorities' plans to bring Korea's prudential regulations and supervision closer to international best practices. They regarded the proposed regulations relating to short-term external borrowing and foreign exchange exposure as especially important, particularly in view of the liberalization of the capital account. Development of the capital market was also seen as a key element in corporate restructuring and in mobilizing the high level of domestic saving more efficiently.

Directors saw corporate restructuring as a further key challenge facing Korea, emphasizing that delays would only serve to postpone economic recovery and undermine the credibility of the reform effort. Directors noted that the important steps taken to improve corporate governance and strengthen market discipline needed to be complemented by actions to deal decisively with corporate overindebtedness. In this regard, Directors pointed to the need to put in place a framework for corporate debt workouts by June. Some Directors expressed concerns that the making of "rescue loans" could impair banks' balance sheets and represent a return to former modes of lending, others regarded such loans as a temporary necessity pending a more coordinated corporate restructuring. As next steps in this regard, Directors identified the creation of debt workout units in commercial banks with the help of external audits, the formation of voluntary creditor committees, and improved disclosure to creditors by the large conglomerates. Directors underscored that corporate restructuring would also be spurred by the development of capital markets, the phasing out of cross-corporate payment guarantees, further opening up of the economy to foreign investment, and the strengthening of prudential regulations and supervision of banks.

Directors noted that, in view of the continuing difficulties experienced by small and medium-sized enterprises in obtaining trade financing, the provision of temporary credit support was necessary. They stressed, however, that trade financing and trade credit guarantee schemes should be time bound, provided on commercial terms, and not directed toward specific industries.

Press Information Notices (PINs) are issued, at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies.

Korea Selected Economic Indicators, 1992-98

GDP US\$442.6 billion (1997)
Population 45.2 million (1996)
Quota SDR 799.6 million

	1992	1993	1994	1995	1996	1997	Proj 1998
Real GDP (percent change)	5.1	5.8	8.6	8.9	7.1	5.5	1 to -2
Final domestic demand	3.9	5.3	8.8	8.8	7.0	0.8	-12.2
Consumption	6.8	5.3	7.0	7.2	6.9	3.5	-3.5
Gross fixed investment	-0.8	5.3	12.0	11.7	7.1	-3.5	-27.7
Stock building 1/	-0.5	-1.0	1.4	-0.5	1.2	-3.7	0.3
Net foreign balance 1/	1.7	1.4	-1.7	0.5	-0.8	8.6	10.9
Saving and investment (in percent of GDP)							
Gross national saving	35.3	35.4	34.8	35.2	33.7	33.0	32.3
Gross domestic investment	36.6	35.1	35.8	37.0	38.4	35.0	25.1
Prices (percent change)							
Consumer price (end period)	4.6	5.8	5.6	4.7	4.9	6.6	8.2
GDP deflator	6.1	5.1	5.5	5.6	3.4	2.4	7.8
Employment and wages							
Unemployment rate	2.4	2.8	2.4	2.0	2.0	2.7	6.5
Wages (annual percent change) 2/	15.7	10.9	15.5	9.9	12.2	5.2	7.8
Consolidated central government (in percent of GDP)							
Revenues	18.2	19.3	20.2	20.7	21.9	22.2	22.8
Expenditure	18.9	19.0	19.7	20.3	21.7	22.2	24.5
Balance	-0.7	0.3	0.5	0.4	0.3	0.0	1.7
Money and credit (annual percent change)							
MCT (end of period)	22.2	22.4	24.4	23.0	17.4	11.5	10.1 3/
M3 (end of period)	20.9	18.5	26.7	19.1	16.7	13.9	14.9 3/
Yield on corporate bonds (percent period average)	16.2	12.6	12.9	13.8	11.9	13.4	18.1 6/
Trade (percent change)							
Export volume	8.1	7.0	14.8	24.0	19.8	24.9	13.8
Import volume	2.0	1.4	21.5	21.2	12.6	1.5	11.3
Terms of trade	0.3	-1.1	1.5	-3.6	-12.3	11.3	1.9
Balance of payments (in billions of US\$)							
Exports f o b	76.2	82.1	95.0	124.6	130.0	138.6	145.5
Imports f o b	78.0	79.8	97.8	129.1	144.9	142.5	118.9
Current account balance	3.9	1.0	3.9	-8.5	-23.0	-8.6	23.1
Current account balance (in percent of GDP)	1.3	0.3	-1.0	1.9	-4.7	-1.9	7.3
Usable gross reserves 4/							
In billions of U S dollars (end of period)	17.1	20.2	25.6	28.5	29.4	9.1	34.5 6/
In months of imports of goods and nonfactor services	2.2	2.6	2.6	2.2	2.0	0.6	
External debt 5/							
In billions of U S dollars					157.5	154.4	163.3
In percent of GDP					32.5	34.9	51.5
Exchange rate (end of period)							
Won per U S dollar	788.4	808.1	788.7	774.7	844.2	1 695.8	1 400.8 6/
Nominal effective exchange rate	87.4	84.7	82.5	83.7	80.0	49.0	
Real effective exchange rate	95.2	94.8	95.0	98.9	97.2	62.4	

Sources: Bank of Korea Monthly Statistical Bulletin; IMF International Financial Statistics; data provided by the Korean authorities; and IMF staff estimates and projections.

1/ Contribution to GDP growth

2/ Monthly earnings in manufacturing

3/ February 1998

4/ Excluding deposits at overseas branches and subsidiaries of domestic banks

5/ Includes offshore borrowing of domestic financial institutions and debt contracted by overseas branches of domestic financial

6/ May 1998



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June 19 1998

To Ms Iseng

From J R Dodsworth

Subject Korea Domestic Banks' Repayment Schedules

As envisaged in the LOI, payment schedules have been agreed with commercial and merchant banks in respect of outstanding BOK foreign exchange support. The attached schedule indicates repayments of \$7.9 trillion in 1998 and \$3.3 trillion in the first half of 1999. The remaining balance (\$1.36 billion) is within the Bridge Merchant Bank.

One difference with the LOI is that the applicable interest rate has been reduced to LIBOR + 400 bp for amounts in 1998, but only to LIBOR + 600 bp for amounts in 1999.

금융기관 긴급자금 상환계획

(98 5월말 현재)

million
U.S. dollars

(단위: 백만달러)

잔액 98	6	7	8	9	10	11	12	98년중	99	1	2	3	4	5	6	99년중	총계
790	0	38	250	142	255	312	343	1340 (74.9)	0	53	39	0	160	198	450	1790 (100.0)	
825	141	121	91	198	219	254	246	1270 (69.6)	73	75	80	100	84	143	555	1825 (100.0)	
445	95	154	0	0	112	116	352	829 (57.4)	107	99	112	50	97	151	616	1445 (100.0)	
218	155	126	150	224	336	255	379	1625 (73.3)	68	53	155	64	62	191	593	2218 (100.0)	
995	15	70	0	100	110	120	130	545 (54.8)	50	60	60	60	110	110	450	995 (100.0)	
290	0	50	80	150	230	230	280	1020 (79.1)	40	40	0	40	70	80	270	1290 (100.0)	
269	30	30	30	30	30	30	89	269 (100.0)	0	0	0	0	0	0	0	269 (100.0)	
289	2	3	10	20	55	60	70	220 (76.1)	20	20	29	0	0	0	69	289 (100.0)	
89	2	3	5	10	12	15	20	67 (75.3)	5	7	10	0	0	0	22	89 (100.0)	
22	8	8	6	0	0	0	0	22 (100.0)	0	0	0	0	0	0	0	22 (100.0)	
75	5	5	0	0	15	15	17	57 (76.0)	3	5	5	5	0	0	18	75 (100.0)	
307	453	608	622	874	1374	1407	1926	7264 (70.5)	366	412	490	319	583	873	3043	10307 (100.0)	
165	0	0	9	0	10	10	95	124 (75.3)	2	5	3	8	23	0	41	165 (100.0)	
109	1	1	1	1	1	1	76	81 (75.0)	1	1	1	1	1	22	27	109 (100.0)	
167	0	0	0	30	30	36	30	126 (75.5)	5	5	10	5	5	11	41	167 (100.0)	
40	15	0	5	10	0	0	10	40 (100.0)	0	0	0	0	0	0	0	40 (100.0)	
126	2	3	5	16	19	24	27	95 (75.0)	5	7	6	6	7	2	32	126 (100.0)	
685	0	0	0	100	0	0	100	200 (11.9)	0	0	70	0	0	50	120	320 (19.0)	
291	18	4	20	157	60	71	338	666 (29.1)	13	18	90	20	35	85	260	926 (40.4)	
598	471	612	642	1031	1434	1478	2263	7930 (62.9)	379	430	580	339	618	958	3303	11233 (89.2)	

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6/19

From: John Dodsworth
To: WTseng
Subject: Supplementary Budget

Wanda:

As I mentioned on the phone, I have been discussing with Mofe officials plans for the second half of the year and have met strong resistance to the revisions to macro projections that are envisaged in the briefing paper. This evening I was called in by the Vice Minister to discuss macro policy direction in the short term. Mr. Chung announced that his staff had prepared a draft supplementary budget, the details of which are set out below. He would like to have an immediate response from the Fund as the plan is to be discussed with the President in broad outline in the next few days. I registered some initial reservations as to the underlying macro assumptions and size of the expanded deficit, and noted that this whole topic would need to be discussed in detail with the mission. I believe that there will be a time period for discussion if only because the National Assembly will probably not be in session until mid July at the earliest; but the higher the plan goes in internal discussions, the more difficult it will be for the mission to make changes. The Vice Minister also gave me an "aide memoire" on macroeconomic policy direction which I will send by fax.

The envisaged Supplementary budget will aim to inject additional funds into credit guarantee and other funds as well as expand the social safety net and increase spending on social overhead capital. Some additional offsetting revenue measures will be taken. These are seen as politically necessary as a form of "burden sharing" and because the authorities feel it imprudent to overly expand the fiscal deficit. Given the authorities' assumption that real GDP will contract by 2.5 percent in 1998, the net effect of fiscal measures would be to increase the fiscal deficit from 1.7 percent to 3 percent of GDP.

The breakdown of the planned measures is as follows:

Initial Deficit (won)	7.8	(trillion)
Tax Shortfall	4.7	
Increase in revenue	3.2	
Automatic redn in expenditure	1.0	
New expenditure	6.1	
New deficit	14.4	
less foreign funded exp (IBRD)	1.4	
Deficit of GDP)	13.0	(3 percent)

The anticipated new revenues are withholding tax on interest income (about w 800 billion), increase in gasoline/diesel taxes (200 billion),

primarily from shortfalls in earmarked taxes. New expenditures comprise an injection into credit guarantee funds of W1.4 trillion (which will be foreign financed), an increase of 0.2 trillion in export insurance, an increase of W1.1 trillion in the National Housing Fund, an increase in social overhead capital of W 1.9 trillion, and additional social safety net expenditure of W 1.5 trillion. There seem few details beyond these broad categories.

The deficit is expected to be bond financed. The Vice Minister said that initially the intention was to avoid monetization of the deficit but it would be necessary to assess the situation in the market as the year progressed.

Korea's Macroeconomic Policy Direction

1 Diagnostics of the Korean economy

As the economy was gripped in a war time 'survival mentality', total domestic demand in the first quarter has fallen over 29.4 per cent. Such a sluggish domestic demand engenders contraction in industrial production and average operation ratio of the manufacturing sector.

Also, an unemployment rate continues to rise, and it may cause social unrest by disrupting long-standing social cohesion in the Korean society.

Furthermore, owing to unfavorable external circumstances such as high yen/dollar exchange rate and low GDP growth in the Asia region, export growth marked a very low rate and even minus during last month despite a sharp currency depreciation.

All in all, these factors, if prolonged, may collapse Korea's industrial base, and undermine greatly Korea's growth potential.

2 Future macroeconomic policy direction

Without any doubt, tight macroeconomic policies are inevitable for a time during the period of crisis. However, economic policies should be pragmatic and flexible in advancing structural reform as rapidly as possible, as well as adapting to developments in the real economy. The Korean government views that this approach will be able to avoid overkill during the crucial period of transition period and successfully implement economic structural reforms.

With this direction as its impetus, **future macroeconomic policies will be centered on resolving a high interest conundrum and a credit crunch through normalizing financial system.**

3 Fiscal policy during the reform period

A high RP rate combined with the newly imposed regulation on the BIS capital ratio and the wave of insolvencies due to the punishing level of interest rate, is engendering a distortion in credit flows and a credit crunch. Supplied money quickly returns to the Bank of Korea since financial institutions including commercial banks tend to purchase RPs rather than to lend to the corporate sector.

Against this background, while it should support reform measures, the fiscal sector should serve as a conduit for money supply. However, newly envisaged fiscal policy does not intend to counter the current cyclical movements. Rather, it will have given priority to resolving the credit crunch *inter alia* by **injecting resources into the credit guarantee agency** to increase guaranteeing capacity for export or small- and medium-sized companies. It also aims at **expansion of a social safety net**.

Toward this end, although tax revenue will be reduced more than originally expected, due to the deceleration of economic growth, government outlays should be increased. **This implied an increase in fiscal deficit in consolidated government balance up to about 3 per cent of GDP**.

As for inflation, considering an asset deflation and decrease in real wage bills along with sharp decline in domestic demand, an inflationary pressure from the fiscal deficit will be subdued. In addition, the decelerating income velocity seems to suppress the possibility of inflation.



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June 18 1998
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To Ms Tseng
From J R Dodsworth

Subject Korea Corporate Viability Assessment

I am attaching a table on the 55 nonviable corporations that were identified yesterday. The data are rough in some areas, but give some indication of the size of the companies involved. The total direct bank indebtedness of the companies is estimated at W5.6 trillion. The W17 trillion quoted yesterday as potential non performing loans includes cofinancing arrangements and guarantees as well as bank liabilities.

I am also attaching a MOFE report on the viability exercise and a Q&A note on the same topic.

able Companies

(in million)

Group		Capital	Total Liab	Sales	Net Profit	Employees	Restructuring
Hyundai Livart	1	47 800	416 100	514 600	(45 800)	926	Merger w/affiliate
Hyundai Construction Equipment	2	10 000	66 600	112 700	300	635	Independent employee company
Hyundai Merchant Marine	3	2 000	21,400	25 600	200	5	Merger w/Hyundai Merch Marine
Hyundai Aluminum	4	21 200	120 500	158 600	(100)	538	Merger w/Koryo Ind Dev
Samsung Watch	5	86 500	77 800	33 600	(6 600)	87	Sale or liquidation
Daewoo Electric	6	6 900	176 300	59 200	(38,800)	630	Sale or liquidation
Daewoo Pharmaceutical	7	1 500	21 600	2 900	(4 800)	110	Sale or liquidation
Daewoo Cable Wire	8	10 000	92,100	81 300	(6 700)	311	Sale or liquidation
Daewoo Industrial Elect	9	1 148	27 751	20 874	(4 206)	127	N/A
Daewoo Auto Systems	10	6 400	21 556	21 050	(2 696)	58	N/A
Daewoo Electric Parts	11	13 240	42 761	79 600	739	5	N/A
Daewoo Construction	12	300	21 115	43 096	167	1 730	N/A
Daewoo Tech Industries	13	5 000	98 300	73 000	(18 200)	138	N/A
Daewoo Elect Parts	14	25 000	143 317	241 679	(8 343)	2 358	Asset sale & liquidation
Daewoo Energy	15	82	47 578	66 729	(1 671)	168	Equity disposal & liquidation
Daewoo Owenscorning	16	49 500	149 033	55 493	(11 172)	297	Equity disposal
Daewoo ENC	17	5 000	24,186	32 116	(3 600)	561	Sale or liquidation
Daewoo TV	18	10 000	12 900	2 900	(7 100)	56	Sale
Daewoo Storage	19	5 000	18 400	8 500	100	72	Acquire or sale
Daewoo Sangjin Shipping	20	200	97 900	36 100	(1 900)	205	Acquire
Daewoo 4 Group							
Daewoo Ssangyong							
Daewoo Ssangyong A Petroleum	21	20 000	597 000	2 153 900	(41 100)	490	Absorb HR to Ssangyong Oil
Daewoo Ssangyong	22	4 300	104 300	33 400	(9 700)	265	N/A
Daewoo Ssangyong Travel	23	1 800	42 200	6 400	(6 800)	156	N/A

Table Companies

(in million won)

Company Name	Year	Capital	Total Liab	Sales	Net Profit	Employees	Restructuring
Dong Ah Engineering	24	6 000	70 600	50 900	(5 800)	420	Liquidation
Hyosung Media	25	17,800	40 752	4 100	(1 772)	111	Sale
Hyosung Number One	26	3 000	4 486	281	(1 774)	15	Liquidation
Dong Kwang Chemical	27	1 550	2 740	2 644	(675)	34	Asset sale & liquidation
Cohap I T	28	1 000	240		(100)	4	Equity disposal
Cohap Fine Chemical	29	1 000	2 350	5 900	(100)	4	Sale or liquidation
Cohap Textile	30	3 300	68 900	29 500	(6 900)	150	Sale or liquidation
C N	31	4 000	-	15 500	40	94	Sale
Latari Distribution	32	29 800	377 000	400 500	(21 400)	2 343	Foreign asset sale
Latari Electronics	33	66 800	794 000	419 900	(139 100)	2 835	Asset sale
Latari Confectionery	34	44 600	1 086,100	789 000	10 400	4 226	Foreign asset sale
Hinho Trading Corp	35	23 500	294 900	237 900	(12 600)	203	N/A
Hinho Telecom	36	11 500	68 500	103 800	(20 600)	131	N/A
Coungjin Tech	37	24 500	133 200	31 900	(73 300)	36	N/A
Core							
Seow Town	38	6 700	76 327	24 700	(4 484)	875	Merger w/Department Store
Hu Dae Livestock	39	11,770	46 515	70 400	(17 927)	52	Merger w/Department Store
Hu Dae Distribution	40	10 513	185 257	204 900	(24 624)	372	Merger w/Department Store
Yong							
Se Han Tungsten	41	272 500	357 000	215 100	600	800	Sale & liquidation
Uopyong Ind Development	42	(25 900)	343 200	48,500	(18 900)		Liquidation
Uopyong Construction	43	26 000	182 700	118 500	200	170	Liquidation
Uuil Synthetic	44	97,900	1 140 100	697 500	(87 400)	1,500	Merger w/international company
Uhae Chemical	45	2 800	65 400	56 900	(12 400)	200	Sale
Ujju Development	46	22 000	80,300	16 400	(8 700)	270	Sale to US holding company
Uinnam Development	47	26 000	170,000	21 600	(19 700)	360	Sale to US holding company

**ble Companies
in million)**

		Capital	Total Liab	Sales	Net Profit	Employees	Restructuring
ul	48	4 150	48 500	15 750	(12 500)	300	N/A
inhan Fabric duk	49	5 000	68 900	16 600	(13 100)	225	N/A
ingguk Elect	50	99 250	332 394	126 331	(8 969)	883	N/A
ha	51	230	1 553	2 069	53	30	Liquidation
lang	52	1 090	12 000	37 900	(6 000)	500	Merger w/affiliate
e Sung Housing	53	1 700	81,100	32 480	(6,570)	438	In auction after bankruptcy on 6/10
uk Synthetic	54	8 400	-	63 000	200	230	In auction after bankruptcy on 5/30
ha Distribution	55	-	35 600	9 300	(1 000)		Takeover by 3rd party or liquidation
e Han Wool							
ig Young Paper							
o Jung Hospital							
al		1,141,323	8,611,311	7,733,092	(732,684)	27,739	
of cooperative loans							

Assessment on Corporate Viability: Progress Report

June 19, 1998

**Ministry of Finance and Economy
Republic of Korea**

1. Background

Korea's economic restructuring program consists of a coordinated, two-pronged approach which we believe is particularly germane given the close linkage between the financial and corporate sectors

Specifically, the government is exercising its supervisory power to enforce financial sector restructuring, which impels financial institutions, in turn, to apply corresponding pressure on corporations with regard to their debt reduction and business restructuring

In short, the government is creating the proper institutional framework to facilitate and monitor the restructuring process. This leaves the actual duty of corporate sector restructuring to the creditor banks themselves

This process has been underway since early May. The creditor banks' formal review committees completed their first round assessment of client firms, and on June 18, made a public announcement of the list of firms deemed to be financially non-viable. In making their assessment, creditor banks have been exercising full autonomy, and will continue to do so with regard to enforcing any necessary requirements for change.

As banks enforce more stringent standards on their client firms, increased bankruptcies and liquidations could potentially worsen the financial institutions' asset portfolios. The FSC will monitor the possible adverse incentive this poses for financial institutions with respect to enforcing a policy of no forbearance.

2. Assessment Results and Resolution Scheme

Coverage and Criteria of Assessment The assessment covers 313 corporations that show indications of significant financial weakness, most of which are subsidiaries of the 64 largest business groups, (*chaebols*), including those 11 business groups currently under co-financing arrangements made by creditor banks

The creditor banks' committees made their assessments on an autonomous basis. In order to ensure an objective decision-making process, a voting scheme was utilized by the assessment committees

Creditor banks established on an individual basis their own assessment criteria. Nevertheless, several core criteria have been commonly applied

- Financial standing of corporations
- Potential for future business profit
- Business capacity to accommodate financial costs

In addition, the following principles have been applied in the process of assessment

- The assessment of the future value of a business firm should be made assuming a normal interest rate, instead of the current, unusually high rate,
- The future value of a firm should be the primary criteria in viability assessment when such firm is indebted to more than one creditor bank

Assessment Results The assessment result shows that 55 corporations, which represent 17.6% of the total number of assessed firms, were classified as financially non-viable

Among those deemed to be non-viable, 52 corporations are affiliated with Korea's top 64 business groups, 20 of which are affiliated with the 5 largest business groups. The remaining 3 corporations do not have any affiliation with business groups.

- Korea's 5 largest business groups: 4 firms each from Hyundai, Samsung, and LG, 5 from Daewoo, and 3 from SK were deemed non-viable,
- Business groups ranked 6th to 64th: 32 firms from 15 business groups, including those 8 groups that are currently under co-financing arrangements.

Resolution Scheme The basic modality of resolution is as follows:

- Corporations classified as financially viable will receive full support from financial institutions,
- Those deemed to be non-viable (or, equivalently, classified as "subject to exit") will be subject to mandatory exit on a timely basis,
- Those classified as "subject to restructuring" will benefit from proactive support from financial institutions conditional upon self-rescue efforts.

Corporations deemed to be non-viable will not be able to receive any new credit from financial institutions. In order to facilitate their smooth exit, however, creditor banks will allow a grace period for repayment of loans falling due until the resolution scheme is finalized.

- Financial assistance across affiliate companies for the purpose of bailout will not be allowed, although the fulfillment of cross-debt guarantees can be enforced,
- Creditor banks will formulate, as soon as possible, specific resolution programs and a resolution timetable in consultation with the concerned corporations

For those non-viable corporations under court receivership or mediation proceedings, creditor banks will decide the resolution scheme by the end of July, creditor banks will either facilitate the legal process or induce third party acquisition, etc

Upon the completion of the first round assessment of client firms, creditor banks will establish workout units by June 20, in order to provide timely support to viable firms

Future Measures For the 5 largest business groups, illegal inside trading and financial assistance across affiliates will be banned

More importantly, the financial institutions' disproportionately large exposure to the 5 largest chaebols will be reduced. In this process, creditor banks will monitor and assess, on an ongoing basis, the financial viability of these groups, and take necessary actions if there is any further indication of financial weakness

To this end, major creditor banks will reformulate by the end of July their contract with the 5 largest chaebols for capital structure improvement to reflect specific steps to be taken for debt reduction

For SMEs, banks will sort out healthy firms, and will provide full financial support to them

3. Ancillary Measures: Alleviating the Credit Crunch

The already severe credit crunch is likely to further intensify over the course of financial and corporate sector restructuring. The Korean government has and will respond to this possibility by implementing various macroeconomic and financial measures.

Stabilizing Interest Rates At the macroeconomic level, monetary policy will be conducted more flexibly in order to create room for gradual interest rate reduction.

At the microeconomic level, the deposit insurance scheme will be revised so as to discourage adverse incentives on the part of banks' liability management. Under the current full protection on depositors, banks are inclined to offer high deposit rates without due consideration of risks involved.

Increasing Credit to Small and Medium Enterprises Banks plan to mobilize their own financial resources of 12.5 trillion won to be used exclusively for lending to SMEs. Also, they will convert the existing overdue loans made to SMEs into general loans. This will improve the access of SMEs to bank loans.

Expanding Credit Guarantee Facilities Credit guarantee agencies will expand their allowance by about 4 trillion won by strengthening their loan collection efforts and self-restructuring. The Korean government will allocate additional fiscal resources to credit guarantee agencies.

Furthermore, in order to improve efficiency, more credit guarantee services will be made available to healthy SMEs. A system of partial guarantee will also be introduced.

Expanding Trade Financing The Bank of Korea will expand its support for trade financing. The allowance of the Korea Export Insurance Corporation will be augmented from the current 20 trillion to 31 trillion won. The KEXIM Bank will also mobilize additional financial resources in advance of the original schedule.

Others: More financing facilities will be provided to housing investment and construction companies. The Korean government will set up a contingency plan in order to make a timely response to changes in market conditions.

Q & A
Assessment on Corporate Viability

June 19, 1998

Ministry of Finance and Economy

Contents

- 1 It seems that the government was involved in some parts of the corporate viability assessment process. Is this not going against the market principle?
- 2 The announcement had originally been scheduled to be made in early June, but was delayed to include the affiliates of the top 5 chaebol among those companies classified as non-viable. Why?
- 3 Although 20 companies affiliated with the top 5 chaebol have been ordered to exit as a result of the corporate viability assessment, they are relatively small and unimportant units. Will their exit be sufficient for the corporate reform of these conglomerates, and do the assessment results mean that there are no more non-viable companies affiliated with them?
- 4 Was the viability assessment made in a fair and objective manner? And, will an appeal be accepted for those companies that refuse to accept the judgment of mandatory exit?
- 5 Was there sufficient consultation with foreign banks in creating the list of non-viable companies?

6. Has the government discussed the viability assessment issue with international institutions, such as the IMF and the IBRD?
7. Samsung Motors is known to be experiencing financial difficulties, while problems concerning the government's industrial policy against duplicate investments are still being raised. What was the reason for Samsung Motors' exclusion from the recent list of non-viable companies?
8. Is it not against the principle of fairness that all other recipients of co-financing have been classified as non-viable with the exception of Dongah group?
9. The government announced that it would settle the problem of companies under court mediation and receivership, like Kia and Hanbo, as soon as possible. But it seems that the government can hardly solve the problem without the courts' agreement. What are the chances of an early settlement in view of the courts' positions?
10. Will the viability assessments continue on to the second or the third round for those pending companies which have not been judged as being non-viable in yesterday's announced results?

- 11 **The announcement of the results of the corporate viability assessment may worsen the credit crunch on the domestic financial markets. What measures have you prepared to deal with the possibility?**

- 12 **Will not the other affiliates of chaebol that have cross-guaranteed the debts of the non-viable affiliates become non-viable themselves?**

- 13 **Many people are currently working for the companies that have been judged non-viable. Have you prepared any measures to assist them?**

- 14 **What are the measures to protect minority shareholders who have invested in the companies judged non-viable?**

Question 1 It seems that the government was involved in some parts of the corporate viability assessment process. Is this not going against the market principle?

The government was not directly involved in the process of evaluation carried out by the financial institutions. However, the government did urge the financial institutions to do their best to make the judgments with integrity.

The reason for this urging was that, if the bad loans are allowed to increase further, not only would it become more difficult to protect the depositors and maintain the stability of the financial system, but also the burden of the accumulated bad loans would be ultimately laid on the general public in the process of consolidation. Thus, the government only exercised its supervisory rights to ensure the soundness of those financial institutions.

Question 2 The announcement had originally been scheduled to be made in early June, but was delayed to include the affiliates of the top 5 chaebol among those companies classified as non-viable. Why?

Affiliates of the top 5 chaebol were not initially subject to the assessment by corporate viability assessment committees, because of their cross payment guarantees or their apparent ability to repay debts. However, those companies, like affiliates of other chaebol ranked 6th and below, eventually came to be included, based on the judgment that there was a need to assess the soundness of each individual company as a separate and independent entity aside from its affiliation with the parent business group. The decision is only natural, considering that the top 5 chaebol need to lead the way in overcoming the current crisis as quickly as possible.

Question 3 Although 20 companies affiliated with the top 5 chaebol have been ordered to exit as a result of the corporate viability assessment, they are relatively small and unimportant units. Will their exit be sufficient for the corporate reform of these conglomerates, and do the assessment results mean that there are no more non-viable companies affiliated with them?

In the case of the affiliates of the top 5 business groups, even though there were signs of financial troubles, only a few companies had actual problems in repaying loans owed to the financial institutions. From the view point of the financial institutions, they could not judge a company as non-viable as long as it was paying interests on its loans on time. Part of the reason that loan repayment problems did not occur with these affiliates could be financial supports through internal transactions within the groups.

However, the corporate viability assessment ultimately aims to judge every pending company for its ability to survive independently. In the case of the affiliates of the top 5 chaebol, there is a high possibility that there were illegal intra-group financial supports. Therefore, more affiliates of the top 5 chaebol may be judged as non-viable in the future, regardless of yesterday's assessment results.

In the future, strict investigations into illegal internal transactions among the chaebol affiliates will be carried out to prevent intra-group financial supports. And, should any loan repayment problems occur to these companies as a result, financial institutions will be directed to continually assess their viability as an individual company.

Moreover, if the top 5 business groups do not carry out more active restructuring efforts such as business swap deals for their affiliates from the viewpoint of national competitiveness, financial institutions will be directed to stop providing further credit to these companies

Question 4 Was the viability assessment made in a fair and objective manner? And, will an appeal be accepted for those companies that refuse to accept the judgment of mandatory exit?

The criteria for the viability assessment were set by the individual creditor banks of their own. Therefore, we cannot say that all creditor banks relied on the same criteria, but the government had required the next two points to be considered in order to guarantee objectivity and fairness in the process.

1 The judgments should focus on an individual company's business prospects in terms of factors such as profitability and cash flow rather than its affiliation with other companies in the parent group.

2 The judgments should consider the future value of each company under normal interest rate conditions rather than the current high interest rate conditions.

Because these points were fully reflected in the assessment process along with the help of external experts in applying the newest credit risk management techniques, we are convinced of the fairness and objectivity of the results. Moreover, yesterday's assessment was to decide whether or not propriety of fresh loans will be given to the pending companies. However, this decision is ultimately to be made under the authority of the individual creditor banks and therefore, the ruling of mandatory exit will be difficult to reverse.

Question 5 Was there sufficient consultation with foreign banks in creating the list of non-viable companies?

We feel that there was no need to consult with foreign banks because the companies subject to the viability assessment have almost no borrowings from abroad. But should such assessments be required to be made on companies with large foreign bank loans in the future, consultation with foreign banks will be included in the process

Question 6 Has the government discussed the viability assessment issue with international institutions, such as the IMF and the IBRD?

The government closely consulted with officials from the IMF and the IBRD on the issue, and reached an agreement as to the assessment as well as general corporate restructuring processes. Both the IMF and the IBRD have sent delegates to discuss regularly with the Financial Supervisory Commission on various corporate reform issues. They have also provided technical support by hiring experienced consultants out of their own budget. Currently, Dr. Ira Liebermann, the head of the corporate restructuring team, is in Seoul to observe our progress in carrying out the restructuring process. He appears to be satisfied at least for confirming our firm will to reform by observing the assessment process of non-viable companies.

Question 7. Samsung Motors is known to be experiencing financial difficulties, while problems concerning the government's industrial policy against duplicate investments are still being raised. What was the reason for Samsung Motors' exclusion from the recent list of non-viable companies?

Samsung Motors is not classified as a company on the verge of insolvency as it is still in the initial development stages of its business. Financial institutions will decide whether they will extend or suspend the company's credit, as the process of voluntary restructuring in the automobile industry gets under way.

Question 8 Is it not against the principle of fairness that all other recipients of co-financing have been classified as non-viable with the exception of Dongah group?

Unlike prior cases, co-financing to Dongah group was not a bailout assistance. Financial assistance was given to the group as part of a "workout" process based on a loss-sharing agreement between Dongah and its creditor financial institutions. Dongah Group is expected to sell off of all its affiliates, with the exception of Dongah Construction. The owners will also give up the majority stakes and management rights as well as contribute privately owned real estate properties.

Such corporate restructuring cases in which a "workout" is established, with the owners giving up the business, could be applied not only to Dongah, but to any company facing financial problems as long as an agreement can be reached with its creditor financial institutions.

Question 9 The government announced that it would settle the problem of companies under court mediation and receivership, like Kia and Hanbo, as soon as possible. But it seems that the government can hardly solve the problem without the courts' agreement. What are the chances of an early settlement in view of the courts' positions?

Early settlements of issues concerning the troubled companies under court mediation and receivership still needs to be made within the legal framework

Under the new Composition Act and Company Reorganization Act revised in February this year, the creditor banks can promptly obtain the courts' agreement when the banks decide upon a reasonable course of action. Because of the introduction of the creditor council consisting of major creditors, it is now possible for the creditor banks' intention to be fully reflected in the settlement process. It is also possible now to terminate the process early, in the case in which the revival of the company is deemed improbable.

By utilizing these procedures, pending issues concerning court mediation and receivership may be settled at an earlier date.

Question 10 Will the viability assessments continue on to the second or the third round for those pending companies which have not been judged as being non-viable in yesterday's announced results?

In the case of the affiliates of the top 5 chaebol, the extent of the assessments was limited by the fact that publicly available accounting documents served as the only basis for judgment. If in the process of restricting intra-group financial supports, these companies fail to repay their loans, individual creditor banks will decide the viability of these companies.

For those business groups ranked 6th and below, sufficient evidence have been gathered in the process of their assessments, and therefore those not announced in the list of mandatory exit companies, have for the moment been classified as viable and will undergo an aggressive workout plan. However, if the company faces financial trouble during the process of restructuring, again it will be up to the creditor banks to decide the viability in each case.

Question 11 The announcement of the results of the corporate viability assessment may worsen the credit crunch on the domestic financial markets. What measures have you prepared to deal with the possibility?

It is possible that the announcement will cause a temporary clog in the financial market by destabilizing interest rates and stock prices as well as tightening the money supply

To cope with the possibility, we will

- 1 maintain a flexible money supply,
- 2 strengthen efforts to stabilize interest rates, such as stabilizing the call rates through open market operation, and
- 3 carefully supervise every financial institution to ensure proper supply of money, such as the special fund (worth 125 trillion won) for small and medium-sized firms, so that the damages will not spread to other companies that have business relations with the non-viable companies

After a transition period, the announcement will ultimately lead to stability by removing the uncertainties in the financial markets

Question 12 Will not the other affiliates of chaebol that have cross-guaranteed the debts of the non-viable affiliates become non-viable themselves?

There is a possibility that the companies which guaranteed the debts of the non-viable companies will become non-viable as well when they become incapable of repaying the debts. In such a case, the matter will most likely be settled in the end by a sharing of the losses between the company and its creditor banks. Again, this is one part of the aforementioned process known as "workout".

Question 13 Many people are currently working for the companies that have been judged non-viable. Have you prepared any measures to assist them?

We believe that some of these people will not have to leave their jobs if the companies they are working for are merged into or acquired by financially healthy companies, be they domestic or foreign. Some people will also be able to get a job at other companies. However, we foresee that quite a lot of those people will inevitably be out of employment due to the tight job market.

Unfortunately, it is difficult for the government to provide special arrangement for these people, nevertheless. The government will, however, do its best to provide them with every possible means of assistance within the existing framework of retirement payments, unemployment insurance and other general support measures for the unemployed.

Since a lot more people than originally expected are projected to lose their jobs in the ongoing process of corporate and financial restructuring, the government plans to strengthen general unemployment policies even at the cost of extending deficits in public finance.

Question 14 What are the measures to protect minority shareholders who have invested in the companies judged non-viable?

Since an investment in a company is made at one's own risk, the government will not prepare any measure to compensate the losses from having invested in the companies which will be forced to exit. However, the listed companies judged as non-viable will not be immediately unlisted from the stock market, and part of the investment may be redeemed through selling off of company assets.

~~WJF~~

~~AN~~

cc: FSS

BIS

Jim W

cc

98 JUN 18 AM 8:04

To M^s Tseng
From J R. Dodson

Subject: Non viable Firms

Attached are "initial" translations of
the speeches made by the Chairmen of
KCB and FSC earlier today.

Results of Corporate Viability Assessment

1 Progress to-date of Corporate Viability Assessment

- A total of 313 corporates, including corporates in 11 business groups that are recipients of cooperative assistance, as well as troubled corporates belonging to the big 64 business groups were assessed in the recent corporate viability assessment
- As for the corporates belonging to the top 5 business groups, they were excluded at first as they were deemed to not have problems in connection with repayment of liabilities. However, under the judgement that the assessment of those corporates in accordance to the soundness of the individual corporate is needed as well, they were added onto the list of corporates to be identified
- Corporate Viability Assessment Committees at each bank came up with internal assessment results by June 13 and following a period of reconciliation to resolve discrepancies among banks the final results were conceived on June 17
- The banks' assessment process was based on the principle of voluntary decision-making and after a sufficient level of discussion between members of the assessment committees, objective measures such as voting were utilized to arrive at final results
- In principle, criteria for viability assessment was left for each bank to decide on their own. However, there were some common criteria. For example, financial standings, capacity to create profit-making opportunities or capabilities to endure financial costs were commonly considered throughout the evaluation process
 - Instead of evaluating a corporate's viability under the current high interest rate environment, normal interest rate levels were applied when calculating a corporate's future value,
 - Much weight was placed on the corporate's future value when it came to making reconciliation toward the viability of a certain corporate during deliberation sessions between banks

2. Results of Corporate Viability Assessment

- The recent assessment revealed that 55 corporates, which represent 17% of total number of corporates subject to the assessment, are subject to mandatory exit
- Among the 55, 20 corporates are affiliated with the top 5 business groups, 32 with the 6th-64th ranking business groups, while the remaining 3 do not have any affiliation with business groups
 - Corporates that are subject to exit and are affiliated to top 5 business groups are 4 corporates each from Hyundai, Samsung, LG groups, 5 from Daewoo and 3 from SK
 - Among the 6th-64th ranking business groups, 15 corporates, which include 8 corporates in the business groups that are recipients of cooperative assistance were evaluated as corporates subject to exit

3. Restructuring Scheme

- Corporates classified as "viable" will receive full support from financial institutions, whereas corporates that are classified as "subject to exit" will be exited on a timely basis and those that are classified as "subject to restructuring" will benefit from proactive support toward restructuring from financial institutions to the degree of self rescue efforts displayed on part of the corporate itself
- New credit from financial institutions to corporates that face mandatory exit will be suspended. However, for the smooth exit of corporates, upon deliberation between credit banks, a grace period for repayment of loans reaching maturity will be applied until the resolution scheme is finalized
 - Although the fulfillment of liabilities guarantee by affiliate companies is allowed, financial assistance for the purposes of continuing operations will not be permitted

Specific timetable and scheme for the exit of such corporates will be set in a timely manner by creditor banks after consultation with the concerned corporates

- Among the 11 business group recipients of cooperative assistance, 7 business groups, that is, Hanhwa, Dongah Construction, Gohap, Haitai, Shinho, New Coro, Hanil will be subject to exit and groupwide restructuring
 - As 4 corporates of the Hanil business group, including a core unit Hanil Textile, are subject to mandatory exit, a serious restructuring of the overall group will be required
 - As for Dongah, it has already announced plans to dispose of all of its affiliates except for Dongah Construction, and the majority shareholder of the group has decided to give up its share holdings as well as management position and has contributed privately owned real estate property
- Among the rest of the 11 recipients of cooperative assistance, Jinro group will be handled under the mediation and court receivership proceedings and corporates of Jindo, Shinwon, Woobang will, depending on internal decisions, either be exited or will be provided with support toward their restructuring efforts
 - Hyosung, which although is not a recipient of cooperative financing but is facing difficulties in fundings at it's core unit Hyosung Industries, is subject to the exit of 3 affiliates including Hyosung Media, while other restructuring measures within the group will be pursued such as mergers or sell-offs
 - For those corporates that are under mediation or court receivership, such as Kia and Hanbo, creditor banks will prepare by the end of July schemes to facilitate the legal process or to induce a third party acquisition etc

FSC Chairman Announcement

1 Corporate Restructuring and Viability Assessment

- From the point of view of financial institutions, the current restructuring efforts represent a core piece of economic reform pursued by the Korean government and can be taken as a process of connecting problem loans or possible problem loans of the future that are embedded in the system
- Along these lines, financial institutions' practices of suspending credit extension to corporates that do not possess the capacity to make repayment on their liabilities and on the other hand continuing support to corporates of which a prompt repayment is expected, in fact coincide with the process of assessing corporate viability
- Corporate viability is assessed on a routine basis at most of the financial institutions of advanced nations and therefore it could be said that corporate restructuring is carried out on a continuous basis in those countries
- However, the corporate viability assessment mechanism has not been put into work at financial institutions in Korea and the number of troubled corporates have been accumulating ever since, calling for the resolution to provide a one shot solution to overhaul the system, according to restructuring plans
 - Once the financial system is rehabilitated, financial institutions will be transformed and will regard the evaluation of corporate viability as an ongoing activity within their overall operations
- Corporate viability assessment will mark the start of serious restructuring efforts toward the corporate sector and will be followed by workout plans or business exchange arrangements as a way to enhance competitiveness and efficiency, which at the end will mark the completion of overall corporate restructuring

2. Results of Corporate Viability Assessment

- The initial assessment results of early June was not deemed satisfactory as it revealed only 14 corporates as being subject to exit, while the assessment of 7

corporates were put-off and none of the affiliates to the top 5 business groups were included

- Confronting unsatisfactory results and with concerns that by accepting such results problems in financial institutions would continue to present serious impediments to the financial system, the FSC required the reassessment of corporates to be completed by respective banks until June 20
- In comparison to previous assessment results, the number of corporates that will be subject to exit rose to 55 corporates an increase of 34 corporates from the previous 21. Among the 34, 20 of them belong to the top 5 business groups representing 59% of the increase seen between the two results
- Initially, financial institutions excluded corporates belonging to the top 5 business groups from viability assessment, as they were deemed to possess the capacity to make repayments on their loans through means like mutual guarantees within a given group
 - However, as the leading role by the top 5 business groups within the overall corporate restructuring scheme is regarded to be of significant importance, the FSC directed financial institutions to assess the viability of each affiliated company of the top 5 business groups in accordance to the soundness of the individual corporate and the capacity of loan repayments etc, the same way in which other ranking business groups were evaluated
- Although results of corporate viability assessment of the top 5 business groups reflect an aggressive and forward-looking approach pursued on the part of financial institutions, there is also concern for some weaknesses in the procedure
- As only accounting reports that were readily available were utilized for the recent assessment, there were unavoidable limitations in identifying funding flows between affiliated companies within a business group and in turn the viability of a given affiliate within a group

3 Future Direction for Corporate Restructuring

- In accordance to results from the first round of corporate viability assessment a workout plan for those corporates that were identified as viable will be pursued, based on negotiations between financial institutions and corporates

<Top 5 business groups>

- The possibility of pursuing mutual funding arrangements among affiliated companies through insider trading deals will be eliminated and more importantly the practice of disproportionate lending toward the top 5 business groups will be overhauled
 - In the event problems in the repayment of principal on lending to a particular corporate is revealed, banks will reassess the viability of the given corporate on a voluntary basis
- Assertive judgements on the part of financial institutions will be required for corporates who in spite of lack of competitiveness of international standards, fail to pursue a more aggressive approach in its restructuring efforts through business exchange etc (eg, motor vehicle industry)
- With input from outside experts, creditor banks of the top 5 business groups will make adjustments to the financial structure improvement agreement in order to provide a more detailed and feasible approach to restructuring and based on such agreement workouts will be pursued

<Other large business groups>

- As for corporates belonging to other large business groups, workout teams of banks will be dispatched to corporates that were identified as being viable to support efforts toward enhancement of corporate value
 - As for the 64 business groups 8 large commercial banks will each identify by July 15, 2 business groups that will be subject to workout
 - As for other large corporates as well as relatively large sized corporates, 8 large commercial banks will each identify 10 corporates or accept applications from corporates

<Small-to-medium sized corporates>

- As for small-to-medium sized corporates, each bank will identify sound and promising corporates and through the special task force on small-to-medium sized corporates financial supervisory authorities will encourage banks to provide

full support to such corporates

- ⇒ **The first round of corporate restructuring efforts will be completed by the end of September and possible problems that may arise throughout the overall corporate restructuring efforts will be deliberated at the Economic Policy Coordination Meeting**
- **Restructuring efforts based on negotiations between creditor banks and corporates are practices used at advanced nations (eg, London approach) and we fully consider their experiences**

HN

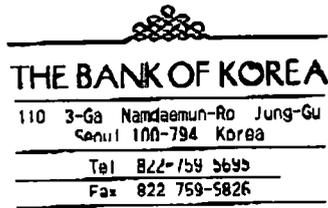
cc. FOSS
JIS
Kwim
SC

98 JUN 18 11 05 AM '98
THE BANK OF KOREA
110 3 Ga Namdangmun Ro Jung Gu Seoul 100 794, Korea
(Telephone 82 2 759 5826)

Facsimile Transmittal Form

DATE	June 18, 1998	(Total Pages 2)
TO	Mr Hyan B Aghevli Acting Director Asia and Pacific Department International Monetary Fund Washington, DC USA (ROOM NUMBER 4-320)	(Fax No 1-202-623 4795)
From	Joong-In Ha Head International Relations Office	(Fax No 82 2 759-5826)
Subject	Letter	

Please see the attached letter



HLAD
INTERNATIONAL RELATIONS OFFICE

June 18 1998

Mr Bijan B Aghevi
Acting Director
Asia and Pacific Department
International Monetary Fund
Washington DC USA

Dear Mr Aghevi

In response to your letter dated June 17, 1998 I am writing to inform you of a change regarding the host to your scheduled trip in July Dr Hyunchul Shin has been transferred to another position, Director of International Department I have succeeded his office since May 14, 1998 On this account I will be responsible for working with your mission to Korea I look forward to meeting you for the first time and cooperating closely with your mission for a successful completion of the third quarterly review

Should you have any questions, of course please do not hesitate to contact me via telephone at 822-759-5695 or via fax at 822-759-5826

Thanking you in advance for your cooperation in this regard, I send my warmest regards

Sincerely yours


John In Ha



98 JUN 18 AM 8 05

Office Memorandum

HAN CC FOSSE
DJS
KMM
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To Ms Tseng

June 18, 1998

From J R Dodsworth

Subject **Korea List of Nonviable firms**

A preliminary translation of the list of nonviable firms announced earlier today is attached. There is little information available as of now but it appears that most of the firms, aside from Haeil Group, Hyundai Livart, and Hanil Synthetic are quite small. Of the 55 firms identified only 10 are listed companies and most of these had already been identified as defunct. There was therefore little direct impact on the stock market. It is estimated that, in total, the 55 firms employ about 20,000 workers.

It is reported that the maximum potential addition to nonperforming loans in the banking system from the 55 firms will be \$17 trillion. However, a good part of this may be recouped through asset sales and guarantees. The indebtedness appears to be well spread among the banks, though I have not been able to obtain data on this so far.

Non Viable Companies

Top 5 Group

Hyundai	
Hyundai Livart	1
Hyundai Heavy Machinery	2
Sunil Merchant Marine	3
Hyundai Aluminum	4
Samsung	
Samsung Watch	5
Icheon Electric	6
Dædu Pharmaceutical	7
Hanil Wire	8
Daewoo	
Hankuk Industrial Elect	9
Hankuk Auto Systems	10
Orion Electric Parts	11
Dongwoo Construction	12
Daechang Industries	13
LG	
LG Elect Parts	14
Wonjeon Energy	15
LG Owenscorning	16
LG E&C	17
SK	
My TV	18
SK Storage	19
Kyungjin Shipping	20

Top 6 to 64 Group

Ssangyong	
Bum A Petroleum	21
* Hanwha	
Otron	22
Hanwha Travel	23
* Dong Ah	
Dong Ah Engineering	24
Hyosung	
Hyosung Media	25
Hyosung Number One	26
Dong Kwang Chemical	27
* Kohap	
Kohap I T	28
Kohap Fine Chemical	29
Kohap Textile	30
F C N	31
* Haitai	
Haitai Distribution	32
Haitai Electronics	33
Haitai Confectionery	34
* Shinho	
Shinho Trading Corp	35
Shinho Telecom	36
Youngjin Tech	37
* New Core	
New Town	38
Shi Dae Livestock	39
Shi Dae Distribution	40
Keopyong	
Dae Han Tungsten	41
Keopyong Ind Development	42
Keopyong Construction	43
* Hanil	
Hanil Synthetic	44
Jinhae Chemical	45
Namju Development	46
Shinnam Development	47
Kabool	
Shinhan Fabric	48
Dongguk	
Dongguk Elect	49
Tongil	
Ilwha	50
* Woo Bang	
Tae Sung Housing	51
Han Kuk Synthetic	
Ewha Distribution	52
Others	
Dae Han Wool	53
Yang Young Paper	54
Woo Jung Hospital	55

recipient of cooperative loans

INTERNATIONAL MONETARY FUND

June 18, 1998

To Ms Siegel

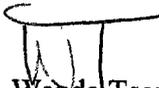
Subject **Korea--Foreign Exchange Mangement Law**

I would appreciate if you could respond to point 3 of Mr Dodsworth's memorandum (attached) regarding the correspondence with the Korean authorities at the time of Korea's acceptance of Article VIII status as soon as possible

Thank you

Attachment

cc Ms Coorey (without attachment)
Mr Gordon (without attachment)


Wanda Tseng
(4-320, ext 37182)



Office Memorandum

Mr Balino

P 7 - illegible new P 7
being requested

To Ms Tseng
From J R Dodsworth ~~JD~~
Subject Korea Various Topics

BBA

HW June 17 1998

cc Kmm,
SC
DU 5

- 1 **Financial Sector Restructuring** I am attaching an updated English translation of the FSC document on "Financial Sector Restructuring," an earlier version of which was given to World Bank staff. I have informed the FSC that our comments would be coordinated with those of the World Bank.

In the meeting with FSC Chairman yesterday, I made the points on capital adequacy ratios communicated by Mr Hayward in his E-mail. The Chairman wished to mainly discuss corporate restructuring (see below), but on the financial side he indicated that the audit of the 12 undercapitalized banks had, on a preliminary basis, increased the estimate of troubled loans in the 12 banks by over 25 percent -- (tentatively from about W46 trillion to W61 trillion as at end - March). As expected most of the banks have negative net worth, particularly the regional banks. The work of one firm (Coopers and Lybrand) had not been completed, but the Appraisal Committee will go ahead from Thursday/ Friday this week. The Committee will not include any members of FSC staff. The Chairman expressed regret that neither the Fund nor the Bank could suggest a participant for the committee.

- 2 **Corporate Restructuring** The report, on corporate restructuring made to the Cabinet earlier in the day by the FSC Chairman and the Finance Minister had apparently not found favor with the President (i) because there was little progress on the "big deals," and (ii) because the nonviable company list (to be issued tomorrow) still had insufficient representation from big-5 affiliates. It appears that following the cabinet meeting, the corporate 'death list' (as it is known within FSC) was expanded and resubmitted for Presidential approval. I reiterated the position that corporate restructuring could not be achieved in a short time period that it needed to be market driven and led by creditors, and that any 'big deal' needed to be commercially advantageous to all the different parties. I also emphasized that government intervention and politicization of corporate restructuring was likely to undermine credibility of the whole process and divert attention from the real issue of how debt workouts could best be achieved.

98 JUN 17 AM 7 57

On this latter point, the Chairman said that Mr Smith's report and recommendations accorded well with the views of FSC staff, particularly on the question of the extent of powers of the Central Arbitration Committee. He said that Bank staff particularly Mr Berggren were pushing very hard for a more centralized and government-influenced process in which there was a less clear dividing line between bank restructuring and corporate restructuring. Chairman Lee believes it is very important to avoid any implication that public money utilized for purchase of bad banking sector assets is effectively being used to help corporate restructuring. He asked that the Fund help to moderate the views of the Bank on this subject and, to this end, I will be meeting with Messrs Libermann and Berggren later this evening.

- 3 **Foreign Exchange law** MOFE staff indicate that they will be prepared to discuss the technical questions raised and the possibility of a LEG visit tomorrow (Thursday) afternoon. As of now, they are reluctant to give me a full draft of the new Law (it is only available in Korean). I have asked that they check with their superiors. I will push further tomorrow if necessary, but the draft will be in Korean. The MOFE staff are requesting copies of earlier correspondence on exchange restrictions at the time of the acceptance of Article VIII status. They believe that in that discussion, many of the same topics had been raised and resolved. I wonder if LEG could provide the relevant correspondence from that time?
- 4 **Position in National Assembly** The resumption of National Assembly is waiting for the "political party restructuring" to be completed. One member crossed party lines this morning and another four or five are expected to do so during the next three - four weeks. This will, I am told, give an effective majority to the President's coalition. A special session of the National Assembly can thus be expected in late - July. However, there are many bills awaiting passage and most of these will not be dealt with until September.

Attachment

cc (Please copy to MAE)



Office Memorandum

To Mr Anjaria

June 18, 1998

From Sharmini Coorey 

Subject **Letter from Treasury Secretary Rubin**

You requested our assistance in drafting a reply to Treasury Secretary Rubin's letter to the Managing Director regarding the need to limit the use of government-subsidized and government-directed lending policies in Fund-supported programs in Asia

As noted in the letter, there are commitments to end trade-related government subsidies and directed lending in the IMF-supported programs with Korea and Indonesia At the same time, it should be recognized that in most countries, both inside and outside Asia, public funds are used to further specific public policy objectives, for instance, the support of small and medium-sized enterprises (SMEs) or specific sectors, such as agriculture Even in the United States, subsidized credit schemes for agriculture, the Small Business Administration and the Export-Import Bank support specific policy objectives

In the programs in Asia, policy lending is already guided by the principles mentioned in the letter new credit schemes benefiting private producers are intended to be well-targeted, temporary, on a commercial basis (i.e., without subsidies), appropriately conditional, and as nondistortionary as possible They are necessary to ameliorate the credit crunch and its impact on economic activity, particularly in view of the severe recession these countries are facing as a result of the crisis Some countries (Korea, Indonesia) have existing credit schemes to support certain sectors (mainly SMEs and agriculture), but these are relatively small (less than 2 percent of GDP) We have no evidence to suggest that government financial resources are being directed to provide unfair trade-related subsidies or to attempt to evade market forces

On the suggestions in the attachment

- While we can agree with the principle that firms having access to credit from market sources or that are not viable should not have access to government credit, operationally it is impossible to ascertain whether this is indeed true in every case The credit schemes in these countries are not directed at specific industries or firms For instance, in Korea, the decision on which SMEs gain access to credit under the US\$3.3 billion in trade financing schemes is left to individual commercial banks
- The credit and credit-guarantee schemes are largely focused on SMEs rather than on larger corporations and do not involve explicit interest subsidies (i.e., the charges are usually some markup over the cost of funds or are at market rates) It makes

little sense to condition the use of these resources on changes in corporate structure, management etc , since most of these loans are targeted at SMEs and are considered normal business loans

- Under current Fund-supported programs in Asia, policy-based lending is carried out through official institutions, typically government-owned development banks, export-import banks, or credit-guarantee funds
- With the exception of the program with Indonesia, official reserves are not being used to provide guarantees for trade finance or any other such purpose. Since reserves in these cases are liquid and unencumbered, there is no need for adjusters for this purpose. In Korea, the US\$3.3 billion in trade credit schemes is to be financed by reserves in excess of program targets, when funds are allocated to these schemes, reserves would register a decline. In the case of Indonesia, adjusters apply to the bulk of the reserves that are not highly liquid.
- Some judgement is needed on including the lending operations on government financial institutions in the fiscal accounts. In Indonesia, interest subsidies are included in the budget. In Thailand, a part of the interest cost of financial sector restructuring will be incorporated into the 1998/99 budget, with full fiscalization of such costs envisaged in the following year. In Korea, policy lending has been largely discontinued and is limited to a few, small credit facilities at the Bank of Korea, subsidized credit schemes have also been reduced significantly since the early 1990s. Many government financial institutions (e.g., KDB, KEXIM, Industrial Bank of Korea) finance lending through borrowing on domestic and international markets and their operations do not involve a subsidy.
- In Korea and Indonesia, public funds will be used to help with bank recapitalization, in the context of the ongoing financial sector restructuring. The recapitalization will involve asset purchases and direct subscriptions to capital in the form of equity or convertible bonds. In Korea, the program attaches conditions to ensure that the use of public funds would be accompanied by adequate contributions of capital by new or existing shareholders. In Thailand and Korea, the government recapitalized and took over troubled commercial banks which were of systemic importance following a complete (in the case of Thailand) or almost complete write-down of the capital of existing shareholders and the removal of managers responsible.



INTERNATIONAL MONETARY FUND

WASHINGTON, D C 20431

ASIA AND PACIFIC DEPARTMENT

Fax # (202) 623-4432

Tel # (202) 623-7602

MSG NO	DATE June 18, 1998	PAGE 1 OF 1
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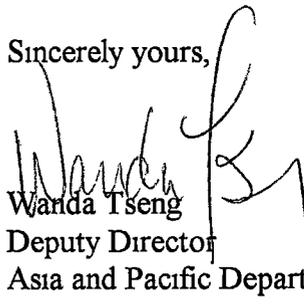
TO

Mr Nakki Baek
 Research Fellow/Director
 Korea Institute for Industrial Economics and Trade
 (KIET)
 Washington, D C

(703) 383-9647

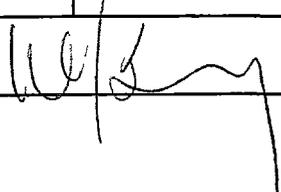
In our meeting several weeks ago, you had mentioned that the KIET has some views concerning the McKinsey report I would appreciate it if you can send me any studies that KIET has done in connection with the McKinsey report and/or on firm level productivity in Korea Many thanks

Sincerely yours,



Wanda Tseng
 Deputy Director
 Asia and Pacific Department

FROM Wanda Tseng
 APD/AI

ROOM NO 4-302	EXTENSION (202) 623-7182	ACCOUNT CODE
AUTHORIZED BY Wanda Tseng	SIGNATURE 	



Office Memorandum

WT
CC
KHN
SC
005
TO MANOLE

To Wanda Tseng

June 18, 1998

From Kai Aaen Hansen *KAH*

Subject **Korea - Shipbuilding Industry**

The Danish shipping company Maersk line - one of the world's largest - asserts in a memo to the Danish Shipowners' Association that the IMF has "suggested that Korean companies reduce their debt-equity ratio to 200 percent" but "that for many companies the present ratio was closer to 2000 percent" Moreover, the memo claims that "Korean Shipowners' Association was putting heavy pressure on the government to insist on IMF acceptance of a debt-equity ratio of up to 400 percent"

The memo has been forwarded to me by the Danish Ministry of Economic Affairs I enclose an unofficial translation of the memo as well as the Danish version

I would very much appreciate your comment at your earliest convenience

Attachment

98 JUN 18 PM 2 28

TRANSLATION

MEMO

To Knud Pontoppidan
From Flemming R. Jacobs
Date June 5, 1998
Re Korea

During a meeting with Mr. K. H. Lee, President Keo Yang (Cape-size Bulk) and Vice President Hanjin Shipping (Container, Tank, LNG) Mr. K. H. Lee mentioned that the IMF had suggested that Korean companies reduce their debt-equity ratio to 200 percent (it was mentioned that for many companies the present ratio was closer to 2000 percent). However, Korean shipowners' association was putting heavy pressure on the government to insist on IMF acceptance of a debt-equity ratio of up to 400 percent.

It does not seem fair that Korean shipowners could continue to compete supported by IMF money and thus underbid non-Korean shipowners internationally. They have done that long enough and now those who cannot manage should not be given further assistance.

9406101400

**M E M O**

Til . Knud Pontoppidan
Fra Flemming R. Jacobs
Dato 5 juni 1998
Ang : Korea

Under samtale med Mr K.H Lee, President Keo Yang (Cape-size Bulk) og Vice President Hanjin Shipping (Containere, Tank, LNG) nævnte denne, at IMF foreskrev koreanske virksomheder at reducere deres equity ratio til 200% (det blev nævnt, at for mange virksomheder var det nuværende talt snarere 2000%) Imidlertid pressede Korean Shipowners Association kraftigt på regeringen for at denne overfor IMF skulle insistere på, at denne equity ratio kunne blive op til 400%

Det synes bestemt ikke fair, at koreansk skibsfart derved fortsat kan konkurrere støttet af IMF penge og derved underbyde ikke-koreanske redere internationalt Det har de gjort længe nok, og nu bør de, der reelt ikke kan klare sig, ikke gives yderligere hjælp.

Flemming R. Jacobs

P 7 - illegible new P 7
being requested



Office Memorandum

BBA

HW June 17 1998

To Ms Tseng

From J R Dodsworth ~~769~~

cc kmh,
SC
DUS

Subject Korea Various Topics

1 **Financial Sector Restructuring** I am attaching an updated English translation of the FSC document on "Financial Sector Restructuring," an earlier version of which was given to World Bank staff I have informed the FSC that our comments would be coordinated with those of the World Bank

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98 JUN 17 AM 7 57

- 2 -

On this latter point, the Chairman said that Mr Smith's report and recommendations accorded well with the views of FSC staff, particularly on the question of the extent of powers of the Central Arbitration Committee. He said that Bank staff particularly Mr Berggren were pushing very hard for a more centralized and government-influenced process in which there was a less clear dividing line between bank restructuring and corporate restructuring. Chairman Lee believes it is very important to avoid any implication that public money utilized for purchase of bad banking sector assets is effectively being used to help corporate restructuring. He asked that the Fund help to moderate the views of the Bank on this subject and, to this end, I will be meeting with Messrs Libermann and Berggren later this evening.

- 3 **Foreign Exchange law** MOFE staff indicate that they will be prepared to discuss the technical questions raised and the possibility of a LEG visit tomorrow (Thursday) afternoon. As of now, they are reluctant to give me a full draft of the new Law (it is only available in Korean). I have asked that they check with their superiors. I will push further tomorrow if necessary, but the draft will be in Korean. The MOFE staff are requesting copies of earlier correspondence on exchange restrictions at the time of the acceptance of Article VIII status. They believe that in that discussion, many of the same topics had been raised and resolved. I wonder if LEG could provide the relevant correspondence from that time?
- 4 **Position in National Assembly** The resumption of National Assembly is waiting for the political party restructuring to be completed. One member crossed party lines this morning and another four or five are expected to do so during the next three - four weeks. This will, I am told, give an effective majority to the President's coalition. A special session of the National Assembly can thus be expected in late July. However, there are many bills awaiting passage and most of these will not be dealt with until September.

Attachment

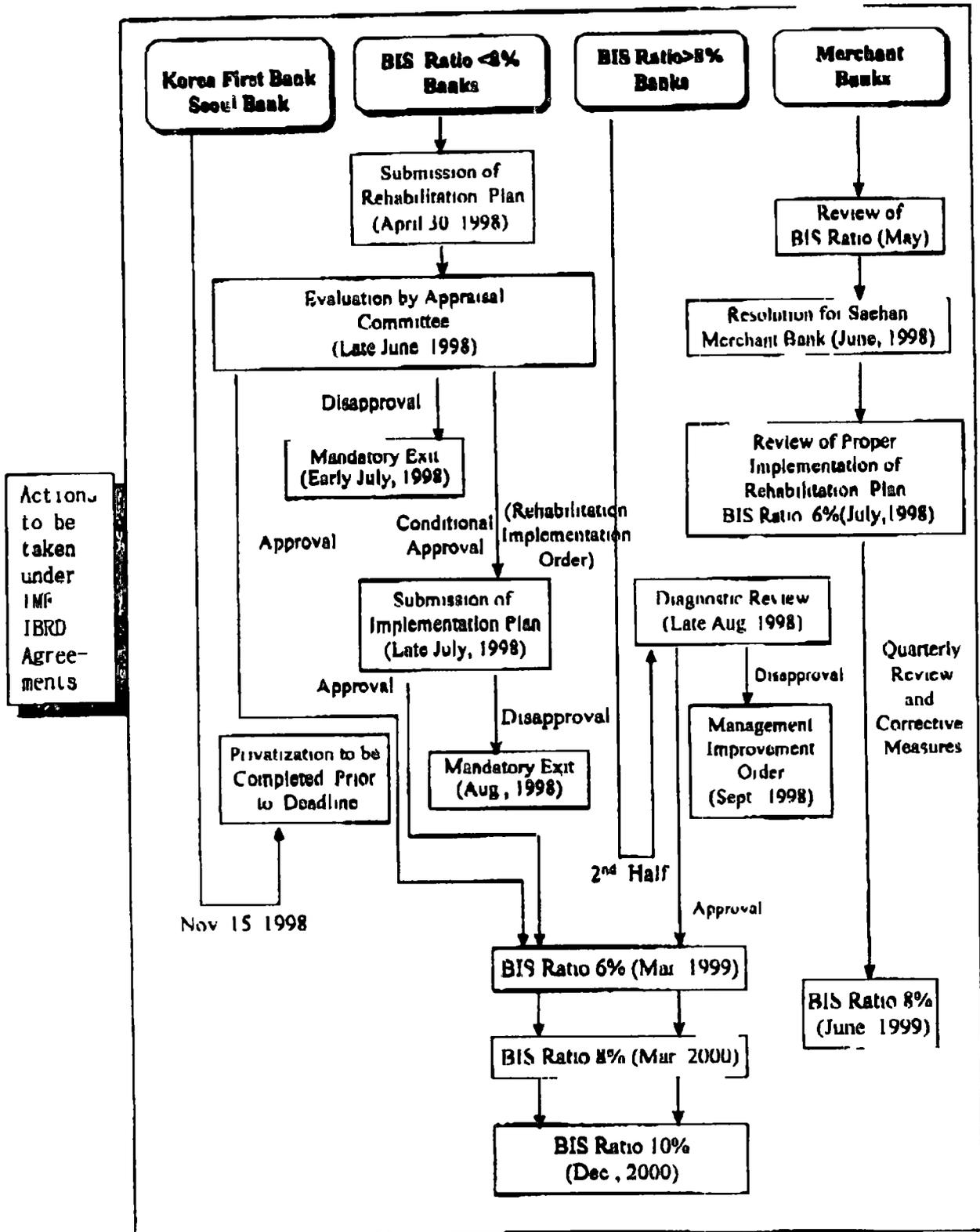
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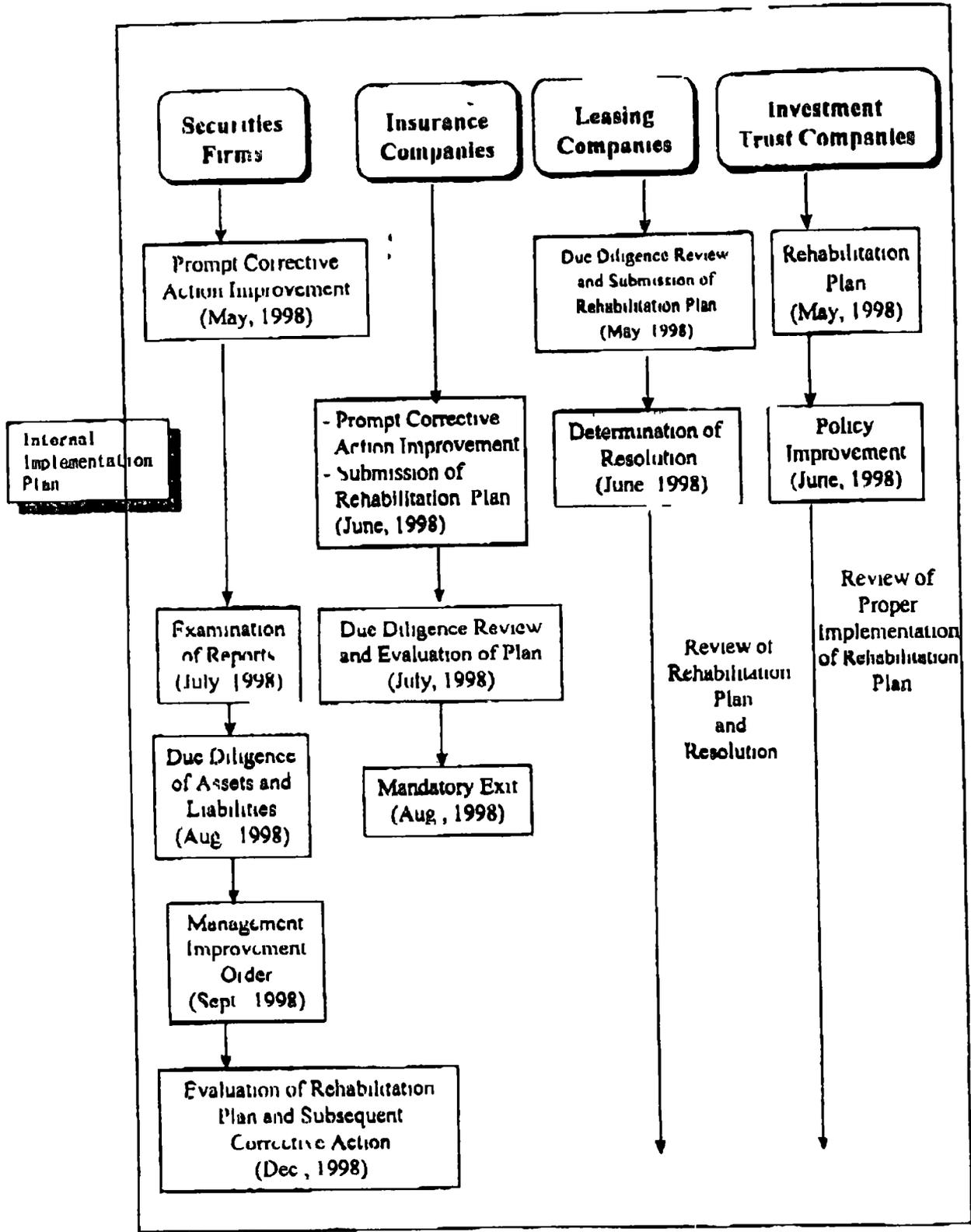
FINANCIAL SECTOR RESTRUCTURING

June 17th, 1998

Structural Reform Planning Unit

Financial Restructuring Plan





I Bank Restructuring Plan

- Financial restructuring is being carried out in accordance to the MOUs with IMF and IBRD as well as other previously announced plans

▶ Seoul Bank and Korea First Bank

- Privatization will be pursued in close cooperation with an internationally well-known lead manager, Morgan Stanley
- If the sell-off to foreign financial institutions is not successful an alternative plan will be put into place

▶ 12 banks that fall short of BIS capital adequacy ratio of 8%

- Upon completion of asset appraisal reviews by respective accounting firms the Bank Appraisal Committee (consisting of 10 outside experts including academics accountants lawyers etc) will be formed (June 18 1998)
- Rehabilitation plans submitted by each bank will be evaluated and the results of the evaluation will be reported to the Financial Supervisory Commission (June 25, 1998)
- Taking into account the recommendations by the Bank Appraisal Committee the Financial Supervisory Commission will prepare a corrective scheme for troubled banks (June 30 1998)

▶ 12 banks that satisfy the BIS capital adequacy ratio of 8%

- Upon completion of due diligence reviews by the end of August, troubled banks will be subject to forceful management improvement orders, such as the change in management or merger with another bank

II Leasing Company Resolutions

An Overview of Leasing Business

- o Currently 25 leasing companies are in operation (total assets of 38.8 trillion won)

24 are subsidiaries of banks and the remaining one is a subsidiary of the Credit Guarantee Fund

- o According to the regulatory authority's asset appraisal reviews as of May 1998, 21 companies have an eroded capital base (Δ 2.1 trillion won)

* not included in the 21 companies are Shinhan Korea Exchange Korea First and Chuneun Leasing Co

Resolution Scheme

- o Leasing companies whose total liabilities exceed total assets will be subject to resolution as a general rule,

- o However, if the majority shareholders (parent bank community enterprises etc) possess a clear commitment and have the capacity to recapitalize the leasing company will continue to operate upon the agreement of the creditor financial institutions

→ A total of 9 leasing companies (total borrowings of 7.6 trillion won) will be subject to resolution

Timeframe for Resolution

- o Preparation of a scheme with close consultation with parent bank (June 15, 1998 - June 20 1998)

- o Resolution of troubled leasing companies (end of June, 1998)

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III. Bank Resolutions

□ Bank Principles

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- o Allow for a stage-by-stage approach in achieving BIS ratio over a 2 year period

Set the minimum intermediate target for March 1999 at BIS ratio 6% and review the progress of implementation on a quarterly basis in order to encourage an early achievement of such targets

Apply a more lenient set of BIS ratios for regional banks and commercial banks that do not lend in amounts above a set amount (eg , 5 billion won) to an individual corporate and that do not engage in international business

	<u>Mar 31 1999</u>	<u>Mar 31, 2000</u>	<u>Dec 31, 2000</u>
- banks that engage in international business	6%	8%	10%
- banks that do not engage in international business	4%	6%	8%

iii) Submission of recapitalization plan for capital deficiency

- o Capital increase or joint venture with a foreign institution
- o Enhancement in profitability through self-rescue efforts

iv) Bank Appraisal Committee evaluates recapitalization plan

<Evaluation Standard>

Adequacy in capitalization, asset soundness, profitability, liquidity and management expertise will be ranked either as suitable conditionally suitable, unsuitable

Assessment of the normalization of bank management based on BIS ratios as well as other standards

Recommendation on the feasibility of rehabilitation of banks will be submitted to the FSC (banks will fall under one of three categories , approval conditional approval and disapproval)

o Approval

o Conditional Approval → Submission of implementation plan within one month of bank normalization order

o Disapproval → Resolution through mandatory merger order or transfer of business

v) Fiscal support toward deterioration of BIS ratio upon acquiring troubled bank

o Capital increase etc

Fiscal support toward the acquiring bank to cover the deterioration of BIS ratio will be provided

o if the BIS ratio of the acquiring bank exceeds BIS ratio targets fiscal support will not be provided

Actions to be taken subsequent to bank appraisal reviews

◇ Taking into account the evaluation report of the Bank Appraisal Committee banks will be placed into one of three categories (approval, conditional approval disapproval) upon evaluation of whether or not each bank has achieved respective BIS ratio targets

o Approval

Mandated to prepare and submit a MOU containing detailed quarterly implementation plans

Implementation of rehabilitation plans will be monitored on a continuous

basis and in the event the plan is not being implemented accordingly management improvement measures such as capital reduction, change in management or merger will be imposed

0 Conditional approval

Submission of implementation plans within one month since the date conditional approval was obtained This plan should contain contents summarized below

In the event of disapproval of an implementation plan a mandatory merger order or transfer of business order will be imposed

<Content of Implementation Plans>

Change in management

Capital reduction

Expense reduction through adjustments in organization personnel and compensation schemes as well as improvement in profitability

Maintenance of sufficient liquidity

Plans of recapitalization such as merger, joint venture or rights issue

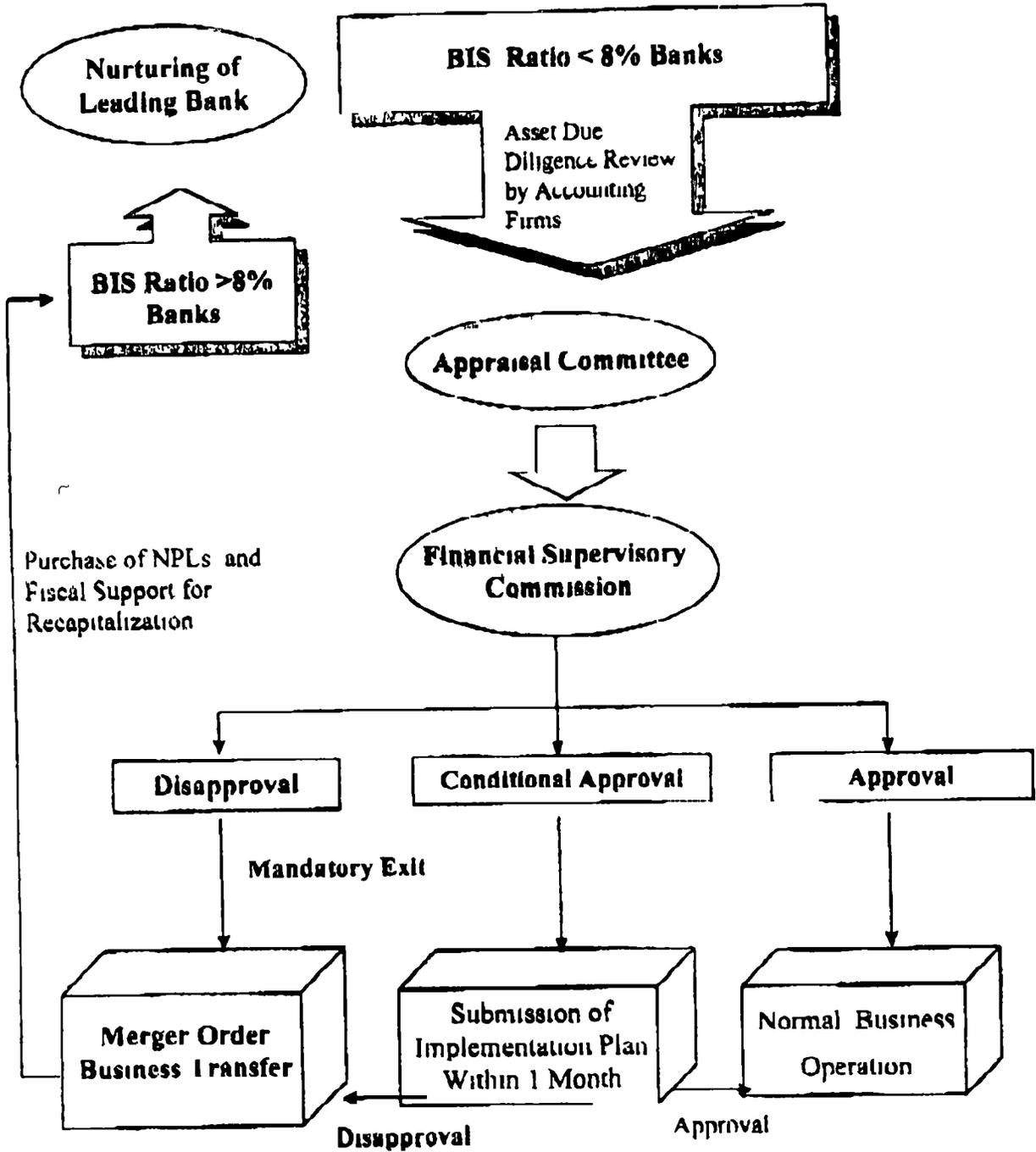
0 Disapproval

A mandatory merger or transfer of business will be ordered

Resolution Scheme for Troubled Banks

- 0 In the event either a bank subject to conditional approval or disapproval pursues a merger with a sound bank on a voluntary basis it will be exempted from mandatory exit**

Resolution for Non-Viable Banks



- o Disapproved troubled banks will be subject to mandatory merger with a sound bank or transfer of business under a purchase & assumption arrangement

※ Purchase and Assumption Arrangements

- Troubled bank will transfer its good assets and debt to a sound bank

If the failing bank's total liabilities exceed total performing assets the Korea Deposit Insurance Corporation (KDIC) will cover the discrepancy by injecting capital and etc

IV Fiscal Support for Bank Restructuring

Size of Fiscal Support

- o Fiscal support for financial restructuring was set at 50 trillion won at the National Economic Council Meeting on May 20
- o This can be broken down as follows , purchase of non-performing assets 25 trillion won, recapitalization of bank 16 trillion won deposit payment 9 trillion won

Underlying Principles

- o To minimize taxpayers burden
- o To be pursued in tandem with self-rehabilitation efforts
- o To establish a responsible management system

burden-sharing with existing shareholders and change in management etc

Criteria for extension of fiscal support

- o Purchasing criteria for non-performing assets

KAMC will buy non-performing assets from the sound banks or the banks whose rehabilitation plans are approved

KAMC will purchase NPLs from banks at a firm offer to reduce uncertainties in banks financial status by eliminating contingent liabilities

Acquired troubled banks non-performing assets will be purchased

KAMC's losses resulting from the sell-off of non-performing loans will be borne by fiscal budget

Capital injection etc

Payoff of net debt when transferring assets and liabilities to acquiring bank

Deterioration of BIS adequacy ratio resulting from a merger with a troubled bank will be covered by the government

Estimated size of fiscal support

- Total cost for bank restructuring is estimated to be 23 trillion won at the most
- Among this amount 18 trillion won is to be allocated to purchasing of non-performing assets, recapitalization and payoff of net debt
- 5 trillion won is to be allocated to purchasing of non-performing assets and recapitalization toward merging banks and others

V Supplementary Measures

Amendment of related statutes to facilitate bank resolutions

- [Act Concerning the Structural Improvement of the Financial Industry]

needs amendment to include regulation concerning 3rd party claims that may arise during the process of transferring assets and liabilities

- Taxation Law should be amended to reduce tax burden in the process of transferring assets and liabilities
- Prepare contingency programs to minimize adverse side effects such as disruptions to the financial market as a result of bank restructuring (in consultation with Ministry of Finance and Economy and the Bank of Korea)
 - Liquidity support from the Bank of Korea will be provided for through RPs and repurchase of monetary stabilization bonds in the event a bank subject to resolution encounters liquidity shortage
 - Difficulties in financing faced by corporates linked to bank resolutions will be resolved through uninterrupted credit extension, strengthening of credit guarantee support and enlargement of trade financing
 - Contingency plans to prevent a crisis situation such as massive withdrawal from non-bank financial institutions or liquidity shortage stemming from bank restructuring
- Bank support schemes will be determined according to proportion of loans to small-to-medium enterprises by bank (as of June, 1998)
 - All banks are categorized into one of three categories (A, B, C), where banks categorized as A and B banks will be provided with subordinated loans or capital injection amounting to 1 trillion won on a 2:1 basis
 - In addition, subordinated loans or capital injection worth 1-2 trillion won will be provided to the banks who provided loans actively to small-to-medium sized enterprises, based on an evaluation of their performance every 3 or 6 months
- Enhancement of sound management through amendment of related

regulations

Sound Management of Financial Institutions

- Improve disclosure regulations concerning NPLs and financial soundness to the extent that it matches international standards
- Adopt mark-to-market accounting principles
- Strengthen internal control standards, conduct more detailed review of external audits

Strengthening of Prudential Regulations

- Mandatory loss provisioning for principal-guaranteed bank trust accounts
- Cutback of amounts in excess of large exposure limits and further reduction of those limits
- Adoption of loan classification standards based on loan payoff capacity

Acceleration of corporate restructuring

- Additional credit to business groups is not feasible due to financial restructuring and an adjustment to lower exposure limits for a single borrower group is needed → increase in corporate bankruptcies
- Accelerate corporate restructuring to reduce corporate debt ratios

Measures to eliminate excessive dependency on short-term debt (eg; CPs etc.)

- Moral hazards connected with financial institutions' purchases of CPs issued by troubled corporates such as Kia and Ginro through merchant banks continue to exist

0 As a result there is constant concern for the occurrence of financial debacles of massive size and the reoccurrence of a serious financial crisis

→ Provisions to prevent excessive issuance of CPs are needed

Make adjustments to the size of discounting and purchase of CPs by financial institutions to ensure CP issuance is within operating fund ceilings

VI Non-bank Restructuring Plan

Underlying Principles

- ◇ Insolvent non-banking financial institutions that emerge as a result of bank restructuring will be resolved
- ◇ Self-rehabilitation through recapitalization will be encouraged under the responsibility of major shareholders. However if a recovery is deemed unrealistic those institutions will be exited without hesitation

Merchant Banks

- 0 Determination of resolution scheme for Saehan Merchant Bank (June, 1998)
- 0 Review of proper implementation of rehabilitation plans. In the event dissatisfactory implementation is revealed additional mandatory exits will be pursued (July, 1998)

Insurance companies

- 0 Submission of rehabilitation plan (June 1998)
- 0 Asset due diligence reviews, formation of appraisal committee, evaluation of rehabilitation plan (July 1998)

o Resolution for troubled insurance companies (August 1998)

Securities Firms

o Submission of operational net capital ratio asset liability ratio reports (July, 1998)

o Prompt corrective actions are to be imposed upon completion of asset due diligence reviews (September, 1998)

o Evaluation of management improvement plans and subsequent appropriate actions (December, 1998)

Investment Trust Companies

o Submission of rehabilitation plans (May 1998)

o Adoption of mark-to-marketing of bonds, amendment to withdrawal policies etc (June 1998)

o Review of proper implementation of rehabilitation plan and subsequent management improvement measures (September, 1998)

HN



INTERNATIONAL MONETARY FUND

WASHINGTON, D C 20431

MESSAGE CENTER

Fax # (202)623-4795

Tel # (202) 623-7177

MSG NO	DATE June 17, 1998	PAGE 1 OF 2
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TO

Mr Hyunchul Shin,
Director
International Relations Office, International Dept
Bank of Korea
Seoul Republic of Korea

82 2 759 5826

FROM

Bijan B Aghevli
APD

ROOM NO 4-320	EXTENSION 3-7177	ACCOUNT CODE
AUTHORIZED BY	SIGNATURE	



INTERNATIONAL MONETARY FUND
WASHINGTON D C 20431

CABLE ADDRESS
INTERFUND

June 17, 1998

Mr Hyunchul Shin
Director
International Relations Office
International Department
Bank of Korea
Seoul, Korea

Dear Mr Shin

I would like to inform you that the IMF will be visiting Seoul during July 8-22 for the third quarterly review under the stand-by arrangement. Also, we have had a reshuffle of responsibilities of the senior staff in the Asia and Pacific department, and I am pleased to be leading the July mission to Korea, as Ms Tseng will be leading the work on China. It has been a few years since I visited Korea, but I have been closely involved in formulation of the Korea program at headquarters.

I am looking forward to working with you closely with a view to completing the review as expeditiously as possible.

Sincerely yours,

A handwritten signature in black ink, appearing to read "Bijan B. Aghevli".

Bijan B Aghevli
Acting Director
Asia and Pacific Department



HN

INTERNATIONAL MONETARY FUND
WASHINGTON, D C 20431
MESSAGE CENTER

Fax # (202) 623-4795

Tel # (202) 623-7177

MSG NO	DATE June 17, 1998	PAGE 1 OF 2
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TO Mr Chol-Hwan Chon
Governor
Bank of Korea
Seoul
Republic of Korea

82 2 759-4037

Please see attached

FROM Bijan B Aghevli
APD

ROOM NO 4-320	EXTENSION 3-7177	ACCOUNT CODE
AUTHORIZED BY	SIGNATURE	



INTERNATIONAL MONETARY FUND
WASHINGTON D C 20431

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INTERFUND

June 17, 1998

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Bank of Korea
Republic of Korea

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Bijan B Aghevlı
Acting Director
Asia and Pacific Department



INTERNATIONAL MONETARY FUND
WASHINGTON, D C 20431
MESSAGE CENTER

fen

Fax # (202) 623-4795

Tel # (202) 623-7177

MSG NO	DATE June 17, 1998	PAGE 1 OF 2
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TO The Honorable Lee Kyu-Sung
Minister of Finance and Economy
Ministry of Finance and Economy
Seoul
Republic of Korea

82 2 503-9138

Please see attached

FROM Bijan B Aghevli
APD

ROOM NO 4-320	EXTENSION 3-7177	ACCOUNT CODE
AUTHORIZED BY	SIGNATURE	



INTERNATIONAL MONETARY FUND
WASHINGTON D C 20431

CABLE ADDRESS
INTERFUND

June 17, 1998

The Honorable Lee Kyu-Sung
Minister of Finance and Economy
Ministry of Finance and Economy
Republic of Korea

Dear Mr Minister

I would like to confirm that, as agreed between Vice-Minister Chung and Mr Dodsworth, the IMF mission will be visiting Seoul during July 8-22 for the third quarterly review under the stand-by arrangement. Also, we have had a reshuffle of responsibilities of the senior staff in the Asia and Pacific department, and I am pleased to be leading the July mission to Korea, as Ms Tseng will be leading the work on China. It has been a few years since I visited Korea, but I have been closely involved in formulation of the Korea program at headquarters.

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Bijan B Aghevi
Acting Director
Asia and Pacific Department

H-21



INTERNATIONAL MONETARY FUND
WASHINGTON, D C 20431
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Fax # (202) 623-4795

Tel # (202) 623-7177

MSG NO	DATE June 17, 1998	PAGE 1 OF 2
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TO Mr Chung Duck-Koo
Vice-Minister for International Affairs
Ministry of Finance and Economy
Seoul, Republic of Korea

82 2 503-9138

Please see attached

FROM Bijan B Aghevli
APD

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AUTHORIZED BY	SIGNATURE	



INTERNATIONAL MONETARY FUND
WASHINGTON D C 20431

June 17, 1998

CABLE ADDRESS
INTERFUND

Mr Chung Duck-Koo
Vice-Minister for International Affairs
Ministry of Finance and Economy
Republic of Korea

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Bijan B Aghevi
Acting Director
Asia and Pacific Department



INTERNATIONAL MONETARY FUND
WASHINGTON D C 20431

CABLE ADDRESS
INTERFUND

June 17, 1998

The Honorable
Kyu Sung Lee
Minister of Finance and Economy
Ministry of Finance and Economy
Government Building II
Kwacheon
Kyunggi Do, 171-11
Republic of Korea

Dear Minister

I would like to inform you that I will be taking up new responsibilities in the Asia and Pacific Department of the IMF—overseeing the work on China and Hong Kong

It was a great honor and privilege to have worked with you and your staff in helping Korea through this difficult period. On this occasion, I would like to express my sincere appreciation for all the cooperation and support you have extended to me during my tenure. I very much appreciate your leadership and the dedication of the staff at the Ministry of Finance and Economy that has brought about the substantial progress in overcoming Korea's current economic problems. I will continue to follow developments in Korea with keen interest.

Wishing you every success in what will continue to be a challenging period ahead, I look forward to meeting you again in the future.

Please accept my highest personal regards.

Sincerely yours,


Wanda Tseng
Deputy Director
Asia and Pacific Department



INTERNATIONAL MONETARY FUND
WASHINGTON D C 20431

June 17, 1998

CABLE ADDRESS
INTERFUND

The Honorable
Chung Duck-Koo
Vice-Minister for International Affairs
Ministry of Finance and Economy
Government Building II
Kwacheon
Kyunggi Do, 171-11
Republic of Korea

Dear Mr Vice-Minister

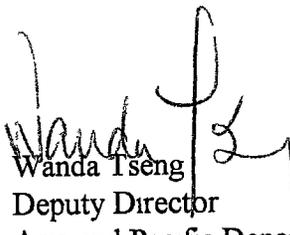
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Wishing you every success in what will continue to be a challenging period ahead, I look forward to meeting you again in the future.

Please accept my highest personal regards.

Sincerely yours,


Wanda Tseng
Deputy Director
Asia and Pacific Department



INTERNATIONAL MONETARY FUND
WASHINGTON D C 20431

CABLE ADDRESS
INTERFUND

June 17, 1998

Mr Woo-Suk Kim
Director-General
International Finance and Securities
Ministry of Finance and Economy
Government Building II
Kwacheon
Kyunggi Do, 171-11
Republic of Korea

Dear Mr Kim

I would like to inform you that I will be taking up new responsibilities in the Asia and Pacific Department of the IMF—overseeing the work on China and Hong Kong

It was a great honor and privilege to have worked with you and your staff in helping Korea through this difficult period. On this occasion, I would like to express my sincere appreciation for all the cooperation and support you have extended to me during my tenure. Thanks to your efforts and that of your dedicated staff at the Ministry, substantial progress has been made in overcoming Korea's current economic problems. I will continue to follow developments in Korea with keen interest.

Wishing you every success in what will continue to be a challenging period ahead, I look forward to meeting you again in the future.

Please accept my highest personal regards.

Sincerely yours,


Wanda Tseng
Deputy Director
Asia and Pacific Department



INTERNATIONAL MONETARY FUND
WASHINGTON D C 20431

CABLE ADDRESS
INTERFUND

June 17, 1998

Mr Tae-Shin Kwon
Deputy Director-General
International Finance Bureau
Ministry of Finance and Economy
Government Building II
Kwacheon
Kyunggi Do, 171-11
Republic of Korea

Dear Mr Kwon

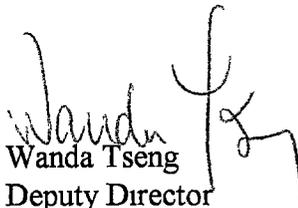
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Please accept my highest personal regards.

Sincerely yours,


Wanda Tseng
Deputy Director
Asia and Pacific Department



INTERNATIONAL MONETARY FUND
WASHINGTON D C 20431

June 17, 1998

CABLE ADDRESS
INTERFUND

Mr Kyung Wook Hur
Director
IMF Task Force
Financial Policy Office
Ministry of Finance and Economy
Government Building II
Kwacheon
Kyunggi Do, 171-11
Republic of Korea

Dear Mr Hur

I would like to inform you that I will be taking up new responsibilities in the Asia and Pacific Department of the IMF—overseeing the work on China and Hong Kong

It has been a great honor and pleasure to have worked with you and your staff. Thank you very much for all your supportive cooperation during my tenure. Your efforts in facilitating the work of the missions have been invaluable. I will continue to follow developments in Korea with keen interest.

Wishing you every success in what will continue to be a challenging period ahead, I look forward to meeting you again in the future.

With warm personal regards

Sincerely yours,


Wanda Tseng
Deputy Director
Asia and Pacific Department



INTERNATIONAL MONETARY FUND
WASHINGTON D C 20431

June 17, 1998

CABLE ADDRESS
INTERFUND

The Honorable
Chol-Hwan Chon
Governor
The Bank of Korea
110, 3-Ga, Namdaemun-Ro
Jung-Gu
Seoul 100-794
Republic of Korea

Dear Mr Governor

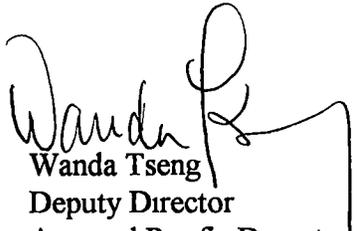
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Sincerely yours,


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Deputy Director
Asia and Pacific Department



INTERNATIONAL MONETARY FUND
WASHINGTON D C 20431

CABLE ADDRESS
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June 18, 1998

Dr Jin Lee
President
Korea Development Institute
P O Box 113, Cheong Nyang
Seoul 130-012
Republic of Korea

Dear Dr Lee

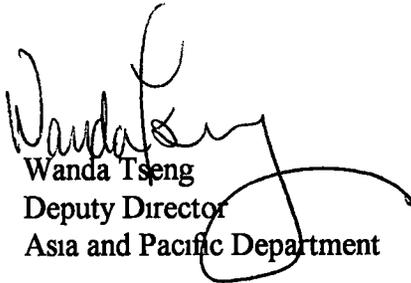
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It was a great honor and privilege to have worked with the staff of the KDI. Our discussions with the KDI have always been a highlight in our mission. On this occasion, I would like to express my sincere appreciation for all the cooperation and support the KDI has extended to me during my tenure. I will continue to follow developments in Korea with keen interest.

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Please accept my highest personal regards.

Sincerely yours,


Wanda Tseng
Deputy Director
Asia and Pacific Department



INTERNATIONAL MONETARY FUND
WASHINGTON D C 20431

CABLE ADDRESS
INTERFUND

June 17, 1998

Mr Hun-Jai Lee
Chairman
Financial Supervisory Commission
Seoul
Republic of Korea

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Sincerely yours,


Wanda Tseng
Deputy Director
Asia and Pacific Department



INTERNATIONAL MONETARY FUND
WASHINGTON D C 20431

CABLE ADDRESS
INTERFUND

June 18, 1998

Dr Bongsung Oum
Vice President
Korea Development Institute
P O Box 113, Cheong Nyang
Seoul 130-012
Republic of Korea

Dear Dr Oum

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Deputy Director
Asia and Pacific Department



INTERNATIONAL MONETARY FUND
WASHINGTON D C 20431

CABLE ADDRESS
INTERFUND

June 17, 1998

The Honorable
Chol-Hwan Chon
Governor
The Bank of Korea
110, 3-Ga, Namdaemun-Ro
Jung-Gu
Seoul 100-794
Republic of Korea

Dear Mr Governor

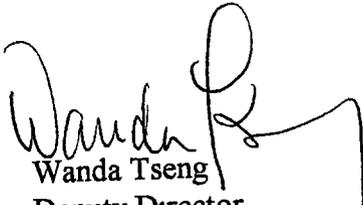
I would like to inform you that I will be taking up new responsibilities in the Asia and Pacific Department of the IMF—overseeing the work on China and Hong Kong

It was a great honor and privilege to have worked with you and your staff in helping Korea through this difficult period. On this occasion, I would like to express my sincere appreciation for all the cooperation and support you have extended to me during my tenure. I very much appreciate your leadership and the dedication of the staff at the Bank of Korea that has brought about the substantial progress in overcoming Korea's current economic problems. I will continue to follow developments in Korea with keen interest.

Wishing you every success in what will continue to be a challenging period ahead, I look forward to meeting you again in the future.

Please accept my highest personal regards

Sincerely yours,


Wanda Tseng
Deputy Director
Asia and Pacific Department



INTERNATIONAL MONETARY FUND
WASHINGTON D C 20431

June 17, 1998

CABLE ADDRESS
INTERFUND

The Honorable
Hoon Shim
Deputy Governor
The Bank of Korea
110, 3-Ga, Namdaemun-Ro
Jung-Gu
Seoul 100-794
Republic of Korea

Dear Mr Shim

I would like to inform you that I will be taking up new responsibilities in the Asia and Pacific Department of the IMF—overseeing the work on China and Hong Kong

It was a great honor and privilege to have worked with you and your staff in helping Korea through this difficult period. On this occasion, I would like to express my sincere appreciation for all the cooperation and support you have extended to me during my tenure. I will continue to follow developments in Korea with keen interest.

Wishing you every success in what will continue to be a challenging period ahead, I look forward to meeting you again in the future.

Please accept my highest personal regards.

Sincerely yours,


Wanda Tseng
Deputy Director
Asia and Pacific Department



INTERNATIONAL MONETARY FUND
WASHINGTON D C 20431

June 17, 1998

CABLE ADDRESS
INTERFUND

Mr Cheul Park
Assistant Governor
The Bank of Korea
110, 3-Ga, Namdaemun-Ro
Jung-Gu
Seoul 100-794
Republic of Korea

Dear Mr Park

I would like to inform you that I will be taking up new responsibilities in the Asia and Pacific Department of the IMF—overseeing the work on China and Hong Kong

It was a great honor and privilege to have worked with you and your staff in helping Korea through this difficult period. On this occasion, I would like to express my sincere appreciation for all the cooperation and support you have extended to me during my tenure. I will continue to follow developments in Korea with keen interest.

Wishing you every success in what will continue to be a challenging period ahead, I look forward to meeting you again in the future.

Please accept my highest personal regards.

Sincerely yours,

A handwritten signature in cursive script that reads "Wanda Tseng".

Wanda Tseng
Deputy Director
Asia and Pacific Department



INTERNATIONAL MONETARY FUND
WASHINGTON D C 20431

CABLE ADDRESS
INTERFUND

June 17, 1998

Mr Hyunchul Shin
Director
International Relations Office
International Department
The Bank of Korea
110, 3-Ga, Namdaemun-Ro
Jun-Gu
Seoul 100-794
Republic of Korea

Dear Mr Shin

I would like to inform you that I will be taking up new responsibilities in the Asia and Pacific Department of the IMF—overseeing the work on China and Hong Kong

It was a great honor and privilege to have worked with you and your staff in helping Korea through this difficult period. On this occasion, I would like to express my sincere appreciation for all the cooperation and support you have given me during my tenure. I will always remember the many kindnesses you extended to me during the various missions to Seoul. I will continue to follow developments in Korea with keen interest.

Congratulations on your new appointment as Director of the International Department. I wish you every success in what will continue to be a challenging period ahead, and I look forward to meeting you again in the future.

With warm personal regards

Sincerely yours,


Wanda Tseng
Deputy Director
Asia and Pacific Department



INTERNATIONAL MONETARY FUND
WASHINGTON D C 20431

CABLE ADDRESS
INTERFUND

June 17, 1998

Mr Hun-Jai Lee
Chairman
Financial Supervisory Commission
Seoul
Republic of Korea

Dear Mr Lee

I would like to inform you that I will be taking up new responsibilities in the Asia and Pacific Department of the IMF—overseeing the work on China and Hong Kong

It was a great honor and privilege to have worked with you and your staff in helping Korea through this difficult period. On this occasion, I would like to express my sincere appreciation for all the cooperation and support you have extended to me during my tenure. I will continue to follow developments in Korea with keen interest.

Wishing you every success in what will continue to be a challenging period ahead, I look forward to meeting you again in the future.

Please accept my highest personal regards.

Sincerely yours,

A handwritten signature in cursive script that reads "Wanda Tseng".

Wanda Tseng

Deputy Director
Asia and Pacific Department



Office Memorandum

To Mr Kwon

June 16, 1998

From Wanda Tseng

A handwritten signature in black ink, appearing to be "Wanda Tseng", written over the printed name.

Subject **Korea Rescue Loans**

As discussed, I would appreciate your help in obtaining further information on rescue loans. The attached was prepared with information provided to Mr Dodsworth. In particular, we would appreciate any information on

- 1 What is the definition of a rescue loan?
- 2 Do banks have to report "rescue loans" to the FSC (or how is this information collected)?
- 3 Is there any further information on the terms (i.e., interest rates, maturity) and other conditions for these loans? If not, can we say why we don't have this information?
- 4 Other than Dong Ah Group, can we say whether any of the other groups are restructuring (either on their own or forced by the creditor banks)?

Thank you

Attachment



Office Memorandum

To The Secretary

June 16, 1998

From Wanda Tseng

Subject **Korea Information Note on "Rescue Loans"**

The following provides information concerning "rescue loans" requested during the Executive Board meeting on May 29

- Commercial banks have been extending "rescue" loans to large corporate groups pending debt workouts and corporate restructuring.
- Eleven groups received rescue loans totaling W 3 trillion during October 1997 to May 1998 (Table 1)
- More than half of the total was loaned by the 12 banks considered to be undercapitalized and by Seoul Bank and Korea First Bank, while government-controlled banks accounted for 20 percent of the total
- Since the beginning of March four rescue loans have been extended
- The Dong Ah group, a large construction company, received three of the recent loans and accounts for more than one-third of the total, while the Hanwha group accounts for one-quarter of the total
- The terms of the loans to Dong Ah in May reportedly included new money at one-year maturity, the rollover of existing loans, the replacement of management, the sale of noncore units, and debt-to-equity conversions
- These loans are reportedly being made by banks independent of government intervention

Attachment

Table 1 Korea Rescue Loans

Group	Amount (In billions of won)	Dates of Loans
Dong Ah	1,041.5	10-Jan-98, 3-Apr-98, 6-May-98, 21-May-98
Hanwha	742.0	17-Dec-97, 28-Feb-98
Kohap	278.7	30-Jan-98
Haitai	250.0	15-Oct-97, 6-Nov-97, 13-Nov-97
Shin Won	200.0	11-Feb-98
Woo Barg	110.0	2-Mar-98
Jindo	106.0	19-Nov-97
Shin Ho	80.0	27-Nov-97
Hwa Sung	80.0	14-Apr-98
New Core	54.5	21-Oct-97
Hanil	50.0	31-Dec-97
Total	2,992.7	

Source: Financial Supervisory Commission

Table 2 Korea Rescue Loans by Month

Group	Amount (In billions of won)	Date
Haitai	54.7	10/15/97
New Core	54.5	10/21/97
Haitai	150.0	11/6/97
Haitai	45.3	11/13/97
Jindo	106.0	11/19/97
Shin Ho	80.0	11/27/97
Hanwha	300.0	12/17/97
Hanl	50.0	12/31/97
Dong Ah	294.0	1/10/98
Kohap	278.7	1/30/98
Shin Won	200.0	2/11/98
Hanwha	442.0	2/28/98
Woo Barg	110.0	3/2/98
Dong Ah	140.0	4/3/98
Hwa Sung	80.0	4/14/98
Dong Ah	81.5	5/6/98
Dong Ah	526.0	5/21/98
Total	2,992.7	

Source: Financial Supervisory Commission

4N
cc: BBA
DUS

98 JUN 16 AM 8:04

Office Memorandum

To: Ms. Tseng

June 16, 1998

From: J. R. Dodsworth Subject: **Korea: Letter to Minister Lee**

It appears to me that the letter regarding change in mission head can be quite short and could perhaps include a personal message from yourself. My suggestion would be along the following lines:

Dear Mr. Minister:

Vice-Minister Chung will have informed you that the discussions for the third quarterly review of the stand-by arrangement are scheduled to be held in Seoul during July 8 - 22. On this occasion, the staff team will be headed by Mr. Bijan Aghevli, Deputy Director of the Asia and Pacific Department. I am sure that you are well acquainted with Mr. Aghevli from his earlier work on Korea. More recently, he has been at the forefront of tackling the economic crisis in Indonesia.

While I will be taking up new responsibilities within the Asia and Pacific Department, I will, of course, be continuing to follow Korean developments with keen interest. Please accept my best wishes for success in what will be a challenging period ahead. It was a great pleasure to have worked with you.

(H)
cc: BBA
JUS

98 JUN 16 AM 8:04



Office Memorandum

To: Mr. Balino

June 16, 1998

From: J. R. Dodsworth Subject: **Korea: Resident Advisor to FSC**

The FSC have informed me officially that Mr. Abeles' candidacy has been rejected. They would like MAE to continue the search for a suitable advisor. The main reason for the rejection was that Mr. Abeles had not worked within an "advanced country" banking system. They said they would feel more comfortable with a candidate for example from the Bank of England or Banque de France. They are not looking for a candidate who has international experience across countries, but would like to find someone familiar with the banking system of an industrial country.

cc: Ms. Tseng

cc: Foss
SC
DS

THE NIXON CENTER

1615 L STREET, NW, SUITE 1250
WASHINGTON, DC 20036
(202) 887-1000 ♦ (202) 887-5222 FAX

ORIG: EXR

CC: MD

PRESIDENT
DIMITRI K. SIMES

June 15, 1998

Mr. Michel Camdessus
International Monetary Fund
By Fax: 202-623-4661

MR. FISCHER
MR. OUATTARA
MR. SUGISAKI
MR. M. CROSS
APD

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ROBERT B. ZOELICK

SENIOR STAFF
GEOFFREY KEMP
PETER W. RUDMAN
PAUL J. SAUNDERS

ASSOCIATE FELLOWS
PAUL GOBLE
BRUCE HERSCHENSOHN

Dear Mr. Camdessus:

The Nixon Center is pleased to invite you to a working lunch entitled "Korea: Up or Down?" with Lionel H. Olmer, a partner with Paul, Weiss, Rifkind, Wharton & Garrison. The session will take place at The Nixon Center on Tuesday, June 23, from 12:00 to 2:00 p.m.

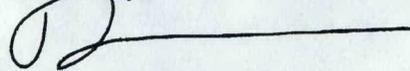
South Korean President Kim Dae Jung received a triumphal reception in Washington last week but has now returned to a very difficult economic situation at home. Though justifiably praised for his commitment to democracy and his personal courage, President Kim has yet to prove himself capable of solving the financial crisis he has inherited.

We are very pleased to have as a speaker a man with first-hand knowledge of South Korea's economic problems and of the abilities of the new president to solve them. Mr. Olmer is in Seoul this week meeting with President Kim, along with senior political and business leaders, and will share his observations from the trip.

A frequent traveler to Korea, Mr. Olmer served as Under Secretary of Commerce for International Trade during the Reagan Administration. He is also Vice Chairman of the Richard Nixon Library and Birthplace Foundation.

Please RSVP to Emily Klinker at (202) 887-5151. I look forward to seeing you on June 23.

Sincerely,



Dimitri K. Simes

80 6 W 91 NOV 86

058175

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IMF FAX CENTER



Office Memorandum

To Mr Hansen

June 12, 1998

From Wanda Tseng

Subject **Korea—Shipbuilding Industry**

At the Board meeting on the 1998 Article IV Consultation with Korea, you had asked whether staff had any information about alleged subsidies to the shipbuilding industry. You also said that European shipowners claim that Korean shipbuilders were delivering vessels well below production costs and that Korea has been supporting shipyards with government subsidies which have created unhealthy overcapacity. The following provides the information that we have.

Subsidies to the shipbuilding industry

Our understanding is that in fora such as the OECD, Korea maintains that it provides no direct government subsidies to the shipbuilding sector and the public support that is provided is in line with the OECD Agreement on Shipbuilding. Our understanding is that existing public support to shipbuilding in Korea consists mainly of loan guarantees or loans from the Korean Development Bank. In 1996, the government guaranteed about US\$2 billion in loans to finance the construction of new vessels, and to a limited extent, the purchase of second-hand ships. Korea maintains that these guarantees are at market conditions and meet the OECD guidelines for export credits (coverage 80 percent of credit, 12-year limits, interest rate within OECD benchmarks).

You should also be aware that large Korean companies, which include the main shipbuilders, do not qualify for the trade financing facilities established under the stand-by supported program. Only small- and medium-sized enterprises are eligible for these facilities.

Corporate restructuring and the shipbuilding industry

Korea ranked closely behind Japan, and ahead of China, as the world's second largest ship producer in 1997. The main shipbuilders are among the country's top conglomerates, including Hyundai Heavy Industry, Daewoo Shipbuilding and Heavy Machinery, Samsung Heavy Industries, and Halla Engineering and Heavy Industries. As you noted at the Board meeting, the Korean shipbuilding industry faced overcapacity problems well before the crisis, some of the investment surge that took place in 1994 and 1995 went into raising shipbuilding capacity.

The shipbuilding industry is highly indebted, the debt-equity ratio of the industry was 366 percent in 1996, and certainly increased in 1997. Halla, the country's 12th largest conglomerate sought bankruptcy court protection in early December 1997 for six of its subsidiaries—including the group's main flagship, the shipbuilder Halla Engineering and Heavy Industries—and is currently operating under court receivership. The group had a debt burden 20 times equity, and part of its problems resulted from its heavy investment in a new shipbuilding yard in the southern part of Korea that opened in 1995. Halla is now undergoing restructuring and has hired Rothschild Inc., a mergers and acquisition specialist, to advise the company on restructuring.

Shipbuilders' orders dropped by 45 percent (year-on-year) in the first quarter of this year, in part due to cancellation of orders by foreign clients following Halla Engineering and Heavy Industries bankruptcy. Order receipts rebounded somewhat in April, however.

Mr. Gordon (Ext. 38663) is available to answer any questions you may have on this memorandum.

cc The First Deputy Managing Director
The Secretary



Office Memorandum

HN
Kmm
SC
DUS

To Ms Iseng
From J R Dodsworth *(JD)*
Subject **Korea Co-operative Loans**

Following on from my fax of yesterday we have obtained additional information on the lending banks involved in the co-operative loans. The breakdown by lender (attached) indicates that of the W3 trillion total over half of the rescue loans have been extended by the 12 undercapitalized banks plus Seoul Bank and KFB. A further 10 percent is accounted for by merchant banks and insurance companies, while the banks where government has a large share -- KDB, KLTCD and Housing Bank -- account for 20 percent.

98 JUN 12 AM 8 17

Cooperative Loans to Business Groups
(unit: W billion)

Group	Date	Total Amt	SB	KEB	CBK	HANIL	KLTCB	CHB	KDB	KFB	HANA	Daedong	Boram	Shinhan	Kyongnam	DAEGU
Harta	10/15/97	54.7	6.7	5.5	6.5	3.4	9.6	8.0	7.2	6.8						
	11/13/97	45.3	5.6	5.3	5.3	2.7	8.0	6.7	6.1	5.6						
	11/6/97	150.0														
New Core	10/21/97	54.5	5.6	5.1		6.0	6.0	3.2		1.1	6.4	2.9		2.8		
Jindo	11/19/97	106.0	20.8	6.2				29.0	38.6							
Shin Ho	11/27/97	80.0	10.2					2.9	32.5	16.8						
Hanwha	12/17/97	300.0	18.2	9.2	21.0	32.2	36.2	17.9	100.0	13.7	17.1		10.3	16.6		
	2/28/98	442.0	47.3	30.8	52.8	106.7	18.7	33.7	45.1	47.3	13.5			15.2		
Hanil	12/31/97	50.0		4.1	10.5	21.1				10.5		3.8				
Dong Ah	1/10/98	220.0	101.5	80.2	15.8									10.6	11.9	
	4/3/98	140.0	64.6	51.1	10.1									6.7	7.5	
	5/6/98	60.2	27.8	22.0	4.3									2.9	3.2	
	5/21/98	600.0	149.2	90.8	44.8	14.8	17.2	12.5	1.6	21.9	19.3		7.5	22.9	10.2	1.6
Kohap	1/20/98	300.0	7.9	33.3		75.3	27.5		77.2	18.1						
Shin Won	2/11/98	200.0	9.3	55.6			9.1	7.1	41.8							
Woo Barg	3/2/98	10.0	26.1		9.5							18.3		6.6	19.3	
Hwa Sung	4/14/98	80.0	22.6											11.6		29.6
Total		2992.7	523.4	401.2	180.6	262.2	132.3	121.0	350.1	151.8	56.3	25.0	17.8	89.3	41.4	49.5
% breakdown			17.5%	13.4%	6.0%	8.8%	4.4%	4.0%	11.7%	5.1%	1.9%	0.8%	0.6%	3.0%	1.4%	1.7%

Cooperative Loans to Business
(unit: W billion)

Group	Date	Total Amt	Koram	Kookmin n	Dongwh a	Dongna m	CHEJU	Kyungg i	PUSAN	HCB	MB	Other	NACF	NFFC	NLCF	Check
Hartai	10/15/97	54.7														54.7
	11/13/97	45.3														45.3
	11/6/97	150.0									150.0					150.0
New Core	10/21/97	54.5											5.4			54.5
Jindo	11/19/97	106.0				5.1	6.3									106.0
Shin-ho	11/27/97	60.0	3.8				5.0	4.0					4.8			60.0
Hanwha	12/17/97	300.0	7.6													300.0
	2/28/98	442.0	20.1		10.8											442.0
Hanil	12/31/97	50.0														50.0
Dong Ah	1/10/98	220.0														220.0
	4/3/98	140.0														140.0
	5/6/98	60.2														60.2
	5/21/98	600.0	9.6	2.0	1.8	19.5			2.7	7.6	69.4	72.6	1.4			600.0
Kotap	1/30/98	300.0	17.5		12.1								21.3	9.8		300.0
Shin Won	2/11/98	200.0	8.9							18.6			11.4	21.0	16.2	200.0
Woo Bang	3/2/98	110.0								29.2						110.0
Hwa Surg	4/14/98	80.0								16.2						80.0
Total		2992.7	67.5	2.0	24.7	19.6	5.1	11.3	6.7	71.6	219.4	72.6	44.3	30.8	16.2	2992.7
% breakdown			2.3%	0.1%	0.8%	0.7%	0.2%	0.4%	0.2%	2.4%	7.3%	2.4%	1.5%	1.0%	0.5%	

cc HW
KMM
SC
DUS



Office Memorandum

To Ms Tseng

June 12, 1998

From J R Dodsworth *JRD*

Subject **Korea Interest Rates**

You will have noted the steep fall in the call rate during the first four days of this week (from 16 78 to 16 16) During this period, the won remained stable despite the downward drift of the yen and other Asia currencies With the weakening of the won at the outset today I discussed the situation with Assistant Governor Park who agreed that a more cautious approach may be needed given current tensions in the region The BOK slowed the downward movement and the call rate at 4 30 pm today was 16 09

Political pressure for further reduction in interest rates is mounting Today's lead stories include the usual "IMF Agrees on Lowering Rates" following the breakfast meeting between the Managing Director and President Kim Still, unless you disagree, I would continue to emphasize the gradual and symmetric aspects of interest rate policy

I have been looking at the impact of the reduction in call rates on actual lending rates BOK staff indicate that almost all new credit from banks is extended by way of overdraft facilities The rates charged on such facilities (for large firms)¹ increased from 13 percent in mid 1997 to 39 percent by December 1997 Since then overdraft rates declined to 24 percent by end-April, 21 percent by end May and to 19 7 percent as of yesterday Compared with the call rate the overdraft interest rate thus appears to have been falling more sharply since end April

98 JUN 12 AM 8 16

¹ This is an average rate for seven largest commercial banks

Copies to - Ms Tseng, Ms Gobat, Mr Stone, Mr Dodsworth, Mr Abrams

cc: Foss
SC
DS

INTERNATIONAL MONETARY FUND

June 11, 1998

To Mr Baliño

Subject **Korea - Report by Mr Michael Smith, expert on corporate debt workouts**

As promised in my e-mail, copy attached, I enclose Mike Smith's report and the detailed proposals he worked out with FSC staff (I thought it worth circulating immediately, even though it is in 'rough' form)

I will send to Laura Ard at the World Bank to-morrow, as she leaves at the week-end for Seoul

Personally, I think Mike Smith approaches the centralization/decentralization argument sensibly, but I would welcome views Also should the Fund be doing anything more, or should we leave it to the Bank, who are probably better placed to hire the expertise needed?

One possibility would be for Mike Smith to join the next, July, quarterly review mission, he would be available

Peter Hayward
(IS8-822, ext 36616)

98 JUN 12 AM 10 27

From Peter Hayward
To TBalino
Date 6/11/98 3 07pm
Subject Korea - corporate debt

Mike Smith rang this morning and I have now received his report which I will circulate

He was glad to have a couple of useful conversations with John Dodsworth after he had returned to Seoul and also spoke to Arne Berggren more than once on the phone. He did not, apparently, have an opportunity to meet Lee Hun-Jai but worked closely with his staff, particularly Kyungkug Seo and his immediate colleagues. He has helped the FSC develop a set of guidelines, attached to the report, and which deal with the centralized/decentralized issue. Mike Smith reports that the FSC were moving towards a compromise position which would as far as possible leave decisions in the hands of the banks but would give an important role to the Central Arbitration Committee which could, as a last resort, impose a solution. Mike Smith's view is that this is a sensible solution but emphasized he did not attempt to push his hosts into it. As to future assistance he agrees with John Dodsworth's view that the CAC could be the best point of access. He suggests the appropriate people would be "corporate recovery" experts from accountancy firms or banks (these are the same people who used to be called "insolvency practitioners"). Some of them are already in the region (and in Korea doing the diagnostic reviews) and their supply is not unlimited.

Smith would be available to return to Korea, but has not made any proposal to do so at this stage.

Peter Hayward

CC WTseung, JGobat, MStone, JDodsworth, RAbrams

VISIT TO KOREA BY M T R SMITH

2nd - 10th June 1998

My assignment at the instigation of the Monetary and Exchange Affairs Department of the I M F , was to advise the Financial Services Commission (FSC) of Korea on a possible framework for a work-out process for handling banks' negotiations with large corporates over debt reduction, liquidity problems and the minimising of losses in value I drew on my experience in the development and use of the London Approach but ensured that I took into account, where possible, the local conditions and culture In preparing for my visit, I had the benefit of a number of papers which had been prepared by both IMF staff and the Korean authorities on the problems facing the Korean economy, especially their banking and corporate sectors I also had a brief telephone discussion with Arne Berggren, a World Bank consultant, who had been involved in a detailed analysis and diagnosis of the particular problems and in suggesting possible structural solutions

During my visit, I had unfortunately little contact with either World Bank or IMF staff I met Stan Silverberg on a number of occasions (he was staying at the Hilton) and discussed with him the nature of his work on the banks The IMF Resident Representative in Seoul, John Dodsworth, was away for most of my visit and I saw him only briefly during my last two days Otherwise I came across no World Bank or IMF staff However I spoke briefly to Peter Hayward by telephone and had a number of conversations with Arne Berggren in Sweden, as he was sending comments on the corporate restructuring questions to the FSC during my visit

My main contact was Kyungkug Seo (known as Cliff) of the Structural Reform Planning Unit who is heavily involved in the preparation of the arrangements for corporate work-outs He gave me plenty of help, both by briefing me initially on the current position and in providing facilities for me We had many useful discussions on a possible framework for a work-out process He already had acquired a broad perspective of the London Approach from articles and his many questions were, I found, both penetrating and relevant As our discussions proceeded the advice he was looking for took shape and we were able to discuss and reshape my drafts to his requirements over

the last two days. My visit proved very timely, as Cliff and his team were under great pressure to produce specific plans for dealing with corporate restructuring for their Chairman. I had brief meetings with Dr. Goun Woo Seoh, Cliff's boss, and with Dr. Buhmsoo Choi, who is working on the banking sector.

The challenges facing the authorities, especially the FSC, are formidable. Deadlines for producing plans and for announcing specific action in the banking and corporate sectors, set by the new Government, look almost un-realistic as well as producing expectations among investors and markets. The objectives and targets call for fundamental change in the way both the banking and corporate sectors have traditionally behaved and operated. In terms of the corporate sector where very high levels of debt, especially among the Chaebols are unsustainable in the face of high interest rates, the Government has set various targets both for the reduction of debt and the liquidation of those parts of the Chaebols which are loss-making. In terms of the banking sector the traditional direction of lending by the Government has reduced banks' capability to assess credit risk. The changes being demanded by the Government will force the banks to improve their ability both to assess credit and to forge closer working relationships with the corporate sector. Such changes will require considerable resources and expertise at a time when the banks have additional challenges to meet, for example over capital adequacy.

I think that the time-table set for the corporate restructuring - the first stage, I believe, concerns the major 30 Chaebols - is probably unrealistic in such an environment. One of the main policy issues which was still under discussion during my visit was whether to centralise the corporate restructuring process or to force the banks to set up work out units and agree such restructurings with the assistance of a central arbitration committee. My contacts in the Structural Reform Planning Unit were in favour of forcing the banks to set up their own work-out units and to undertake most of the work on corporate restructuring, with resort, if they were unable to agree a plan, to an Arbitration body which would have powers to enforce a solution. The lack of experienced resources is a serious constraint on achieving rapid results among the

the banks although the banks will have to undertake such changes. The availability of expert resources, especially in terms of the work-out process, is the key to the success or failure of the targeted objectives for restructuring. These would have to come from abroad, notably Europe or the U S and the question is whether they should be attached to individual banks or to the Central Arbitration Committee. The latter is probably the most practical solution in the circumstances but it probably means that the 'Arbitration Committee' should have a more pro-active role in the process, at least in the early stages.

The view at the operating level of the FSC is that the banks must make the changes necessary to undertake work-out cases. To help the process they are considering ways of incentivising the banks to produce results. Given that aim I have drawn up a fairly detailed outline of a work-out process and how it would work. This together with a simplified set of principles which would be an important part of what the banks should seek to establish are attached to this note and have been discussed in detail with my contact. I have also set out an analysis of the challenge with arguments for and against a centralised system. Whether or not the Koreans decide to centralise the restructuring in the interests of speed and results, there will still be a need for an informal work-out process to be introduced in the banks. This will require considerable assistance, initially from those with experience of such a system. In the U K such experts are to be found in the main commercial banks and in the major accountancy practices which were heavily involved in the restructurings of the early 1990's. They have in most cases established corporate recovery units which specialise in this area of work. Those Korean banks with offices in London might consider approaching the specialised work-out units of the commercial banks for assistance and guidance.

The question of whether I should return at some stage to Korea is an open one. I think I have taken my work as far as it can go at the moment and the need in future will be for those with hands-on experience.

11 6 98

Handwritten signature

APPENDIX

General Principles for Workouts

The aim for a Korean workout procedure should be to have all banks working together through specialist workout teams supported by advisors and basing their procedures on a common and agreed set of principles. I suggest that all banks should agree to the following principles for the process:

- (a) Once a meeting of all banks involved has been called, all lending should be kept in place, but with no new drawings on unused facilities, no bank should seek repayment of its existing facilities.
- (b) If additional money is required by the company for its continuing trading, this should be agreed by all banks and shared pro-rata to their existing exposures.
- (c) Immediate steps should be taken by the group to establish the accurate financial position of the debtor, by appointing independent accountants to carry out a review as quickly as possible.
- (d) Once this has been received, the banks, together with the accountants (or other advisors) should formulate proposals for a restructuring of the company's outstanding debt.
- (e) At all stages banks should be treated equally on the basis of their outstanding exposures and any restructuring of debt should be based on equal sharing of loss.
- (f) At all stages information should be shared between all members of the workout group.
- (g) Decisions on restructuring proposals should be made on the basis of a (75%) majority vote (by value).

□ Specific Workout Process

Objectives

- to seek to carry out restructuring of companies as quickly as possible outside of the formal bankruptcy process,
- to minimize the cost of restructuring to the banks concerned,
- to ensure that any given restructuring will provide for the continuing viability of the company

Process

- (1) creation of workout unit, headed by a senior executive of the bank who can take responsibility for most decisions - and containing a minimum of 6 staff able to make credit judgments and negotiate with other banks,
- (2) Develop (through the senior executive) closer relations with those corporate customers in difficulty - involving the relevant loan officer at that stage may be helpful and important, although the workout unit should ultimately come to an independent view of the credit risks involved,
- (3) seek as much financial information on the company and identify all sources of lending both through other banks and through the company,
- (4) call a meeting of all the bank creditors (assuming that you are the lead bank in that you have the largest exposure) ,
- (5) analyze at the meeting the arguments for/against a restructuring if in favor of a restructuring, agree existing exposures*, and call for a

moratorium on existing lending i.e. no bank should seek repayment of an existing facility. If not in favor of restructuring, consider the other options, including liquidation.

* This would take into account the nature and seniority of the various facilities.

- (6) In the course of a restructuring, the need for additional cash needs will have to be considered separately by the creditor group.
- (7) The lead bank should suggest an independent review of the corporate's financial position (by accountants - not the company's auditors) and communicate this to the company (it may be helpful for the lead bank to ask some members of the group to participate in this communication), and then instruct the accountants, giving directions on what is needed by the banks - this will depend on how much financial information is available - and the date on which their report should be completed.
- (8) The lead bank should, discuss with the other banks the most efficient way forward. If there are too many banks in the group, a steering group should be appointed, consisting of a small number but representative of the many banks in the group. This would help to speed up discussion of restructuring proposals in the formative stage.
- (9) The accountants' report should take account of the company's existing budgets and business plans, and focus on the cash flow and the company's ability to repay debt.

- 7
- (10) Once received, the report would form the basis of discussions in the steering group to decide on the appropriate restructuring and to discuss possible proposals with the management of the company
 - (11) The steering group should put forward (a number of) proposals for the creditors group to consider and should call a meeting – the meeting would be designated as the first formal meeting to discuss – and agree on a particular set of proposals
 - (12) A 75% majority (by value) will be required for the approval of a set of proposals for the restructuring of a company
 - (13) If agreement cannot be reached at the first formal meeting of the creditors group, a formal record should be made of the reasons for the failure to agree
 - (14) A maximum of 3 such formal meetings can be held to secure agreement. If at the end of the 3rd meeting no agreement is forthcoming, formal notification will be made to the Central Arbitration Committee (CAC). That committee will have the powers to decide on what proposal the restructuring should be based
 - (15) If agreement is reached by the creditors group, the decision will be communicated to the company, and steps taken to implement the decision by drawing up appropriate documentation
 - (16) The creditors group should ensure that the company is closely monitored during the implementation of the restructuring agreement and that any failure to achieve the necessary targets requires a

meeting of the creditors group This could be the responsibility of the lead bank

The Problem

Corporate restructuring is necessary to reduce companies' traditional high levels of debt (the target set by the government is 200%), eliminate cross guarantees in the chaebols, improve the transparency of financial information, and if necessary, put into liquidation non-performing assets

The Challenge

Change the ways in which business and finance have hitherto operated and introduce a system whereby corporate restructuring can be carried out as efficiently and speedily as possible outside the formal bankruptcy process

The hurdles

The lack of a proper relationship between the corporates and the banks, previous 'directions' of bank lending by the government, the lack of a credit risk assessment culture, no previous culture of banks working together to resolve problems, an urgent need to create some structure and process, fragility in the banking sector, lack of expertise

Possible solutions

(a) a centralized system directing workout solutions

(b) a decentralized system in which the banks set up processes to deal with restructuring

(c) Variations in (a) and (b), involving some central body, and possible incentives for banks (and companies ?)

centralized system – arguments for and against

For

- (1) lack of any experience / expertise in the banks in managing workouts
- (2) traditional lack of cooperation between companies and banks
- (3) traditional lack of cooperation between banks
- (4) provide a framework for banks to develop for themselves

Against

- (1) banks will have to build up credit risk assessment capability and a cooperation approach as quickly as possible
- (2) a centralized body would provide little motivation to the banks to set up their own methods
- (3) a centralized body would be faced with a huge workload which could delay progress

Decentralized system – arguments for and against

For

- (1) banks will have to develop the capacity and capability as quickly as

possible

- (2) the banks will be forced to work with the corporate sector and develop closer relationships, not least in exchanging information

Against

- (1) lack of expertise
- (2) banks could find it difficult to negotiate on a collective basis
- (3) the need for some sort of arbitration or mediation

Conclusion

Some sort of initial central involvement is necessary to help the development of the workout process and to provide some element of arbitration or guidance. The proposed Central Arbitration Committee is a sensible compromise between a fully centralized system and a decentralized one. It should have minimum powers to impose a solution on the parties concerned. Incentives for the banks (and for the corporates) would be a useful tool in achieving results – perhaps additional input of capital for the banks and fiscal benefits for corporates.

Workout Processes Some potential difficulties

In this section, I set out some areas of workouts which from our experience in London can give difficulties. Any system which is based

on broadly based principles is bound to encounter operational questions and challenges, and it will be for banks in Korea to ensure that they operate within agreed guidelines and principles

Lead Bank

The lead bank carries a great deal of responsibility. Its importance cannot be over-exaggerated, the way that the lead bank sets about its task can make a substantial difference to the progress that is made. It has to perform a difficult balancing act. It must, for example, provide firm, but not overbearing leadership. It must be a good communicator, and it must not take the views of banks for granted. It must also be flexible, able to respond to the unexpected and prepared to give ground in difficult discussions. All banks should ensure that they raise concerns about any part of the workout process as soon as possible.

Legal Representation

A workout is not a legally-based process. The principles do not lend themselves to legal interpretation and banks should not place over-strict interpretation on the principles. One of the advantages of an informal system is that it can be flexible. Lawyers may well try to influence interpretations (as they have unsuccessfully tried to do in the UK) but should be resisted. Lawyers will nevertheless be required to advise their clients but care should be taken to avoid too much cost being incurred in legal advice.

Responsibilities

Those involved in workouts carry considerable responsibility for helping to move the process along. Hard decisions will have to be taken in the course of meetings, and it is important that those representing their banks have the authority in most cases to give a decision. There will be occasions when such authority will have to be sought outside a meeting, but in the interests of efficiency, speed and cost these occasions should be limited. Delay in obtaining approval for a particular course of action can be harmful to the impetus of a workout.

New Money

Once a standstill (effective moratorium) has taken effect (when the banks are notified by the lead bank of a meeting to consider restructuring), there will be an effective freeze on existing facilities. A company's cash requirements will therefore have to be met either from internal sources or from a new facility which should be shared pro rata by the banks involved. The amount required should be checked by accountants and should be viewed as a short term facility, pending a restructuring agreement.

Cash Flow

One of the key parts of any restructuring is the ability of the company to service debt, reduce its costs and generate sufficient cash to ensure that it can meet future obligations without the need for new borrowings. The focus of the accountant's report should be on the production of cash flow.

over the period of the restructuring (the agreement may be fixed in term)

Sharing of Information

It is very important for the success of a workout that all the financial creditors involved in the group are given the same information at the same time. Responsibility for that rests principally with the lead bank. Smaller creditors (in terms of size of exposure) may feel disadvantaged and can cause unnecessary difficulties if they feel they are being treated differently by the lead bank.

Other Creditors

There may be approaches from other non-financial unsecured creditors for inclusion in the workout process. These should be resisted, since it will be impossible to include all such creditors. The banks hold the key to any restructuring and could therefore suffer heavier losses in a restructuring than other creditors. Trade creditors are unlikely to want to participate in a workout, and their significance to the company's continuing viability may mean that new money is required.

Costs

It will be important to keep the costs of any restructuring down to a minimum. The costs of advisors and accountants have to be checked carefully, and responsibility for that lies as much with the lead bank. But all the banks have a responsibility, especially in terms of the advice which

individual banks may need. Delays in reaching agreement can be particularly expensive (although the important point is that the banks should arrive at a prudent and practical solution!)



INTERNATIONAL MONETARY FUND

WASHINGTON, D C 20431

ASIA AND PACIFIC DEPARTMENT

Fax # (202) 623-4432

Tel # (202) 623-7602

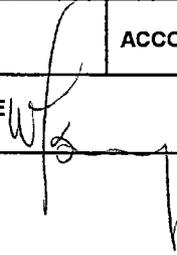
MSG NO	DATE June 11, 1998	PAGE 1 OF 4
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TO The Honorable
Lee Kyu-Sung
Minister of Finance and Economy
Ministry of Finance and Economy
Republic of Korea

011-82-2-503-9138

Please see attached

FROM Hubert Neiss
APD/AI

ROOM NO 4-320	EXTENSION (202) 623-7604	ACCOUNT CODE
AUTHORIZED BY Hubert Neiss	SIGNATURE 	



INTERNATIONAL MONETARY FUND

WASHINGTON, D C 20431

ASIA AND PACIFIC DEPARTMENT

Fax # (202) 623-4432

Tel # (202) 623-7602

MSG NO	DATE June 11, 1998	PAGE 1 OF 4
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TO Mr Lee Hun-Jai
Chairman
Financial Supervisory Commission
Seoul
Korea

Fax 82-2-3771-6129

Please see attached

FROM Wanda Tseng
APD/AI

ROOM NO 4-320	EXTENSION 37182	ACCOUNT CODE
AUTHORIZED BY Wanda Tseng	SIGNATURE	



INTERNATIONAL MONETARY FUND

WASHINGTON, D C 20431

ASIA AND PACIFIC DEPARTMENT

Fax # (202) 623-4432

Tel # (202) 623-7602

MSG NO	DATE June 11, 1998	PAGE 1 OF 4
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TO Mr Kyung Wook Hur
Director
IMF Task Force
Financial Policy Office
Ministry of Finance and Economy
Korea

Fax 82-2-504-7873

The attached has been faxed to Minister Lee Kyu-Sung and Mr Lee Hun-Jai

FROM Wanda Tseng
APD/AI

ROOM NO 4-320	EXTENSION 37182	ACCOUNT CODE
AUTHORIZED BY Wanda Tseng	SIGNATURE	



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WASHINGTON, D C 20431

ASIA AND PACIFIC DEPARTMENT

Fax # (202) 623-4432

Tel # (202) 623-7602

MSG NO	DATE June 11, 1998	PAGE 1 OF 4
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TO Mr John Dodsworth
Senior Resident Representative
Seoul, Korea

011-82-2-792-1651

S

The attached has been faxed to Minister Lee Kyu-Sung, Mr Lee Hun-Jai, and Mr Hur

Attachment

FROM Wanda Tseng
APD/AI

ROOM NO 4-320	EXTENSION (202) 623-7182	ACCOUNT CODE
AUTHORIZED BY Wanda Tseng	SIGNATURE	



INTERNATIONAL MONETARY FUND
WASHINGTON D C 20431

CABLE ADDRESS
INTERFUND

June 11, 1998

The Honorable
Lee Kyu-Sung
Minister of Finance and Economy
Ministry of Finance and Economy
Government Building II
Kwacheon, Kyunggi Do, 171-11
Republic of Korea

Dear Mr Minister

Your government has taken several important measures recently to further liberalize the capital account, bringing forward some measures contained in the Letter of Intent of May 2, 1998. We welcome these measures, particularly those related to the liberalization of foreign direct investment and of restrictions on equity ownership in Korean companies. At the same time, and as your government recognizes, it would be important that the removal of restrictions on short-term capital movements be accompanied by adequate safeguards, particularly strengthened prudential regulations, consolidated supervision, and improved monitoring.

More specifically, restrictions on foreign investment in domestic money market instruments issued by financial institutions (CDs and RPs) and corporate borrowing of one-two year maturities are being liberalized ahead of the schedule in the Letter of Intent. These liberalization measures were timed in the Letter of Intent to take into account the implementation of a number of prudential regulations, particularly those related to short-term foreign borrowing and foreign exchange exposures, and with the start of consolidated supervision (January 1, 1999). Also, the Letter of Intent envisaged the submission of necessary legislation to ensure compliance with reporting on external liabilities of the corporate sector by October 31, 1998.

On a related subject, we thank you for the opportunity to review the draft paper on revisions to the Foreign Exchange Act. We will communicate, through Mr Dodsworth, more detailed comments on these revisions directly to your staff. As a general point, we welcome the further liberalization of the capital account, particularly the move from a positive list to a negative list system, and the proposed streamlining of foreign exchange regulations. Again, the accelerated liberalization of short-term capital flows envisaged in the revisions to the Foreign Exchange Act highlights the need for safeguards in terms of prudential regulations, supervision, and monitoring.

Thus, in view of the acceleration of capital account liberalization, there is also a need to move faster on the prudential regulations on short-term foreign borrowing and foreign exchange exposures and on the monitoring and reporting requirements. We would urge your consideration of accelerating these measures from those set out in the Letter of Intent (shown in the enclosure). I look forward to hearing from you on the possibility of accelerating these measures. The July review mission will also discuss this matter further.

A copy of this letter is also being sent to Mr. Lee Hun-Jai at the Financial Supervisory Commission.

With best regards,

Yours sincerely,

A handwritten signature in black ink, appearing to read "H. Neiss". The signature is written in a cursive, slightly slanted style.

Hubert Neiss
Director
Asia and Pacific Department

Enclosure

Prudential Regulations and Data Monitoring Measures

(Timing of implementation shown in the May 2, 1998 Letter of Intent)

- Measures on strengthening compliance with existing guidelines for commercial banks to limit maturity mismatches in foreign exchange and the announcement of similar guidelines for merchant banks (August 1, 1998)
- The full phase in of prudential guidelines to limit maturity mismatches in foreign exchange for merchant banks (December 31, 1999)
- The announcement (August 15, 1998) and implementation (as of January 1, 1999) of additional regulations for commercial and merchant banks. The additional regulations to include introduction of an internal liquidity control system based on a maturity ladder approach, agreement with the Financial Supervisory Commission (FSC) on allowable maturity mismatches, the monthly monitoring of implementation by the FSC, and the public disclosure of statistics on foreign currency liquidity by bank
- With respect to foreign exchange exposure limits, the implementation of the supervision of observance to be undertaken by the FSC, the replacement of separate limits on combined spot and forward positions, the incorporation of cross-currency positions in the measurement of exposures, and the introduction of consolidated limits for banks, including their offshore branches (November 15, 1998)
- The introduction of improvements to the reporting of off-balance sheet foreign currency denominated exposure of financial institutions and the submission of necessary legislation to ensure compliance with reporting on external liabilities of the corporate sector (October 31, 1998)



Office Memorandum

To Mr Saito

June 11, 1998

From Wanda Tseng

A handwritten signature in black ink, appearing to be "WT", written over the printed name "Wanda Tseng".

Subject **Seminar in Korea**

Sorry for the delay in responding to your memorandum of May 21 on the seminar in Korea

As you may know, EXR has been asked by Mr Fischer to develop a public relations program in the crisis countries

The seminar in Korea (and timing) should be considered in that context

cc Mr Neiss
Mr Anjaria
Mr Chu
Mr Dodsworth



Office Memorandum

cc HN
KMN
SC
DUS

June 11, 1998

To Ms Iseng

From I R Dodsworth *IR*

Subject **Korea Cooperative Loans**

I have received from the FSC the attached update on cooperative loans extended to business groups during this year. The loans that are listed for 1998 total W 15 trillion (\$ 1.5 billion). In addition, total amount of loans in 1997 was W 840 billion (see second attachment). The breakdown by lending banks shows that largest loans are coming from the troubled banks i.e. Seoul Bank, Hanil Bank, KEB and CBK.

98 JUN 11 AM 8 21

Attachment 1

Cooperative loans to Business Group

(Billion won)

Business Group	Agreement date	Agreed Amount	Allocation by bank
Dong Ah Const	1st Jan 10 98	220	SB 101.5 KEB 80.2 CBK 15.8 Kyongnam 11.9 Shinhan 10.6
	2nd Apr 3 98	140	SB 64.6 KEB 51.1 CBK 10.1 Kyongnam 7.5 Shinhan 6.7
	3rd May 6 98	60.2	SB 27.8 KCB 2.2 CBK 4.1 Kyongnam 3.2 Shinhan 2.9
	4th May 21 98	600	banks(23) 460.3 non-banks(30) 139.7
Kohap	Jan 10 98	300	Hanil 75.3 KDB 77.2 KEB 33.3 KLTCB 27.5 Agriculture 21.3 KFB 18.1 Koram 17.5 Donghwal 2.1 Fisheries 4.8 SB 1.9
Hanwha	Feb 10 98	442	Hanil 116.7 CBK 52.8 KFB 90.8 KFB 47.3 SB 47.3 KDB 45.1 CHB 37.7 Koram 20.1 Shinhan 15.2 Donghwal 10.8 KLTCB 8.7 Hanil 3.5
Shin Won	Feb 11 98	200	KEB 56.6 KDB 41.8 Fisheries 2.1 HCB 18.6 Livestock 16.2 Agriculture 11.4 SB 3 KLTCB 9.1 Koram 8.9 CHB 7.1
Woo Hang	Mar 2 98	110	SB 26.1 HCB 24.2 Daegu 18.3 CBK 9.5 Kyongnam 8.6 Daedong 18.3
Hwa Sung	Apr 14 98	80	Daegu 29.6 SB 22.6 HCB 16.2 Shinhan 11.6

* SB Seoul Bank KEB Korea Exchange Bank (CBK The Commercial Bank of Korea)
KLTCB Korea Long Term Credit Bank CHB Cho Hui Bank KDB The Korea
Development Bank KFB Korea First Bank HCB Housing & Commercial Bank
Agriculture National Agriculture Cooperative Federation Fisheries National Federation
of Fisheries Cooperative Livestock National Livestock Cooperative Federation

Attachment 2

구분 세정기정간

김경하

주요 계열에 대한 협조융자 현황

to ~~Checkel~~ ~~Cooperation~~ ~~Financing~~ ~~Scheme~~

3,111,537,200
For 1997 6.8%

계열명	협조융자 합의일자	협조 유자규모	allocation by banks 은행별 분담액
Harta 에 태 (조흥)	은행 97.10.15	은행 547	조흥 80 장신 96 산업 72 제일 68 서울 07 삼위 65 외환 65 한일 34
	은행 97.11.13	은행 453	조흥 67 장신 80 산업 61 제일 56 서울 56 삼위 53 외환 53 한일 27
	총금 97.11.6	총금 1500	
New Core 뉴코어 (제일)	97.10.21	545	제일 111 이나 64 대동 29 장신 60 한일 60 신한 28 서울 56 농협 54 외환 51 조흥 32
	97.11.19	1060	서울 208 삼위 346 조흥 290 경기 63 외환 62 제주 51
Shin Ho 신 호 (세일)	97.11.27	800	산업 325 제일 168 서울 102 경기 50 농협 48 부산 40 한미 78 조흥 29
	1차 97.12.17	시은 2000 산업 1,000	한일 322 장신 362 산업 210 서울 182 조흥 170 이나 171 신한 166 제일 137 보람 103 외환 92 한미 76 산업 1,000
Hanwha 한 화 (한일)	2차 98.2.10	4420	한일 1067 삼위 528 외환 308 세일 473 서울 473 산업 451 조흥 337 한미 201 신한 152 동화 108 장신 187 하나 135
	97.12.31	500	한일 211 삼위 105 제일 105 외환 41 내동 38
Hanil 한 일 (한일)			

* 본지원 합의액은 해당계열의 기존 주도어음 정리 및 리스크해치 폐지확약 등으로 지원한
신용 한도

** (내국 세원) 거래은행

1998 = 2152.2 billion
1997 = 840.5 billion



Office Memorandum

To Ms Tseng

June 11 1998

From I R Dodsworth 

Subject **Korea Letter from Pan National Movement**

The Pan National Movement staged a small peaceful demonstration against IMF policies outside the Ministry of Finance and Economy earlier today. Following the demonstration, I met with several representatives of the civic groups and trade unions and was handed the attached letter addressed to the Managing Director. The letter contains a list of demands relating to capital account liberalization, interest rates, privatization, and labor market flexibility.

The letter states that the IMF-supported program in Korea has so far been a failure and has contributed to social unrest and hardship. The Pan National Movement requests that the economic program be comprehensively reevaluated and that NGOs are allowed a larger role in future policy planning.

In the ensuing discussion, I attempted to explain the role of the Fund in Korea and the rationale for various policies. I also stressed the importance the Fund attaches to hearing views from all segments of society, and that I would be willing to participate in a coming NGO forum on the impact of IMF policies.

cc EXR

한국국민의 이름으로 일방적인 구조조정 협약의 폐기를 요구한다 - IMF에 보내는 공개 서한

IMF이 일방적인 구조조정 프로그램으로 인해 한국에서의 외환위기가 실효적이지 못하게 전 회하고 있다 IMF 구조조정 프로그램은 한국에 앞서 이미 세계 100여개국에서 거의 인위적이 내 용으로 적용되었다 IMF는 자본/금융시장에 대한 구제의 전통적인 통제수단은 원칙적 없애버리 기' '의 원칙과 경기부흥정책을 강요하여 - 자본/경기 경제의 기압이 되고 있 - 공공부문을 재정적지박 이유로 파탄되도록 미연화시키는 방식 너머로도 구조조정을 추진하였다 그 결과 IMF가 발표 한 내세워야 외환/통화기사의 안정화나 경제위기의 극복과는 거리가 멀었다 오히려 IMF구조조정 프로그램이 식료품/에너지 시장 등 한국적지표의 '투기장'으로 제해비됨으로써 국제금융시장이 불안 정성에 완전히 노출되어 악기가 확산되어온 따름이었다

세계화라는 현실 속에서 분기기한 선택이라는 IMF프로그램의 사용결과 난이구들이 겪어야 했던 부작용은 더욱 악화하기만 하다 비부적자는 극단적으로 심해졌고 경제성장률은 정체되었으 며 1부부는 '단정적' 인업이 고도에 시달리' 있다 브라질이 경우 상층부 20%가 1 나라 부의 60%이상을 차지하고 있는 반면 이구의 20%를 차지하고 있는 미산층부 겨우 부의 2%만 갖고 사 아가고 있다 이러한 IMF구조조정 프로그램에 대해 비판은 단지 노동기대이니 시보적 경제하기 든에 의해서만이 아니라 보수적인 수류경제학자 및 보수어론, 심지어 IMF 자신들에 의해서도 제 기되고 있는 상하이다 실제로 지난 1월 13일 제출된 비밀보고서에서 IMF이사회는 인도네시아 금융위 기에 접근하는 과정에서 IMF가 인도네시아의 금융체제의 미비시각을 '류로 범했다 고 지적하고 있다 그리고 현재 아시아 금융위기가 일본 홍콩 중국 등으로 확산되고 있는데 대해 IMF- 사적 추수고 책 아닌가? 작금의 아시아 경제위기가 아시아뿐만 아니라 결국은 전세계적으로 부역 투기 스펙시사 보- 부문에서 수-와 베풀을 가져올 지이때 과연 이것이 IMF 구조조정 프 로그램의 실효적 과이 과적 수적(overkill)과 무관하다고 할 수 있는가?

그런데 왜 IMF는 1 나라에서 이미 실패한 것으로 판명된 IMF구조조정 프로그램은 근본적 의 재검토없이 한국에 그대로 적용하고 있는가?

위기를 불러온 원인을 처방책 이라고 내놓고 있는 IMF의 구조조정프로그램은 또다른 실패를 갈요하는 것이 아닌가?

IMF는 위기를 불러온 원인을 처방책 이라고 내놓고 있으며 거침이 효과가 없어도 처방 을 지지 않는다 한쪽에 비판의 외환/금융위기를 발생시킨 원인중의 하나가 김영삼대통령 정부 시정부의 부지혜로 게마화 시우화 적적으로 미하 지분에 대한 통제수단 및 능력이 상실에 이 언음은 누구도 부이할 수 없는 사실이다 따라서 위기에 대한 처방도 자본의 유산인에 대한 통제 능력이 가최 규제수단이 확보'라는 마함으로 추진되었어야 함은 당연하다 그러나 이와달리 IMF 는 인공적으로 자본/금융시장의 완전한 탈규제와 자유화 및 한국경제위기에 대해 처방으로 제시 하고 있다 위기가 원인을 위기의 처방책이라고 내놓고 있는 불미디 이는 한국사학 진계등 거대 한 사슬은 무어 세계자본주의 경제라는 퍼즐의 난순한 한 조각으로 전락시키려는 거대한 기획이 아니고 무엇이겠는가 IMF- 한국경제를 올바른 개혁에 ' 관심부시 안' '도되지 '국회기부 미 서시사본주의국가 규제수권이득의 이익만을 보자하고 한국 및 아시아 국가학의 기가사어들을 현 상에 매수하면서 통상시서우-는 추구적가면의 자유로운 이용추구활동은 보장한 제도들을 구부

하- 서예반 시작하' 있는 것으로 보인다

그러나 이 나라에서 이미 실패하면서 셋째로 심각한 위기의 원인이었던 것은 저항책이라고 내놓고 있는 IMF의 구조조정 프로그램의 적용결과로 한국경제위기를 탈출하는 비사수가 아니라 또 다른 기계적타운 부채 일으키는 지분값이 뒤 거이고 또한 눈앞이 이익극대화에 그들로 지참하고 이는 연구저지부에 그 대한 제압으로 나타난 것이다

기초의 IMF 구조조정협약이 폐기되고 한국 민중의 삶이 보장되는 방향으로 새로운 협약이 체결되지 않고서는 경제위기가 극복될 수 없다

그 동력주자들이 주장하는 IMF는 경제정책의 인간적 사회적 결과물 의-적으-외면하고 이니 이제 개혁이 막 시남시안 IMF구조조정 협약에 따라 사국 기업들은 극도의 고통을 겪고 있다 한때에 수천명의 시구실업자가 발생하면서 기리는 밝혀하는 실직자들이 급증하고 있는가 하면 세계화 변화도 줄고 있고 심지어는 막다른 골목에 내몰린 실직자들이 스스로 모순을 쓴-이근에 IMF기상도 주은 이고 있다 또한 미군작이식 정리체제가 본격적으로 추진되고 있는 이 개혁부의 민영화도 급격하게 진행될 예정이다 이 모든 것이 개혁이라는 이름으로 IMF 구조조정 프로그램이라는 이름으로 추진되고 있다 그러나 수백만명의 실직자와 수천명의 최박적이 자살과 같은 내구모익 삶의 파파에 대해서 누가 책임을 지야 아-가? 실제로 IMF협정 2사이의 비비협약에는 분시상-이 유연화 및 분-합의 힘은 아회시키려는 기회의 포함되어 있 좋은 우리는 확인할 수 있었다

최근 허구에서 개혁되고 있는 IMF구조조정 프로그램이 가장 큰 문제점은 노동기준 또한 민중들은 과탄시키고 있다는 점이다 한국내에서 진정으로 개혁은 원하는 유일한 세력이고 또 개혁으로 서모시킬 수 있는 유일한 세력인 노동-중 민중들의 파단은 비루 경제개혁 지체의 파된으로 직면당시 때문이다

한편 피해타사자인 안우 민-들은 기존의 IMF구조조정 프로그램이 근본적으로 새겨진 양고 나트나라의 경우와 비슷하게 한국사회가 몰려가는 것을 그냥 보긴마 있지는 않음 거이다 만약 IMF가 허구 미수주의 저항해 요구를 바아드이지 안고 중전이 반칙을 계속 강행한 기우 허구 민중들의 엄청난 저항에 부너힐 거인은 언중처 경고한다

IMF는 국제기구가 개입성을 거부하고 미국의 이익에 봉사하고 있다 미주주의의 책임은 이 나라의 부-한 경제파장이 이 나라 국민들이 이해하고 삼녀하면서 함께 결정하는 것이나 그러나 한-정서와 IMF에게 걸린 현악은 외원고산은 될기- 이러한 민주주의의 모든 원칙은 사망으며 추진되었다 지금까지도 IMF는 한국인 국민들과 전혀 대화하려 하지 않고 있다 구조조정 프로그램에 의사치러라도 이-바 기준재정의 해시이라고 한 수도 있으며 한국의 민주서인 민간단체들이 오랫동안 요구해온 구방비 사사 주의는 한국은 미국의 무기를 계속 사야 한다는 미국방부 장군이 말 치미년에 자가네 비러디 IMF는 이때 임무했다 이- IMF'양국이 이주것대관 사용하고 있다는 가장 임정인 사제라 하겠다 또 IMF가 한국에 강요한 구조조정 프로그램의 결과가 기군이 100천이 게 위해된다는 사실에 대해서 IMF는 침묵하고 있다

이와 같이 IMF는 경제적 사회적 자원들 이해하지 부하거나 의도적으로 저부하고 있다 이처럼 무책임한 국제기구는 정책의 무능함과 아울러 그 존재 의의를 정당하게는 자은 수 없다

좋은서이 미수적이 경제정치 구조로 외화 개혁은 IMF의 전유물이 아니라 한국 국민 모두의 열망이며 기금까지 오랫동안 해외 탐 그리고 대승적인 민주적 운동은 동하여 이루어 이 것이 나 개혁과 민주주의 주체는 무책임하고 기미원 외부의 판권기구가 아니라 바로 한국의 민중이다

이러한 기부고부너 이식된 외방적인 프로그램으로 개혁이 스페이 미스이 삶이 가리되고 동시에 국민경제의 기간이 와해되고 빈부 격차가 증대될 때 개혁은 불가능해진다 이렇게 되면 개혁은 개혁이 아니나 늘정 이익집단은 거한 투입으로 귀락하는 것이다 우리는 마저런 이속한 평화적 정 권규체가 내량실어과 석제주권 타타도 인하여 무억비배시에서 비주주익와 인권의 가시가 조롱나는 것은 크게 우려한다 우리는 한국에서의 IMF의 구조조정 프로그램이 개혁의 사외서 기마 이로부터 민주주의의 사회적 기반을 파괴시키는 점은 엄중히 경고하며 다음과 같이 요구한다

우리의 요구

- 가) IMF는 국민경제를 파괴하는 자본/금융시장 자유화, 탄규제 공세로 즉각 중단하라!
- 나) IMF는 공공리 및 조신속 재정정책 강요를 즉각 중단하라!
- 디) IMF는 공공성 가치등 스변시킨 것이 민영화 공세를 즉각 중단하라!
- 리) IMF는 정리폐고제나 근로자파견제를 강요하며 한국 민중들이 생존을 위협하는 노동시장 유연화 공세를 즉각 중단하라!
- 마) IMF는 한국경제의 구조조정 프로그램 전반이 이미 실패했음은 인정하고 이는 전면 재검토하라!
- 바) IMF는 한국에 가하 선택 기업과점에서 번국민운동본부를 비롯한 민주적 민간단체와 성실하게 협의하라!

1998 6 11

공동 대표단 권영진, 김근수, 김종배, 김진균, 문대길, 문장현, 양현수 오세권, 유초하, 이갑용, 이수갑, 이수규, 이창복, 임종철, 소영건, 지원스님, 천영세, 최영노, 홍근수(이상 가나다 순)

고용 실업대책과 재벌개혁 및 IMF대응을 위한 범국민운동본부



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Mr. Balino.



Office Memorandum

98 JUN 10 AM 8:04

To: Ms. Tseng
Mr. Balino

June 10, 1998

From: J. R. Dodsworth (RD)

Subject: Korea: Meeting with FSC Chairman on June 9

You may find this summary of my discussion with Mr. Hun Jai Lee useful as background information. The meeting covered three main areas:

- Appraisal of the twelve undercapitalized banks;
- Appraisal of leasing companies;
- Extension of the corporate review process, and plans for debt workouts; and
- Rollover program for small-to medium-sized companies.

1. Appraisal of Rehabilitation Plans

It is planned that Mr. Lee will brief President Kim on the commercial bank rehabilitation plans next Tuesday, June 16. The work of the Appraisal Committee will begin on June 18.¹ The Commission has already formed some tentative ideas on how the process is likely to develop. At least four banks are expected to have positive capital adequacy ratios (of 3-5 percent). These are Korea Exchange Bank, Cho Hung, Hanil and Commercial Bank of Korea. Of these, only KEB--which is well advanced in forming an alliance with Commerzbank--has a high probability of having its initial plan accepted. The others may need to enter a second track process where revised plans would be called for (these would be expected in 20-30 days following decision on initial plan).

For other banks, many of which may prove to have negative net worth, the FSC is likely to distinguish between national and regional or local banks. The first group (which would

¹ The nomination by the Fund of the international expert to join the Appraisal Committee is thus expected at latest by June 15.

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include Donghwa, Dongnam, Dae Dong and Pyonghwa banks)² would require active programs or firm merger plans for liquidation to be avoided. For the remaining four regional/local banks the FSC's approach may be more relaxed in that they may be given additional time to recapitalize and could have different capital adequacy targets. The FSC is considering adopting a rule that banks should be disbarred from international operations unless they reach a specified minimum capital adequacy ratio (not yet determined, but tentatively 4-5 percent).

The Chairman noted that several banks under review had started merger talks with stronger (but generally smaller) banks. He considered these merger proposals as attempts by the weaker banks to preempt the review process and said that there would naturally be opposition from the shareholders of the stronger banks to such mergers. The use of public funds would be crucial in encouraging consolidation of the banking system.

On the appraisal process, I emphasized (i) the need for rigor in judging the realism of the recapitalization plans, (ii) the large credibility loss that would be involved in accepting a plan that subsequently proved infeasible, (iii) the expectation in the LOI that use of public funds would be accompanied by private capital contribution, and (iv) that exceptions to the 8 percent capital adequacy target would be damaging to the overall process.

2 Leasing Companies

A preliminary review of leasing companies has just been completed by the FSC. The tentative findings are that of 25 companies only 4 have positive net worth. Of the remaining 21, perhaps 6-8 may be saved through capital injection, while others will need to be closed. Given that most of the leasing companies are subsidiaries of commercial banks, these results will be held back and no action will be taken until the results of the bank exercise are announced.

3 Extension of Corporate Review Process

The Chairman explained that the bank's evaluation of corporate debtors had (not surprisingly) proved unsatisfactory because of banks' conflict of interest in exposing weakness in major customers. The banks had, therefore, been requested to extend the review to include big five affiliates and to attempt to reconcile differences between creditor banks. The results of the second round review are expected by June 18-20.

The rationale for this process -- to eliminate the weaker corporates at an early stage, reduce uncertainty in the market, and thereby normalize the situation for resumption of bank lending -- appears very weak, and I noted that, in actuality, corporate restructuring would be a long

² Obviously at this stage this is market sensitive information.

- 3 -

process and that a one-off operation of this sort could not be expected to reduce uncertainty. More likely a highly publicized announcement that a large number of companies were insolvent would act to further undermine confidence and could have knock on effects that would adversely affect the stock market and financial institutions.³ The Chairman admitted that a more gradual and less public process would have been desirable, but the President had decided that this course was necessary to convince foreign investors that the authorities' restructuring efforts would be genuine and substantive. The Chairman agreed however that further consideration would be given to the nature of the press release announcing the results of the appraisal.

On the creation of debt workout units, the Chairman said that the individual banks were responding well and that the larger banks were forming alliances with international investment banks which had the necessary expertise for corporate restructuring. However, there was a need to resolve differences between creditors and a Central Arbitration Committee (CAC) would soon be established. The full powers of the Committee had still to be decided. The Chairman was aware of the tension between having a centralized body with large powers (which may be perceived as imposing a government solution) and having a decentralized process (under which individual banks may be too weak to negotiate and may have insufficient expertise). The CAC is presently seen as a compromise. Further Fund and the Bank, the CAC may be the point at which technical assistance can be most effectively directed.

4 Rollover for SMEs

The Chairman noted that the Government's efforts to persuade the banks to voluntarily roll over SME debt were not proving completely successful. The rollover ratio is currently estimated at 75 percent. He was considering bringing in a program of restructuring the debt which would not need to rely on moral suasion. I indicated that this would be an unfortunate move at a time when the government was trying to withdraw from direct interference with the banks and where the banks were being encouraged to build capacity for rational credit appraisal. The Chairman will give further consideration to the idea of enforcing the rollover of the SME debt.

³ Rumors of bankruptcy of parent companies are already affecting deposits at some merchant banks.

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Office Memorandum

To: Ms. Tseng

June 10, 1998

From: J. R. Dodsworth 

Subject: **Planned Demonstration**

A demonstration organized by the Pan-National Movement Group¹ against the Fund policies in Korea is expected to take place outside the MOFE tomorrow afternoon. The demonstration is expected to be orderly and not draw a large crowd. I have indicated to the organizers that I will be available in the MOFE office to discuss any issues they wish to raise and I expect to receive a letter from five or six representatives of the Group following the demonstration.

cc: Mr. Cook (Security Office)

98 JUN 10 AM 8:04

¹ The Pan-National Movement represents many civic groups including Korean Confederation of Trade Unions, Peoples Solidarity for Participatory Democracy, Lawyers for a Democratic Society, Catholic Human Rights Committee, Korea Research Institute for Worker's Human Rights and Justice and etc.

FAX TRANSMISSION

INTERNATIONAL MONETARY FUND

SEOUL, KOREA
TEL: (02) 759-4768
FAX: (02) 759-4769

cc: HN
KMM
SC
DJ5

To: Ms. Tseng

Date: June 10, 1998

Fax # (202) 623-4795

Pages: 1 including cover sheet.

From: J. R. Dodsworth, IMF Seoul

Subject: Number for the Chairman of the FSC

Dear Ms. Tseng,

The numbers of Mr. Hun-Jai Lcc, the chairman of the Financial Supervisory Commission are as below.

Tel. 3771-5001 Fax. 3771-6129

Best Regards,

98 JUN 10 AM 8:04

HW
cc: SC
TO REVIEW/HANDLE

cc: FOSS
KM
DS

INTERNATIONAL MONETARY FUND

June 9, 1998

To: APD

Subject: **Invitation from Institute for Corean-American Studies**

In the attached letter, the Institute for Corean-American Studies invites the MD to be a keynote speaker at its September 29 symposium in Philadelphia on "The Future of Asia."

The MD is unable to accept, but Mr. Fischer suggested that APD might be interested in speaking.

Please let me know and we will respond on behalf of the MD.

mpo

Marina Primorac, Public Affairs
(12-618J, ext. 34789)

98 JUN 10 AM 10: 15

Institute for Corean-American Studies, Inc.

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Blue Bell
PA 19422
U.S.A.

T:(610)277-9989
F:(610)277-3992
E:icas@dvol.com
kim@dvol.com

June 4, 1998

The Hon. MICHEL CAMDESSUS
Managing Director
The International Monetary Fund
Washington, D. C. 20431

ORIG: EXR
CC: MD
MR. FISCHER
MR. OUATTARA
MR. SUGISAKI
APD
MR. CROSS

Philadelphia [Fall] Symposium:
Future of Asia
9/29/1998, Tuesday
University of Pennsylvania

COMMUNICATIONS DIV.

98 JUN -9 PM 1:17

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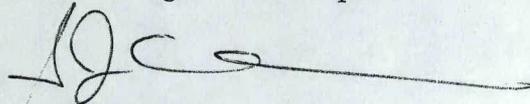
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Wilmington

Dear MD Camdessus:

We wish to follow up with you on the invitation, dated May 22, 1998, asking you to be a keynote speaker for Philadelphia [Fall] Symposium and ICAS Dinner which is slated to be held on September 29, 1998 at the University of Pennsylvania.

We sincerely hope that you will accept this non-partisan and educational platform. As appropriate, your serious consideration will be deeply appreciated.

Personal regards and respect,



Sang Joo Kim / signed
Sr. Fellow & Executive Vice President

encl: copy of the May 22 invitation letter (1 p)

Institute for Corean-American Studies, Inc.

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E icas@dvol.com
kim@dvol.com

May 22, 1998

ORIG & ENCL EXR
CC MD

The Hon MICHEL CAMDESSUS
Managing Director
The International Monetary Fund
Washington, D C 20431

MR FISCHER
MR OUATTARA
MR SUGISAKI
APD
MR CROSS

RECEIVED IMF
MAY 30 AM 8 53
COMMUNICATIONS UNIT

Philadelphia [Fall] Symposium
9/29/1998, Tuesday
University of Pennsylvania

Dear MD Camdessus

We would like to invite you to be a keynote speaker for Philadelphia [Fall] Symposium and ICAS Dinner which is slated to be held on September 29, 1998 at the University of Pennsylvania. The central theme of the conference will tentatively be "Future of Asia". Confirmed speakers to date include, Lawrence R Klein (*ICAS Distinguished Fellow*, Benjamin Franklin Professor Economics Emeritus, University of Pennsylvania, Nobel Laureate), Francis Fukuyama (*ICAS Fellow*, Omer L and Nancy Hirst Professor Public Policy, George Mason University), and Gerrit W Gong (Freeman Chair in China Studies, Director Asian Studies Program, Center for Strategic & International Studies). Invited speakers are Ezra F Vogel (*ICAS Distinguished Fellow*, Henry Ford II Professor Social Sciences, Director John K Fairbank Center for East Asian Research, Harvard University), Rawdon Dalrymple (*ICAS Distinguished Fellow*, former Australian Ambassador to Washington and to Tokyo, Chairman, Asean Focus Group, Sydney), Daniel K Inouye (U S Senator), and James T Laney (*ICAS Distinguished Fellow*, President Emeritus, Emory University, former U S Ambassador to South Korea). Presently we are in the process of inviting a respectable speaker from China, Japan and South Korea, respectively.

This invitation comes with full travel expenses and a moderate level of honorarium. We sincerely hope that you will accept the opportunity. Upon confirmation of your schedule with us, we will arrange logistical details. In the meantime, please feel free to call on us for inquiry and additional information.

Personal regards and respect,



Sang Joo Kim
Sr Fellow & Executive Vice President

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Institute for Korean-American Studies, Inc.

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presents

Philadelphia [Spring] Symposium

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E icas@dvool.com
kim@dvool.com

in collaboration with
Center for East Asian Studies, Center for Korean Studies, University of Pennsylvania
May 11, 1998, Monday, 8 30 AM - 5 15 PM

KOREA'S CHALLENGES AHEAD

economic issues International Relations issues, and Security issues

morning session (8 30 AM - 12 30 PM)

Annenberg School of Communications Room 110, University of Pennsylvania
3620 Walnut Street Philadelphia, PA

Arlington	8 30 AM	REGISTRATION
Atlanta	<u>moderator</u>	<i>Sang Joo Kim (ICAS Senior Fellow)</i>
Bangkok	8 50 AM	Welcome and Opening Address
Beijing		<i>Synja P Kim (ICAS Fellow, President, ICAS)</i>
Boston	9 00 AM	The Financial Crisis in South Korea Key Issues and Prospects
Brussels		<i>Sung Yeung Kwack (Professor of Economics, Howard University)</i>
Buenos Aires	9 30 AM	The IMF's Experience with South Korea 6 Months After, and More to Go
Cairo		<i>Robert Dekle (Economist on Korea, Japan, and Indonesia, IMF)</i>
College Park	10 00 AM	Foreign Investment Environment in South Korea
Columbia		<i>John J Lee (Senior Vice President, Scudder Kemper Investment/ The Korea Fund)</i>
Evanston	10 30 AM	break
Fairfax	10 45 AM	Rule of Law as a Fundamental Basis for Social Justice
Frankfurt		<i>The Hon Lynne Abraham (District Attorney, City of Philadelphia)</i>
Hanoi	11 15 AM	<u>Panel Discussion Critiques & Questions</u>
Hong Kong		<i>William B Brown (Deputy National Intelligence Officer for Economics National Intelligence Council), Jongmoo Jay Choi (Professor of Finance & International Business Temple Univ) Lilian Fischer (President Fischer Financial Architects), Bong Nam Jeon (Assoc Prof Economics Drexel Univ), Vinay Kansal (Senior Economist Asia Service WEFA Group) Synja P Kim (President, ICAS), Yoshuhisa Komori (Editor at Large The Sankei Shimbun Washington) Michael E Scullin (Partner Monteverde McAlee, Fitzpatrick Tanker & Hurd)</i>
Jakarta	12 30 PM	Lunch
Kuala Lumpur		HAN WOOL RESTAURANT
London		3608 Chestnut Street, Philadelphia, PA, 19104
Mexico City		T (215)382-6221
New Haven		
New York		
Philadelphia		
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Taipei		
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afternoon session (1 45 PM - 5 15 PM)

- moderator Sang Joo Kim (ICAS Senior Fellow)
- 1 45 PM **Has the East Asian Financial Crisis Bottomed-out?**
[keynote speech]
Lawrence R Klein (ICAS Distinguished Fellow, Benjamin Franklin
Professor Emeritus Economics, University of Pennsylvania,
Nobel Laureate)
- 2 15 PM **A Strategy for Peace in the Korean Peninsula**
Patrick M Cronin (Director of Research, U S Institute of Peace)
- 2 45 PM **A Perspective on the U S - South Korean Relations**
[keynote speech]
Richard L Walker (ICAS Distinguished Fellow, former U S
Ambassador to South Korea, James F Byrnes Professor Emeritus and
Ambassador-in-Residence, Walker Institute of International Studies,
University of South Carolina)
- 3 15 PM break
- 3 30 PM **U S Policy Towards North and South Korea**
[keynote speech]
Charles Kartman (Deputy Assistant Secretary, U S Department of
State)
- 4 00 PM Panel Discussion Critiques & Questions
Stephen Costello (Washington Representative Kim Dae Jung Peace
Foundation) G Cameron Hurst III (Professor of Japanese & Korean
Studies, University of Pennsylvania), Sang Joo Kim (Senior Fellow ICAS),
Whee Gook Kim (President East West Research Institute), Christopher
Powers (Asian Edition Editor Business Week) Keith W Rabin (President
KWR International) Trudy Rubin (Editorial Writer The Philadelphia
Inquirer), Ken Yates (Senior Vice President Jefferson Waterman International)
- 5 15 PM **Closing Remark**
Sang Joo Kim (ICAS Senior Fellow)
- 6 30 PM **ICAS Dinner** in honour of
The Hon Charles Kartman
The Hon Lawrence R Klein
The Hon Richard L Walker

Faculty Club, 3rd Floor (Connecticut - Delaware Rooms)

9 00 PM Adjourn

Acknowledgement of Contributors Asia Pacific Consulting, First
Commercial Bank of Philadelphia, Fischer Financial Architects, Korean
Chamber of Commerce and Industries U S A

Philadelphia [Fall] Symposium, September 29, 1998, Tuesday
Confirmed speakers to date Francis Fukuyama, Lawrence R Klein

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Philadelphia [Spring] Symposium

Korea's Challenges Ahead

University of Pennsylvania
Philadelphia, PA 19104

May 11, 1998
6 30 PM - 9 00 PM
Faculty Club

ICAS Dinner

In honour of

The Hon Charles Kartman

Deputy Assistant Secretary, U S Department of State

The Hon Lawrence R Klein

ICAS Distinguished Fellow

Benjamin Franklin Professor Emeritus, University of Pennsylvania
Nobel Laureate

The Hon Richard L Walker

ICAS Distinguished Fellow

James F Byrnes Professor Emeritus, Ambassador-in-Residence
The Richard L Walker Institute of International Studies
University of South Carolina
U S Ambassador (former) to South Korea

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Institute for Corean-American Studies, Inc.

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U S A

ICAS Dinner

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kim@dvol.com

May 11, 1998, 6 30 PM - 9 00 PM
Faculty Club
University of Pennsylvania
200 S 36th Street
Philadelphia, PA 19104

Arlington	moderator	Sang Joo Kim
Atlanta		
Bangkok		
Beijing	6 30 - 7 15 PM	Reception (Connecticut Room, 3rd Floor)
Boston		
Brussels	7 15 - 8 15 PM	Dinner (Delaware Room, 3rd Floor)
Buenos Aires		
Cairo		
College Park	8 15 -	Welcome Remark
Columbia		Synja P Kim (President, ICAS)
Evanston		
Fairfax		
Frankfurt	8 20 -	<u>Liberty Award</u>
Hanoi		
Hong Kong		The Hon Charles Kartman
Jakarta		The Hon Lawrence R Klein
Kuala Lumpur		The Hon Richard L Walker
London		
Mexico City		
New Haven	8 30 -	Korea's Vision for Global Citizenship in the New Millenium [dinner address]
New York		Young Man Kim (President, Korean Chamber of Commerce and Industries, U S A)
Philadelphia		
Prague		
Raleigh		
San Francisco		
Seoul	9 00 PM	Adjourn
Singapore		
Stanford		
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The ICAS Lectures

ICAS Seminar 10/20/1993
University of Pennsylvania, Philadelphia

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F (610)277-3992
E icas@dvool.com
kim@dvool.com

No 93-1020-SSH Seung Soo Han Korea and The Emerging World Order

ICAS Seminar 12/8/1994
Philadelphia Bar Association International Law Committee

No 94-1208-CRL Chang Ryul Lee How to Conduct Business in Korea

Chonju Symposium 9/29-9/30/1997
Riviera Hotel, Chonju, South Korea

No 97-929-IrA Irma Adelman The Secrets of Korea's Success
No 97-929-WBB Wilham B Brown China's Economic Relationship with
Korea and the Cholla Provinces The

No 97-929-MaC Mark Clifford Problems of State-owned Enterprises
At the Edge of the Precipice Can Korea
Make the Leap to a New Economy?

No 97-929-RaD Rawdon Dalrymple Looking Up to Korea Potential Roles as
seen from the South

No 97-929-EJF Edwin J Feulner Jr Korea in the World Today
[dinner address]

No 97-929-SPK Synja P Kim Korea's Challenges Ahead
[opening address]

No 97-929-JHP Jin Hyun Paik Multilateralism and the Korean Peninsula
No 97-929-SOP Sam Ock Park Role of Korea in the Organization of
Economic Space in Pacific-Rim

No 97-929-YCP Yung Chul Park Republic of Korea In Search of Its
Place in the World

No 97-929-NLP Nancy Lynn Patton U S -Korea Trade Policy and Promotion
[luncheon address]

No 97-929-HYR Hak Yong Rhee Korea's Future of Market Economy
No 97-929-GrR Greg Rushford Korea's Leadership and Pressures from
Washington

No 97-929-MES Michael E Scullin Korea's Globalization and International
Law

No 97-929-YSY Yong Soon Yim Globalization and the Security of Korea
The Role of the Four Major Powers in
Building a Security Community in Korea

No 97-929-JHY Jang Hee Yoo Korea's New Role in the Emerging
Multilateral Trade Order

No 97-929-JKY Jong Keun You Globalization Policy of Chollabuk-do
Province [welcome address]

No 97-930-MSB Michael S Brown Foreign Perspectives on the Korean
Economy [luncheon address]

No 97-930-SCC Su Chan Chae The Future of the Chaebol System

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The ICAS Lectures

Page Two (2)

No 97-930-JoC	Jonathan Clarke	Korea Inside or Outside of the U S - Japan-China Triangle?
No 97-930-BFF	Ben F Fairfax	Korea's OECD Membership and Meeting the Challenges of Globalization
No 97-930-LGF	L Gordon Flake	Reform and Regime Stability in North Korea The Role of South Korea
No 97-930-StH	Stefan Halper	Korea's Relationship with the U S Role of the News Media
No 97-930-SJK	Sang Joo Kim	Korea s Challenges Ahead [closing remark]
No 97-930-JBL	Jae Bong Lee	Unification of the Korean Peninsula through Cooperation in East Asia in the Borderless World
No 97-930-YSN	Yong Nam Song	Infrastructure and International Competitiveness
No 97-930-YYY	Yung Yong Yang	Structural Adjustment Policy for Korea's Transition to Economic Maturity
No 97-930-HkY	Hank H K Yim	Korea's New Foreign Direct Investment Policy and Chollabuk-do s Strategy

ICAS Seminar

West River Restaurant, Philadelphia

12/15/1997

No 97-1215-JMC	Jong Moo Jay Choi	Korea's Financial Crisis What Went Wrong, and What Are the Opportunities?
No 97-1215-SJK	Sang Joo Kim	A Historical Perspective Views from Washington and Tokyo Angle

Philadelphia [Winter] Symposium

University of Pennsylvania, Philadelphia

2/13/1998

No 98-213-ABD	Abel Beltran-del-Rio	Financial Crises and Economic Modernization The Mexican Experience
No 98-213-ArB	Ariel Bura	An Alternative Approach to Thwart Financial Crisis
No 98-213-NAD	Nelson A Diaz	Rule of Law as a Fundamental Basis for Reform
No 98-213-JPG	James P Gordon	The IMF and Korea
No 98-213-SSH	Selig S Harrison	North Korea, South Korea, and American Policy
No 98-213-SJK	Sang Joo Kim	Korea's Challenges Ahead [closing remark]
No 98-213-SPK	Synja P Kim	Korea's Challenges Ahead [opening address]
No 98-213-WGK	Whee Gook Kim	Evolution of Democracy and Economic Development A Case of South Korea
No 98-213-DoK	Donald Kirk	Chaebol Challenge and Change
No 98-213-LRK	Lawrence R Klein	The World Economic Outlook in the light of the Asian Crisis [keynote address]
No 98-213-DaM	David Malpass	IMF Policy and Asian Turmoil [not presented]

The ICAS Lectures

Page Three (3)

No 98-213-CLM	Catherine L Mann	Korea and the International Financial System What Went Wrong, What To Do about It, and What Role for the IMF?
No 98-213-DoO	Don Oberdorfer	Seoul-Washington Relationship How Strong, and Stable?
No 98-213-RoW	Robert Wade	The Asian Financial Crisis The High Debt Model and The Dangers of the IMF Strategy

ICAS Seminar

4/21/1998

University of Pennsylvania, Philadelphia

No 98-421-DKKa	Djun Kil Kim	A New Perspective on Korea Its National Identity and Culture
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Nul Bom Restaurant, Philadelphia

No 98-421-DKKb	Djun Kil Kim	Korea Its Past and Present
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Philadelphia [Spring] Symposium

5/11/1998

University of Pennsylvania, Philadelphia

No 98-511-LyA	Lynne Abraham	Rule of Law as a Fundamental Basis for Social Justice
No 98-511-PMC	Patrick M Cronin	A Strategy for Peace in Korean Peninsula
No 98-511-RoD	Robert Dekle	The IMF's Experience with South Korea 6 Months After, and More To Go
No 98-511-ChK	Charles Kartman	U S Foreign Policy Towards North and South Korea [keynote address]
No 98-511-SJK	Sang Joo Kim	Korea's Challenges Ahead [closing remark]
No 98-511-SPK	Synja P Kim	Korea s Challenges Ahead [opening address]
No 98-511-YMK	Young Man Kim	Korea's Vision for Global Citizenship in the New Millennium [ICAS Dinner address]
No 98-511-LRK	Lawrence R Klein	Has the East Asian Financial Crisis Bottomed-Out?[keynote address]
No 98-511-SYK	Sung Yeung Kwack	The Financial Crisis in South Korea Key Issues and Prospects
No 98-511-JJL	John J Lee	Foreign Investment Environment in South Korea
No 98-511-RLW	Richard L Walker	A Perspective on U S - South Korean Relations [keynote address]

Philadelphia [Fall] Symposium

9/29/1998

University of Pennsylvania, Philadelphia

No 98-929-FrF	Francis Fukuyama
No 98-929-LRK	Lawrence R, Klein

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INSTITUTE FOR COREAN-AMERICAN STUDIES, Inc (ICAS) was established in 1973. It is a non-partisan, private educational organization incorporated in the Commonwealth of Pennsylvania. ICAS is non-agent of any government and solely supported by voluntary contributions. Its purpose is to engage in wide range of international issues and affairs. ICAS promotes pertinent relations and conducts appropriate activities to enhance cooperations in association with peoples of mutual interests with a special emphasis on multilateral relations between the United States and Asia-Pacific rim nations. Its membership includes individuals from varied sectors embracing academic, corporate, cultural, international and other related fields. Presently, ICAS maintains a roster of thirty-one *Fellows* and cherishes a circle of friends of the Institute. They are,

	BUIRA Seira, Ariel	<i>Fellow ICAS</i> member of Board of Governors Banco de Mexico former IMF Executive Director, and former Director International Organizations and Agreements Mexico
	CAVALLO Domingo	<i>Fellow ICAS</i> member of National Congress and former Minister of Finance and Works Chairman of Currency Board Buenos Aires Argentina, Visiting Professor Krasnoff Professor of Global Business Studies New York University New York
	CHANDRAVITHUN Nikom.	<i>Fellow ICAS</i> Professor and Fellow Royal Institute and Judicial Council, Grand Palace Bangkok Thailand
	CLARKE Jonathan	<i>Fellow ICAS</i> President The American Journalism Foundation Washington, D C
	CI IFFORD, Mark L.	<i>Fellow ICAS</i> Chief Asian Correspondent Business Week, Hong Kong
	DALRYMPLE Rawdon	<i>Distinguished Fellow Director ICAS</i> Chairman, ASEAN Focus Group Sydney Australia former Australian Ambassador to the US and to Japan
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Atlanta	GUIRGUIS Nassef Nazmey	<i>Fellow ICAS</i> Chairman, Cairo Stock Exchange Cairo Egypt
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Buenos Aires	KLEIN Lawrence R.	<i>Distinguished Fellow ICAS</i> Benjamin Franklin Professor of Economics Emeritus University of Pennsylvania, Philadelphia, Nobel Laureate
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Columbia	LEE Nahm Wook	<i>Fellow ICAS</i> President Stanford Software Sunnyvale California
Evanston	LEE Yuan-Tseh	<i>Distinguished Fellow ICAS</i> , President Academia Sinica, Taipei, Republic of China Nobel Laureate
Fairfax	LILLEY James R.	<i>Distinguished Fellow ICAS</i> Professor of Public Affairs and Director of the Institute for Global Chinese Affairs Univ Maryland College Park, former U.S. Ambassador to China and to Korea
Frankfurt	LO Fu Chen	<i>Fellow, ICAS</i> Professor and Deputy Director Institute of Advanced Studies The United Nations University Tokyo Japan
Hanoi	MAIER, Manfred	<i>Fellow, Director ICAS</i> , Professor, University of Vienna, Vienna, Austria
Hong Kong	O'BRIEN Timothy J	<i>Fellow Director ICAS</i> Partner Coudert Brothers New York, Hong Kong
Jakarta	OH, Tae Hee	<i>Fellow Director ICAS</i> Professor Yale University, New Haven, Connecticut
Kuala Lumpur	PANG, Eng Fong	<i>Fellow ICAS</i> Singapore Ambassador to Belgium and European Unions Brussels
London	PARK, Sung In	<i>Fellow ICAS</i> Vice President, Office of the Executive Staff Chairman's Office Samsung Group Seoul, President Korea Skating Union
Mexico City	PATTON Nancy Lynn	<i>Fellow ICAS</i> former Deputy Assistant Secretary for Asia and the Pacific U.S. Department of Commerce, Washington, D C.
New Haven	SHIN, Sun Kyun	<i>Fellow ICAS</i> President and CEO MAC Group Wilmington, DE President Sung Il Printing America, San Francisco California
New York	SINGLETON Kenneth J	<i>Fellow Director ICAS</i> C O G Miller Distinguished Professor of Finance Stanford University Stanford California
Philadelphia	SUHR, Paul	<i>Fellow Director ICAS</i> Senior Partner Suhr & Associates Raleigh, N C
Prague	VOGEL Ezra F	<i>Distinguished Fellow ICAS</i> , Henry Ford II Professor of the Social Sciences and Director John K. Fairbank Center for East Asian Research, Harvard University, Boston
Raleigh	WALKER, Richard L.	<i>Distinguished Fellow ICAS</i> James F. Byrnes Professor Emeritus and Ambassador-in Residence Institute of International Studies University of South Carolina, Columbia, S C former U.S. Ambassador to Korea
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Office Memorandum

To The Acting Managing Director
The Deputy Managing Directors

June 9, 1998

From Wanda Tseng 

Subject **Korea Letter from Mr Neiss to Minister of Finance and Economy**

The Korean authorities have taken measures recently to further liberalize the capital account, including short-term capital movements, ahead of the schedule of the Letter of Intent. They are also in the process of revising the Foreign Exchange Act to liberalize foreign exchange transactions in support of capital account liberalization.

For your information, we are intending to send the attached letter, from Mr Neiss to the Minister of Finance and Economy, by c o b tomorrow

The letter notes that given the decision to accelerate capital account liberalization, there is also a need to move as fast as possible on strengthening the prudential regulations on short-term foreign borrowing and foreign exchange exposures as well as monitoring and reporting requirements. The strengthening of prudential regulations and monitoring in the Letter of Intent were timed to move in line with capital account liberalization, but also took account of the time needed to set up monitoring systems and for banks to adjust their portfolios. Nevertheless, given the authorities' decision to accelerate capital account liberalization, we are asking again about the possibility of moving faster on the prudential regulations. These issues will be taken up by the review mission in early July, the letter is intended to prepare the groundwork for the discussions.

The letter was reviewed by Messrs Ferran (PDR) and Gutian (RES)

Attachment

cc The Managing Director (o/r)
Mr Russo
LEG, MAE, PDR
Mr Cross

Contributors

S Coorey
G Moser



INTERNATIONAL MONETARY FUND
WASHINGTON D C 20431

CABLE ADDRESS
INTERFUND

June 9, 1998

Mr Lee Kyu-Sung
Minister of Finance and Economy
Ministry of Finance and Economy
Government Building II
Kwacheon, Kyunggi Do, 171-11
Republic of Korea

Dear Mr Minister

The government has taken several important measures recently to further liberalize the capital account, bringing forward some measures contained in the Letter of Intent of May 2, 1998. We welcome these measures, particularly those related to the liberalization of foreign direct investment and of restrictions on equity ownership in Korean companies. At the same time, and as the government recognizes, it would be important that the removal of restrictions on short-term capital movements be accompanied by adequate safeguards, particularly strengthened prudential regulations, consolidated supervision, and improved monitoring.

More specifically, restrictions on foreign investment in domestic money market instruments issued by financial institutions (CDS and RPs) and corporate borrowing of 1-3 years maturities are being liberalized ahead of the schedule in the Letter of Intent. These liberalization measures were timed in the Letter of Intent to take into account the implementation of a number of prudential regulations, particularly those related to short-term foreign borrowing and foreign exchange exposures, and with the start of consolidated supervision (January 1, 1999). Also, the Letter of Intent envisaged the submission of necessary legislation to ensure compliance with reporting on external liabilities of the corporate sector by October 31, 1998.

On a related subject, we thank you for the opportunity to review the draft paper on revisions to the Foreign Exchange Act. We will communicate, through Mr Dodsworth, more detailed comments on these revisions directly to your staff. As a general point, we welcome the further liberalization of the capital account, particularly the move from a positive list to a negative list system, and the proposed streamlining of foreign exchange regulations. Again, the accelerated liberalization of short-term capital flows envisaged in the revisions to the Foreign Exchange Act highlights the need for safeguards in terms of prudential regulations, supervision, and monitoring.

Thus, in view of the acceleration of liberalization on capital account, there is also a need to move faster on the prudential regulations on short-term foreign borrowing and foreign exchange exposures and on the monitoring and reporting requirements set out in the Letter of Intent. We would urge your consideration of accelerating these measures from those set out in the Letter of Intent (shown in the attachment). I look forward to hearing from you on the possibility of accelerating these measures. The July review mission will also discuss this matter further.

A copy of this letter is also being sent to Mr. Lee Hun Jae at the Financial Supervisory Commission.

With best regards,

Yours sincerely,

Hubert Neiss
Director
Asia and Pacific Department

Prudential Regulations and Data Monitoring Measures

(Timing of implementation shown in the May 2, 1998 Letter of Intent)

- Measures on strengthening compliance with existing guidelines for commercial banks to limit maturity mismatches in foreign exchange and the announcement of similar guidelines for merchant banks (August 1, 1998)
- The full phase in of prudential guidelines to limit maturity mismatches in foreign exchange for merchant banks (December 31, 1999)
- The announcement (August 15, 1998) and implementation (as of January 1, 1999) of additional regulations for commercial and merchant banks. The additional regulations to include introduction of an internal liquidity control system based on a maturity ladder approach, agreement with the Financial Supervisory Commission (FSC) on allowable maturity mismatches, the monthly monitoring of implementation by the FSC, and the public disclosure of statistics on foreign currency liquidity by bank
- With respect to foreign exchange exposure limits, the implementation of the supervision of observance to be undertaken by the FSC, the replacement of separate limits on combined spot and forward positions, the incorporation of cross-currency positions in the measurement of exposures, and the introduction of consolidated limits for banks, including their offshore branches (November 15, 1998)
- The introduction of improvements to the reporting of off-balance sheet foreign currency denominated exposure of financial institutions and the submission of necessary legislation to ensure compliance with reporting on external liabilities of the corporate sector (October 31, 1998)



Office Memorandum

98 JUN -9 11 4 29

RN
cc: ROSS
KUM
SC
DVS

To Ms Tseng

June 9, 1998

From Manuel Guitian *MG*

Subject **Korea—Assistance to Financial Supervisory Commission on Bank Restructuring**

Thank you for your memorandum of June 5 on the above. We certainly share your views as to the importance of supporting the work of Korea's Financial Supervisory Commission (FSC). I have the following comments on the specific points you raise:

1 The authorities' request for the Fund to recommend an expert to the FSC to join the FSC's Bank Appraisal Committee raises some concerns. First, the conditions set by the authorities (in particular, the bilingual English/Korean requirement, and the imminence of the assignment) make it difficult to find a suitable candidate. Second, the expertise required (commercial banking) is not of the type MAE can provide, directly or through our roster of experts. Third, we have to avoid the risk of the Fund becoming involved in deciding on the fate of specific banks or enterprises. Focusing that involvement on the integrity of the evaluation process, as we (and the Bank) did in the case of the merchant banks, seems more appropriate.

This said, though, to be of assistance to the authorities, we have contacted staff from the Federal Reserve Bank of New York, who indicated they would try to identify a suitable candidate, probably from the banking community. Once we hear from them, we will advise the FSC so that it can make the necessary arrangements directly with the candidate. Actually, assistance in this area is the World Bank's responsibility, so we would be interested in hearing if they are now in a position to assist (as you know, last week they indicated to Mr. Balño that they were not).

2 Yesterday Mr. Ze'ev Abeles, retiring Senior Director and Superintendent of Banks of the Bank of Israel, has confirmed his acceptance of our offer to take the assignment of resident advisor in banking supervision and regulation in Seoul. I have already written to the Chairman of the FSC, requesting his approval for the candidacy. We will seek to place Mr. Abeles in Seoul as soon as possible this summer. However, this cannot be done this month. In the meantime, we will be prepared to handle specific requests for assistance from the authorities in any way that is effective and practical for both sides (e.g., by sending them materials, commenting on drafts, or if necessary arranging for a short-term expert visit).

3 As regards the point in the LOI on issuance of minimum supervisory standards on banks' problem-loan workout units, we are coordinating our views on this matter with the World Bank, and we expect to be able to respond to you shortly

cc Mr Knight
Mr Balño
Mr Downes
Mr Dodsworth
Mr Hayward



INTERNATIONAL MONETARY FUND
WASHINGTON, D. C. 20431

W. Tsang
cc: ~~HW~~
JUS

98 JUN -9 PM 4: 29

June 8, 1998

CABLE ADDRESS
INTERFUND

Mr. Hun-Jai Lee
Chairman
Financial Supervisory Commission
27 Yoido-Dong, Youngdeungpo-Gu
Seoul 150-600
Korea

Dear Mr. Lee:

I am pleased to write to you with regard to your request for the appointment of a resident advisor in banking supervision and regulation.

In this connection, I am happy to inform you that we have identified an excellent candidate, Mr. Ze'ev Abeles, who is retiring as Senior Director and Superintendent of Banks at the Bank of Israel. Mr. Abeles has had a long career at the Bank of Israel in the area of banking supervision and regulation. We believe his background is very well suited for the assignment you have requested. Mr. Abeles's curriculum vitae is attached for your consideration.

I would be grateful if you would let me know at your earliest convenience whether this candidate is acceptable to you, in which case we will continue the process of recruitment. Mr. Abeles would be able to begin his assignment in the later part of July, for a period of one year.

Sincerely yours,

Manuel Guitián
Director
Monetary and Exchange Affairs Department

Attachment

CURRICULUM VITAE

Ze'ev Abeles
25 Mozkin st
Ra'anana, 43343
ISRAEL

EDUCATION

1975 - Licensed - Certified Public Accountant
1973 - BA Economics - Hebrew University Jerusalem
1972 - BA Accounting - Tel Aviv University

EXPERIENCE

Since September 1992 - Bank of Israel Senior Director and Superintendent of Banks
1989 - 1992 - Deputy Superintendent of Banks
1987 - 1989 - Assistant Superintendent of Banks
1985 - 1987 - CEO - North American Bank (The Bank collapsed in August 1985 and I was appointed by the governor of the Bank of Israel to manage the Bank, my task was to stabilize the Bank to evaluate it and to execute its sale. The bank was sold on October 1987 at which time I finished my role)
1976 - 1980 - Lecturer (part time) - Accounting - Bar Ilan University, Ramat-Gan
1970 - 1985 - Bank of Israel
- Senior Examiner
- Head of Foreign exchange and International activities examination unit
- Head of Credit and Collateral examination unit
1967-1970 - Ministry of Finance - Inspector at the Income tax office



INTERNATIONAL MONETARY FUND
 WASHINGTON, D.C. 20431
ASIA AND PACIFIC DEPARTMENT

cc.
 LEG
 MAE
 PDR

Fax # (202) 623-4432

Tel # (202) 623-7602

MSG. NO.	DATE June 9, 1998	PAGE 1 OF 9
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TO Mr. John Dodsworth
 Seoul, Korea
 011-82-2-792-1651

Could you please give the attached to Mr. Kwon. Also, could you please give us the fax number for the Chairman of the FSC.

Many thanks,

Attachment

FROM Wanda Tseng
 APD/AI

ROOM NO. 4-320	EXTENSION (202) 623-7182	ACCOUNT CODE
AUTHORIZED BY Wanda Tseng		SIGNATURE



INTERNATIONAL MONETARY FUND
WASHINGTON, D. C. 20431

CABLE ADDRESS
INTERFUND

June 9, 1998

Mr. T. K. Kwon
Director
Foreign Capital Division
Ministry of Finance and Economy
Seoul, Korea

Dear Mr. Kwon:

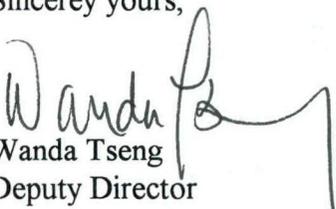
Thank you for giving us the opportunity to review the proposed revision of the Foreign Exchange Control Act. We welcome the government's intentions to streamline the legal and regulatory framework for foreign investment in Korea and to take further steps toward liberalizing foreign exchange and capital flows. At the same time, liberalization of the capital account needs to be accompanied by adequate safeguards, in terms of strengthened prudential regulations and supervision and improved monitoring. We will be discussing these issues further during our next review mission in July.

Attached please find our comments on the revisions to the Foreign Exchange Control Act. In addition, attached is a questionnaire on current account transactions provided by the IMF's Legal Department. The questionnaire is to clarify the status of some current account transactions that were thought to have been liberalized when Korea accepted the obligations of Article VIII. I would appreciate your response to this questionnaire. Alternatively, a staff from the IMF's Legal Department could either call you (or go on a brief mission to Seoul) to clarify these matters if needed.

Thank you.

Best regards.

Sincerely yours,


Wanda Tseng
Deputy Director
Asia and Pacific Department

Attachments

25% Cotton
50% Recycled

Comments on Revision of Foreign Exchange Act from IMF Staff

Relationship with Article VIII

1 A number of proposed liberalizations were thought to have been removed when Korea accepted the obligations of Article VIII. The revised Act should make clear that there are no contradictions between new liberalizations and existing Article VIII obligations. Among the issues that need to be clarified in this context are (i) limits for certain invisible transactions (when Korea accepted the obligations of Article VIII, it was represented that any limits were "indicative," EBD/88/338 (11/21/88)), (ii) licensing for payment of certain services, (iii) transfers from nonresident accounts of proceeds of current international transactions, including interest, (iv) other issues including restrictions on short-term financing and deferred payment for imports. In this connection, we would appreciate receiving answers to the attached questionnaire which seeks to clarify these issues.

2 The twenty items on the negative list should be identified in the Act. 3

Improvements in the Reporting Framework

3 The Act should address needed improvements in the reporting framework to ensure that the central bank can collect adequate and timely information equally from banks, corporations and individuals. In this context, for example, the commitment to submit legislation on reporting by corporations, where a coverage of the current law is acknowledged to be inadequate, would be more important than the reference to a new computer network.

4 The reference to the computer network suggests the setting up of an automatic real time basis system. This seems overly ambitious, and we would like to note that in most other countries reporting is based on (i) the settlement approach, in which banks report aggregated transactions on a settlement basis, and overseas transactions are reported by the persons executing the transactions, (ii) the survey approach, in which the authorities conduct surveys, or (iii) a combination of the two approaches.

Clarification of Terms

5 The Act should appropriately distinguish between restrictions on "transfers of payments and receipts" and on "underlying transactions." Wherever possible, the Act should be explicit on whether the proposed revision refers to the underlying transactions or the transfers of funds that are associated with the transactions.

6 In the Act, language should be clarified, for example "resident corporations" instead "business firms," and "nonresidents" instead of "foreigners."

Information on Existing Restrictions

7 The note introducing the Act could include a summary of restrictions currently in place on both current and capital account transactions to focus the discussion on what needs to be done in the period ahead to move Korea closer to OECD requirements

8 A more detailed description of the measures and a timetable for removing the remaining restrictions (ownership, sectoral, etc) on inward direct investment would be desirable

Development of the Foreign Exchange Market

9 To keep the focus on foreign exchange transactions in the Act, the discussion of institutional aspects of the development of the exchange market could be dropped from the introductory note and taken up separately

Other Issues

10 Concerning two other measures which have been announced—the lifting of the 5 percent individual limit on foreign investments in futures and options trading, and allowing foreigners to borrow from local securities houses for investment in local securities market, we would appreciate knowing the rationale underlying these measures, and whether any limits will continue to apply

Detailed Comments

- **Page 2, paragraph 1** Note that capital account liberalization could bring in substantial capital, but might also cause large outflows, depending on the policy environment and the strength of the domestic financial system
- **Page 2, paragraph 3** Is the timetable for liberalization consistent with other reforms, particularly in the financial sector?
- **Page 3, paragraph 1** It is unclear whether the term “foreign exchange transactions” refers to underlying transactions of foreign direct investment and other investments or transfers of funds arising from these transactions Does this wording mean that foreigners are now not entitled to use for investment purposes won legitimately earned by them? Does that mean that the only way they can use won is to exchange it into convertible currency and then to invest it? If the answer is yes, the text of the Korean page in the Annual Report of Exchange Arrangements and Exchange Restrictions is incorrect, since there seems to be no restriction on these items Also, the OECD Code mentions the so-called “free won” accounts, which could be used freely in 1996

- **Page 3, paragraph 2** Clarify whether “the lift of the restrictions of foreign investment in short-term financial instruments” will be limited only to CDS and RPs, or whether it will also include other short-term government and corporate instruments (such as commercial papers, T-bills, etc) The terms “foreign investment” and “foreigners’ investment” should be replaced by “investment by nonresidents”
- **Page 4, paragraph 2** The term “domestic business firms” should be replaced by “resident firms ”
- **Page 5, paragraph 2** It is not necessary to maintain current account restrictions because of anti crime and anti money laundering considerations Alternative solutions include anti money-laundering laws, which oblige all institutions handling cash to report suspicious transactions or just to record all transactions above certain limits, or—if the matter cannot be solved in any other way—to have a prior reporting system for some transactions
- **Page 5, last paragraph** As indicated above, there are questions of consistency between the proposals and Article VIII status, as well as with Korea’s reservations to the OECD Codes
- **Page 6, last paragraph** A footnote would be helpful describing the remaining 21 types of transactions subject to restrictions
- **Page 7** Need to clarify whether resident firms will be allowed to invest in overseas commercial banks and investment banks
- **Page 7, paragraph 3** We assume that the extension of loans by financial institutions, including securities and insurance companies, as well as pension funds will be governed by prudential regulations
- **Page 7, paragraphs 4-6** These controls are not reflected in the reservations to the OECD Code of Liberalization of Capital Movements
- **Page 8, paragraph 1 and page 11, paragraph 2** We presume that the complete liberalization of foreign exchange business would only mean participation in the foreign exchange market and the opening of exchange bureaus, but not other banking business, which justifiably requires banking licence (lending as main business, keeping accounts, etc) The text is misleading, since it states “ the foreign exchange businesses will be allowed to all juridical persons and natural persons ”
- **Page 9, paragraph 2** How do the authorities envisage to prohibit until 1999 (when this item is planned to be liberalized) that foreigners abroad do not trade in won or issue won-denominated securities abroad?

- **Page 9, paragraph 3** The reference to international peace and public disorder is vague
- **Page 9 bottom and page 10 top** These transactions were also not listed as reservations to the OECD Code, except travel expenses
- **Page 10** A footnote would be helpful describing what will be the remaining six types of transactions subject to restrictions
- **Page 10, fifth full paragraph** This liberalization measure raises the question whether restrictions apply to enterprises selling their debts accrued from borrowing or to buying such debts. If the answer is no, then it could be an easy method to overcome any restriction imposed on short-term borrowing (if the macroeconomic incentives exist). Consequently, even now there might not have a need for this restriction to remain in place

Questionnaire
Korean Exchange System

June 9, 1998

1 “Restricted” transactions to be liberalized The paper from the Korean Institute of Finance (the “paper”) refers to 20 transactions for which payments and transfers are currently “restricted” (which will be reduced to five) We understand from Mr Yang’s letter, that these payments and transfers are largely those that require prior approval¹ and that the liberalization plan involves removing the need for the prior approval We would appreciate clarification of (a) which transactions require approval, and (b) the approval process²

(a)(i) The letter and the regulations (Article 2–24) refer to “admitted” transactions Is an “admitted” transaction one that is permitted even without prior approval and where are these listed? Are these the same as those permitted under the External Trade Act (could we get a copy of that Act)?

(ii) Could we please get a further explanation of the following items on the list from Mr Yang’s letter (1) Items no (7) and (8) payments relating to “guarantees” (do they refer to financial guarantees by banks?), (2) Item no 10 payments of expenses for negotiations an confidential use, (3) Item no 14 “payment without having any relation to creation of credit, etc between the said resident and nonresident ”

(iii) **Services** The paper refers to “individual licenses” for payments for consulting services, commissions for trade brokerage and research and development services (p 5) Payment for these transactions are identified in Mr Yang’s letter as requiring prior approval (items (3), (4), and (9)) and the regulations require prior approval of the Minister of Finance and Economy for payment of “consulting service fees related to financing and insurance Business and proxy exercise of management” (Article 6–15–4(1)) Is this approval requirement the same as the licensing requirement set out on page 5 of the paper? Under what circumstances are payment (or licenses) for services approved?

¹Letter from Dohnson Yang, Deputy Director, Foreign Capital Management Division, International Finance Bureau, Ministry of Finance and Economy, to Mr J Dodsworth, June 1, 1998

²Under the regulations, certain current transactions are specified for prior approval either by (a) the head of a trading foreign exchange bank, (b) the head of the *designated* trading foreign exchange bank, (c) the Governor of the Central Bank, or (d) the Minister of Finance and Economy Covered transactions appear to include, for example, current transactions above certain limits and certain specific transactions such as interest, dividend and rental income, consulting service fees related to financing and insurance business and proxy exercise of management, and payment related to the purchase and sale of goods not prescribed in the External Trade Act

(b) Please answer the following questions concerning the approval process

(i) Under the regulations, certain transactions must be approved by the head of a *designated* trading foreign exchange bank—what is a *designated* trading foreign exchange bank? Will there continue to be a distinction between such banks and other foreign exchange banks after the proposed liberalization?

(ii) In general (1) Is each entity responsible for approval *required* by law to approve requests for a payment once the person making the request has established that the payment is for a *bona fide* current international transaction (e.g., not for transferring capital)? (2) Are such approvals routinely granted in practice? (3) How long does processing the request take for each kind of approval? (4) Are these rules the same as those on “procedure for permission, etc.” in Article 7–3 of the regulation?

(iii) Specific questions on **travel expenses** (1) What is the purpose of the “declaration” that must be made even for payments within the limits (Article 6–22)? (2) It appears that “additional” expenses above the specified limits may be made by credit card (Article 6–21), is this the only means for payment of additional amounts? For example, when residents can prove that transactions above the limit are *bona fide* payments associated with travel), can the resident seek approval to purchase of foreign exchange or make a payment by transferring the additional amount through the banking system? (3) Do similar rules apply for travel abroad for extended stay such as for study (e.g., an “overseas sojourner” as defined in Article 6–17)?

(iv) Certain aspects of **emigration expenses** could involve *current* payments, such as payments to shipping companies, rather than the transfer of capital out of Korea. Are all such *current* payments approved irrespective of the limits stated in Item 17 or the list in Mr Yang’s letter?

(v) The list in Mr Yang’s letter contains two categories (items nos. 12 and 13) on transfers for “**profit, interest, dividend, allotment money, etc.**”, depending on whether they relate to transactions that are specified in Article 21(1) of the foreign exchange law, which require prior approval (1) For transactions that are specified in Article 21(1), are transactions for which prior approval has not been obtained lawful in Korea? Are transfers of profit, interest, etc., permitted even if prior approval for the transaction had not been obtained? (2) Are the transactions that are not listed in Article 21(1) lawful transactions in Korea? On what basis are transfers of profit, interest, etc., relating to these transactions approved?

2 Transfers by Nonresidents

(a) What is the difference between nonresident won currency accounts and nonresident free-won accounts?

(b) (1) Are nonresidents freely permitted to **credit these accounts** with proceeds of current international transactions. Nonresident *won currency accounts* may be credited with “domestic currency domestically acquired by nonresidents” (Article 10-34(1)) and these amounts may be used to buy foreign exchange (Article 10-35(2)). The articles on *nonresident free won* accounts (Articles 10-35-2 through 10-35-4) specifically refer to the “proceeds of current international transactions,” is there a difference in meaning intended between the descriptions of the two accounts? (2) May such amounts be transferred? Mr Yang’s letter refers payment of interest or dividend income to *won currency accounts*, may such income also be credited to *free won* accounts?

(c) Are nonresidents freely permitted to **transfer abroad the interest earned on both** the nonresident accounts transferrable abroad? Interest on *won currency accounts* appears to be transferable because it is listed in Article 2-45 among permissible sales of foreign exchange and it is listed among the circumstance for “disposal for buying foreign exchange” (Article 10-35(2)(c)). However, there is no provision authorizing transfer interest from *free won* accounts.

(d) What is meant by the payment limit of nonresidents noted in the regulations as “recognized foreign means of payment acquired or held”? (Article 6-5(2))

3 Deferred Payment Several provisions in Chapter 3 of the regulations require permission from the Governor of the Bank of Korea for payments that follow the import or the provision of a service beyond a specified period of time (e.g., Articles 7-12, 7-15, 7-24 through 7-32)

(i) Do residents require permission in order to enter into a contract for the import of goods or services that provides for deferred payment, or is permission only required to make the *payments* associated with such contracts? In what circumstances would permission to make such payments be refused?

(ii) Are there separate restrictions on short-term financing for imports?

4 Exchange Rate The paper refers to the daily quotations under the Market Average Exchange Rate System, which it states “do not reflect the most recent market conditions” (p. 9). Is this quoted rate used for any current international transactions (e.g., governmental transactions)?



Office Memorandum

cc SC
TO REVIEW/HANDLE

cc DS Files
FOSS w/o att

To Mr Ferran
Ms Tseng ✓
Mr Downes
Mr Laurens

June 8, 1998

From Tomas J T Balño 

Subject Korea--Mr Nordman's Draft Report

Attached for your comments is a draft report prepared by Mr Tom Nordman (consultant, from the Bank of Finland) who recently visited Seoul to discuss reserve management techniques and issues regarding the local foreign exchange market I would be grateful to receive any comments you might have by c o b Wednesday, June 17

Attachment

cc Mr Johnson
Mr Hayward
Mr Moser
Mr Ubide

98 JUN -9 PM 2 16

Confidential

International Monetary Fund
Monetary and Exchange Affairs Department

Bank of Korea:
Foreign Exchange Market
And
Management of Foreign Exchange Reserves

Prepared by Tom Nordman

June 1998

A INTRODUCTION

At the invitation of the Ministry of Finance and Economy, an MAE consultant, Tom Nordman from the Bank of Finland, visited Seoul between May 24-30, 1998. The purpose of the visit was to review the functioning of the foreign exchange market in Korea and the foreign exchange operations and reserve management of the Bank of Korea. During this week, Mr. Nordman had extensive discussions with officials of the Bank of Korea, including Mr. Hyunchul Shin, Director, International Department, and several of his staff. Mr. Nordman also conducted an informal seminar on reserve management practices at European central banks.

Mr. Nordman also had meetings with representatives of six banks and two enterprises. These discussions provided him with a broad view of how the foreign exchange market functions in Korea.

Korean officials as well as representatives of banks and enterprises were very forthcoming and willing to share their views and concerns in a very constructive manner.

B REVIEW OF CURRENT ARRANGEMENTS

1 Korea's foreign exchange market

Structure of the market

The relevant spot market in Seoul is WON/USD. Nominally, there is also a WON/JPY market. The latter was introduced in October 1996 at the insistence of the Ministry of Finance and Economy (MoF) and against the advice of the Bank of Korea (BoK). MoF officials thought that as the JPY is an important regional currency, there should be a market in Korea for the Yen as well. The market has not taken off, which is not surprising, since international markets are very effective and economical at transforming other currencies into dollars and back. It is therefore international practice for most interbank foreign exchange markets between the local currency and a foreign currency to be against the dollar. Market participants' needs to buy and sell other currencies against the local currency are transformed into dollars in the international markets and then traded as a dollar transaction in the local market. Any direct trading between a local currency and other currencies than the dollar is always at the expense of turnover in the local currency vs. USD market.

Predictably, MoF's initiative was not successful, and there is practically no direct WON/JPY turnover. This incident probably speaks much about the nature of the BoK-MoF relationship. For all practical purposes, only the WON/USD market matters. MoF often does not heed the advice of BoK, which is much closer to the market and better acquainted with market practice.

There are some 100 banks in the foreign exchange market. The core is made up of 15 commercial banks. In addition, there are local banks, specialized banks, development institutions, merchant banks, and a large number of foreign bank branches. Currently

banks need a separate license (virtually all banks have one) to operate in the foreign exchange market. However, legal amendments will soon give all banks with a banking license the right to deal also in foreign exchange, the only condition then being that they have in place the appropriate internal operational control structures.

Some of the market participants have peculiar characteristics. KEXIM Bank is basically only a seller in the market. It usually sells directly to foreign banks due to their role in providing financing for KEXIM. KEXIM does thus not operate through the brokerage system discussed below. BoK has indicated to KEXIM that it should not be a buyer in the market. KEXIM would want a forward market to develop since forwards would make its hedging operations simpler.

At KDB, middle management is seriously constrained by senior management from engaging in active risk management. Forward transactions need the approval of the CEO, which means they are never done.

SK Corporation, with 40 % of the market the largest importer and distributor of oil products. SK is the biggest single buyer of foreign exchange in the market. Annual volume is \$5 billion. SK can raise its prices to cover foreign exchange losses on its import bill, but not to cover the increased cost of loan servicing. Long-term foreign debt amounts to \$39 billion. Importers and distributors use a price formula that was used when prices were regulated. In principle prices are now free, but importers continue to use the same formula voluntarily. So far there are no foreign market participants, but that is expected to change, at which time price competition would also emerge. CEO approval is needed for use of forwards.

Trading in the market

Up to 90 % of interbank transactions are traded over the KFTC (Korea Financial Telecommunications and Clearing), a partly electronic brokerage sponsored jointly by BoK and a group of banks. KFTC is a nonprofit organization to which BoK and a number of banks provided initial funding. Brokerage fees are payable annually to cover 80 % of operating costs (BoK pays 20 %) so that half is of each institution's fee is based on turnover volume, and the other half on the number of transactions. Commissions are thus based on usage. The cost per transaction is 10 won, i.e. virtually nothing.

To place a bid or offer with KFTC, banks call KFTC over the phone and place their order. Bids and offers are displayed on participants' screens ranked according to price and time. When a bank wants to deal at a price it sees on the screen, it again calls the KFTC, who informs the institution who had placed the order. If the two parties are prepared to deal with each other, settlement takes place directly between the two parties in the usual manner. Apparently it is also possible to block bids and offers from banks with whom users do not want to deal, although it is not quite clear how this works technically. KFTC officials only speak Korean and it was not possible to set up a meeting with them.

When the currency crisis broke in December 1997, there were instances where the bid to buy was higher than the offer to sell. These bids were from merchant banks trying

to meet their maturing obligations in foreign exchange. At this time, most other banks were unwilling to trade with the merchant banks.

BoK also has a screen for the KFTC brokerage system. KFTC quotations are also shown on Reuters with a delay of only a few seconds. Major corporate customers, who all have Reuters, are therefore very well informed of the current rate level in the market.

There are no other brokerages in the market, but BoK and MoF have discussed the possibility of introducing additional brokerages in the market. Since the initiative is for a private brokerage, it is not clear why BoK and MoF need to be involved. The motivation for the initiative is not obvious. So far MoF has discouraged other potential (foreign) brokers from applying for this activity which requires a MoF license. It may be difficult for other brokers to become competitive, given the narrow spreads in the market, typically only 1 WON. However, some market participants complained that the current KFTC system could be a bottleneck if market volumes are to increase significantly. Since orders are placed by phone, at peak activity it is already now sometimes difficult to get through to KFTC. This could make the market more volatile, and it certainly makes market participants more nervous.

The brokerage market over KFTC is active between 9:30-12 and 1:30-4:30. The reason for the lunch break is not clear.

There are also some direct bilateral interbank transactions between banks, but no banks are actually market makers in the sense of quoting two-way prices to other banks. There is no formal code of conduct regulating interbank dealing or settlements of transactions over KFTC either, for that matter. While there is a Forex Club in Seoul, it apparently has more of a social than a professional role, although it reportedly recently has been more active in arranging training etc. A group of foreign banks have attempted to introduce bilateral market making and direct dealing between themselves, but the experiment foundered after a few months since direct dealing could not compete with the very narrow spreads in trading over KFTC.

The standard spread in customer transactions is 2%, but this is negotiable. Large corporate customers tend to get significantly better rates.

There is also a forward market in Korea, but its activity is limited by the fact that there is a separate limit on spot positions in addition to a limit on the overall net position. Banks also engage in NDF (Non Deliverable Forwards), which are traded actively offshore, in particular in Hong Kong and Singapore. Foreign banks in particular have expressed a keen interest to liberalize the use of NDFs. The separate limit on spot positions will be abolished in July. This may obviate the need for the NDF market.

The swap market is also small, although merchant banks have used very short swaps to raise dollars to cover liquidity shortages. This has been possible because transaction value today, tomorrow and spot are all considered spot transactions. Thus swaps within this time range did not alter banks' spot positions and thus did not break the spot limit. In such a transaction, a bank would sell foreign exchange spot (two days'

delivery) although it did not have it, and buy it value today or tomorrow to meet their maturing obligations. The next day, the maturing swaps would have to be rolled forward again for a day, in addition to new swaps to meet additional maturing commitments.

There is no netting of settlements in the market. All transactions are settled gross. It is not clear, according to a foreign bank branch that uses netting in its operations with some of its corporate customers, if Korean law would actually uphold a netting agreement if one of the parties to the netting arrangement defaulted.

Turnover in the foreign exchange market is low by international standards. In recent years average daily turnover has been in the \$2 billion range, but this year daily turnover has fallen to \$1 billion. Given the size of the Korean economy, daily turnover in the market could be in the \$30-70 billion range. The low level of turnover can only partly be explained by the fact that there still are restrictions on foreign exchange transactions. The bulk of trading in global exchange markets is in the interbank markets, as banks redistribute their exchange and interest rate risks and engage in a string of often complex hedging operations following one transaction with a customer. The most important restriction affecting turnover is probably the definition of open position limits. Banks have one limit on their overall net position, and another one on their spot position. The latter limit effectively cripples forward trading, since banks cannot hedge their forward trades through their balance sheet. One forward transaction between a bank and an enterprise typically generates several additional transactions as the bank hedges its position.

One other possible factor contributing to the low level of turnover in the market is to be found in corporate culture. Discussions with representatives of banks and enterprises revealed that there is little appreciation at senior management levels for the needs for active risk management and a strong aversion to the use of derivative instruments, which are regarded as speculative and very risky. It may therefore take time for business practices to change, although recent developments may have provided harsh lessons of the consequences of ignoring risks. Another reason for low turnover could also be found in the existence of the huge chaebol corporate conglomerates, for which it would be natural to net as much as possible of foreign exchange internally, and only enter the market with its net needs. This assumption about chaebol's behavior was confirmed by at least at one (Daewoo), where the central treasury takes over all the foreign exchange risks of the different branches, nets them off against each other. This drastically reduces the need for this chaebol to enter the foreign exchange market.

BoK interventions

BoK typically intervenes in the foreign exchange market through a commercial bank, which acts as BoK's agent in the market. The purpose of this arrangement is to keep BoK's interventions secret, although, according to market participants, the market always knows when BoK intervenes. BoK conceded this. This also confirms the experience in many other markets that central bank interventions of any meaningful magnitude are impossible to keep secret.

On the other hand the agent arrangement has the disadvantage of providing the agent bank with very valuable inside information. If it uses the information, it gets an unfair advantage over other market participants. If, on the other hand, it leans over backward not to take advantage of the information (which banks claimed they do), its customers may suffer.

Operationally, BoK informs a bank that BoK wants it to intervene on BoK's behalf. However, BoK decides when and at what rate to intervene. BoK monitors the KFTC screen, and when it sees a rate at which it wants to intervene, it calls the agent bank and instructs it to hit the quotation in question. Both spot and forward interventions have normally been undertaken in this manner, although on occasion BoK has also intervened through direct bilateral transactions.

After the floating of the won, the purpose of the few interventions that have taken place has been to reduce market volatility and prevent sharp changes in the exchange rate. While the operational decision to intervene can be taken by the director of the International Department, he would in practice always defer to a deputy or vice governor for authorization. MoF has apparently given BoK's governor some kind of general authorization to intervene, but the use of this authorization remains to be tested. Since foreign exchange policy is vested with MoF, it can instruct BoK to intervene in the market.

2 Management of Foreign Exchange Reserves

Management of foreign exchange reserves only refers to usable reserves. Foreign currency denominated receivables from Korean commercial bank branches abroad or from commercial banks in Korea is not included in the investment portfolio. For investment purposes, reserves are broken down into liquidity reserves and investment reserves. This system has been in use since the beginning of 1997, when a new computer system for reserve management was launched.

Liquidity reserves

The target level for liquidity reserves is USD 5 billion. In principle reserves are readjusted to this level on a quarterly basis, although the system broke down late in 1997 with the sharp outflow of foreign exchange reserves. Under normal conditions a liquidity reserve of USD 5 billion is considered adequate to meet reserve fluctuations within a quarter.

The liquidity reserve is made up exclusively of USD assets. Liquidity reserves are invested in money market instruments with a maximum maturity of 1 year. Acceptable investment instruments are bank deposits with a maximum maturity of 3 months, US Treasury Bills, US Federal Agency Discount Notes, and Fixbis investments with the BIS. About 10% of the liquidity reserve is invested in US Treasury Bills, some also in commercial bank deposits, but the main investment instrument is the Fixbis.

The return benchmark for the liquidity portfolio is 3 months Libid.

Investment portfolio

Assets in the investment portfolio are invested in the three main currencies USD, JPY and DEM. In addition to DEM, some other European currencies are also accepted for investment under the DEM umbrella: FFR, GBP and ECU. A currency benchmark is maintained for the investment portfolio and the liabilities to IMF on the balance sheet. Other foreign currency denominated assets and liabilities on BoK's balance sheet are not included in the definition of currency exposure.

The currency weights in the basket are confidential, but the USD is over 50%. For each currency a neutral point is defined. Actual reserves may deviate from the benchmark by +/- 5%.

Maximum permissible maturity for securities purchased is 10 years. For the global portfolio a benchmark with a 3 year duration has been defined. Maximum permitted deviation from the duration benchmark is +/- 1 year. The JP Morgan Government Bond Indices for the three core currencies serve as benchmark components.

The investment instruments in the investment portfolios, in addition to the instruments permitted in the liquidity portfolio, are typical core central bank instruments: Government Bonds, sovereign and supranational bonds and Eurobonds with a minimum rating of AA, and bonds issued by commercial banks. No derivative instruments are allowed.

Since the benchmark is global, taking a position in one market may force taking the opposite position in another market. The chief dealer makes these strategic decisions. Portfolios are updated for transactions and changes in asset prices overnight.

Credit risk

Only institutions with a top rating for short-term deposits are accepted for investment. A limit is placed on deposits that is related to each institution's capital. There is no global limit on exposure to credit risk in relation to total reserves. Typically under 5% of reserves are exposed to private commercial bank credit risk.

Decision making and reporting

Decisions on investment and currency benchmarks are taken by the Governor, albeit on the advice of Reserve Management Department.

The director of the department receives daily reports on positions and observance of limits. There is no reporting outside the department. Observance of limits as well as performance measurement are done by the dealing unit, i.e. portfolio managers monitor and evaluate themselves.

Organization

The Reserve Management Department is made up of three units: the portfolio management division, middle office and back office.

C ASSESSMENT AND POSSIBLE RECOMMENDATIONS

1 Strengthening the exchange market

Liquidity

Liquidity is important in any market. When the market is liquid, buyers and sellers can easily their transactions and, more importantly, the market price is not so sensitive to small variations in supply and demand. In an interbank foreign exchange market like in Korea with turnover of 1 – 2 billion USD per day, one big corporate order of, say, 100 million USD, will move the market rate. The reasons for the low level of turnover were discussed in the previous sections.

Some planned changes to regulations could enhance market liquidity and contribute to a more resilient exchange rate. Removal of the separate limit on spot positions would make it possible for banks to engage in normal hedging operations through their balance sheets. As discussed earlier, forward transaction between banks and enterprises or other banks typically generate several additional transactions as banks hedge their positions. Removing the current constraints would probably also assure that forward rates reflect interest differentials – this is not the case now.

It will take longer for corporate culture and the attitude to risk management to change, although recent developments may have contributed to drastically speeding up the learning process. However, BoK could contribute to a more modern attitude by publicly indicating that risk management is prudent, not speculative activity, and that no instrument is good or bad in itself.

Intermediation

The current arrangement for trading through KFTC in the exchange market is efficient and low-cost. It would be difficult for another broker to become competitive, even if the subsidy element were removed from KFTC resources. However, while KFTC should as soon as possible be fully taken over by the banks, other prospective brokers should not be prevented from entering the market, if they so wish.

It is unlikely that a significant OTC interbank market will emerge in Korea, again since it would be difficult for such a market to be competitive against KFTC. However, this is not a problem. The trend in international foreign exchange markets is towards electronic brokerage arrangements. The establishment of a normal forward market may generate more OTC dealing as banks engage in swaps with each other. Swaps are typically negotiated transactions, where both legs are done with the same counterpart.

While KFTC should be taken over by its users, the system should also be modernized to ensure that it can handle larger volumes. The bottleneck in the current system is the use of telephone communications, i.e. the part that has not been computerized. Communication by voice telephone should be replaced by use of computers, i.e.

participants system screens should be upgraded to allow two-way communication, so that orders and dealing instructions can be submitted by computer. Such a system will also be fairer, since the computer will know exactly in which order instructions arrived.

Code of conduct

A code of conduct is needed even if trading takes place over a computerized brokerage system. The Forex Club should be encouraged to do this. Numerous useful international models are available, and ACI, Association Cambiste Internationale, The international organization of national forex clubs, should be able to help in this respect. Central banks have also participated in the establishment of market rules in several of the world's major financial centers. This kind of information can be made available, if desired.

2 Bank of Korea's operations in the exchange market

Interventions

Bank of Korea may wish to reconsider its intervention procedures in a more market-driven direction. Since the main motivation in using agent banks – to keep central bank interventions secret – fails, and since the procedure does have disadvantages for the agent bank and its customers, BoK should look for alternatives.

The obvious, simple and straightforward procedure would be for BoK to intervene directly through KFTC. BoK would thus behave as any other market participant. BoK could either submit its own bids or offers, or follow current practice of reacting to bids and offers placed by others. The latter procedure is to be preferred, since it avoids the possibility that BoK becomes a price maker in the market.

Reference rates

There is still a need for reference rates even though the exchange rate is floating. However, establishing this rate should be kept as simple as possible. BoK could simply use each day's closing rate as the basis for its reference rate calculations.

Making information available to the market

It is important that enough information is made available on a regular and predictable basis. BoK should continue publishing data on reserves, including the forward position, if any. Some central banks publish data on a monthly basis, others weekly or bi-monthly. Any procedure is acceptable as long as the data is published within a reasonable period of time after the end of the reporting period. A lag of one week would be acceptable. It is important that the time limit is observed, since any delay could be interpreted as a sign of problems or disturbances.

3 Managing foreign currency denominated items on Bank of Korea's balance sheet

Deposits with Korean banks

Investment of a significant part of reserves with Korean banks' branches has seriously undermined BoK's possibilities for defending its currency through direct interventions. Lending of foreign currency to local banks can also be regarded as a type of intervention, it seriously weakens the central bank's capacity to perform its main functions. Also, even though central banks often have assumed lender of last resort responsibilities, this is usually fulfilled through lending the local currency.

It would be important for BoK to adopt a rule that does not allow lending of foreign exchange to Korean owned banks. Making such a rule public would send an important message to banks by showing that they can no longer count on BoK to support them if their foreign currency operations have been mismanaged.

Managing currency exposure

In determining its exposure to cross currency exchange rate risk, BoK currently does not take account of all foreign currency denominated assets and liabilities on and off its balance sheet. The resulting calculation is therefore misleading and needs to be modified.

Persons and institutions met in Seoul, May 25-29, 1998

Bank of Korea

Hyunchul Shin, Director, International Department
 Yeong-Rin Kim, Manager, Foreign Exchange Policy Division
 Dowon Kim, Economist, Foreign Exchange Market Division
 Min Ho Son, Manager, International Relations Office
 Hoo-Kyu Rhu, Head of Team, International Relations Office
 Myeong-Guk Suh, Economist, Foreign Exchange Market Division
 Keun-Man Yook, Chief Manager, Planning Division, Reserves Management Office
 Yoon-Chan Choi, Senior Portfolio Manager, Reserves Management Office
 Choo-Hyeong Cheon, Senior Portfolio Manager, Reserve Management Office
 Sung-Kyung Kang, Senior Portfolio Manager, Reserves Management Office
 GIsuk Song, Analyst, Reserve Management Office

Banks and Enterprises, in order of meetings

D J Kim, Vice President and Section Head, Financial Institutions Group,
 Bank of America, Seoul Branch

Jong-Han Song, Chief Country Office – Korea, Deutsche Bank, Seoul Branch

Lee Chang Hoon, Manager, International Treasury, Korea Exchange Bank
 S K Min, Deputy General Manager, International Treasury, Korea Exchange Bank

Yong Sik Kang, General Manager, International Banking Department, Hanil
 J S Chway, Deputy General Manager, International Banking Department,
 Hanil Bank
 Yoo-Jong Kim, Deputy General Manager, International Finance Department,
 Hanil Bank

K1-Ro Pan, Head, Financial Engineering Center, International Treasury, The
 Korea Development Bank

Jin-Kyung Kim, Senior Manager, International Finance Department, The
 Export-Import Bank of Korea
 Seong-Woo Park, Assistant Manager, Funds Management Department, The
 Export-Import Bank of Korea

Don You, Chief Manager, Treasury Team, SK Corporation

Sang-Ha Ju, Manager, FX and Trade Finance Department, Daewoo
 Corporation
 Sung-Soo Choe, FX and Trade Finance Department, Daewoo Corporation
 Hie-Jun Ahn, FX and Trade Finance Department, Daewoo Corporation



Office Memorandum

JM
CC FCS
W.S.
-SC

To Ms Tseng

June 8, 1998

From J Ferran *JF*

Subject **Korea--Draft Letter on Capital Account Liberalization**

The earlier removal of restrictions on short-term capital movements should be matched by an earlier implementation of the prudential regulations on short-term foreign borrowing and foreign exchange and data monitoring. In this context, it is necessary that Korea puts in place the necessary prudential controls and reporting system to prevent a repetition of the excessive short-term borrowing underlying the current crisis. Accordingly, we suggest to modify the last sentence of paragraph three on page 2 by adding the following:

“Given the decision adopted to accelerate short-term capital liberalization, further progress should be also made ahead of schedule regarding data monitoring and prudential regulations. Therefore, we recommend bringing forward the effective date of a number of measures, as set out in the attachment to this letter.”

In addition, I will be offering you a number of drafting suggestions.

Attachment

cc Mr Gutian

98 JUL -3 PM 5 50

ATTACHMENT

Proposed Acceleration of Prudential Regulations and Data Monitoring Measures

We would recommend bringing forward the implementation of the following measures identified in the May 2, 1998 letter of intent (LOI)

- Measures on strengthening compliance with existing guidelines for commercial banks to limit maturity mismatches in foreign exchange and the announcement of similar guidelines for merchant banks (page 10, LOI) Move forward to July 1, 1998
- The full phase in of prudential guidelines to limit maturity mismatches in foreign exchange for merchant banks (page 10, LOI) Move forward to March 31, 1999
- The announcement and implementation of additional regulations for commercial and merchant banks The additional regulations to include introduction of an internal liquidity control system based on a maturity ladder approach, agreement with the FSC on allowable maturity mismatches, the monthly monitoring of implementation by the FSC, and the public disclosure of statistics on foreign currency liquidity by bank (page 10, LOI) Move forward announcement to July 1, 1998 and implementation for commercial banks to October 1, 1998 and for merchant banks to April 1, 1999

- With respect to foreign exchange exposure limits, the implementation of the supervision of observance to be undertaken by the FSC, the replacement of separate limits on combined spot and forward positions, the incorporation of cross-currency positions in the measurement of exposures, and the introduction of consolidated limits for banks, including their offshore branches (page 11, LOI) Move forward to September 1, 1998
- The introduction of improvements to the reporting of off-balance sheet foreign currency denominated exposure of financial institutions and the submission of necessary legislation to ensure compliance with reporting on external liabilities of the corporate sector (page 17, LOI) Move forward to July 31, 1998

DRAFT

June 2 1998

Mr Lee Kyu-Sung
Minister of Finance and Economy
Seoul, Korea

Dear Minister

X The Government has taken several important measures recently to further liberalize the capital account. We welcome these measures, particularly those related to the liberalization of foreign direct investment and of restrictions on equity ownership in Korean companies. At the same time, it ^{is} ~~would be~~ important that the removal of restrictions on short-term capital movements be accompanied by adequate safeguards, particularly strengthened prudential regulations, consolidated supervision, and improved monitoring.

More specifically, restrictions on foreign investment in domestic money market instruments issued by financial institutions (CDs and RPs) are being liberalized ahead of the December 31 1998 schedule in the Letter of Intent. The timing of this liberalization measure in the letter of intent was to ~~take into account the~~ ^{allow for the parallel} implementation of a number of prudential regulations.

particularly those related to short-term foreign borrowing and foreign exchange exposures and with the start of consolidated supervision (January 1 1999)

In addition, two measures have been announced—lifting the 5 percent individual limit on foreign investments in futures and options trading, and allowing foreigners to borrow from local financial institutions for investment in local securities market—that could potentially ^{affect} add to the vulnerability to short-term capital flows

This underscores the importance of moving promptly to improve the regulatory framework for supervision and monitoring

On a related subject we thank you for the opportunity to review the draft policy paper on the revised Foreign Exchange Act We will communicate through Mr Dodsworth a detailed set of ^{technical} comments directly to your staff including clarification on a number of current account

transactions that were thought to have been liberalized when Korea accepted the obligations of Article VIII ~~As a general point~~ we welcome the further liberalization of the capital

account, particularly the move from a positive list to a negative list system, and the proposed streamlining of foreign exchange regulations ^{Consideration could also be given to including explicitly in the Act legal requirements for supervision and reporting of} rapid liberalization of short-term capital flows, but makes little or no reference to ^{short-term capital movements}

~~strengthening prudential regulations and improving reporting requirements. Again we would emphasize that the framework for reporting and supervision of short-term capital movements should be strengthened, and this may involve introducing legal requirements for reporting.~~

With these considerations in mind,

We would urge you as soon as possible to issue in final form the prudential regulations on short-term foreign borrowing and foreign exchange exposures (these measures are shown in

In corporate here the point made in E-mail

the attachment and to set up the monitoring arrangements included in the letter of intent of
May 2 [We would also appreciate hearing from you on the measures the Government intends
to undertake to reduce potential vulnerability arising from the liberalization of short-term
capital ^{ve} movements.]

7
but clear?

With best regards

Yours sincerely

Hubert Neiss

Director

Asia and Pacific Department



Office Memorandum

cc FOSS
KM
SC
D5

To Ms Tseng

June 8, 1998

From Deborah E Siegel *DES*

Subject Korea Foreign Exchange Liberalization

Thank you for the letter from Mr Yang that lists the 20 transactions for which payments and transfers were identified as "restricted" in the paper from the Korea Institute of Finance. As we understand the letter, the "restricted" transactions are explained as those that are currently subject to prior approval. The relevant portion of the attached questionnaire has been revised to clarify which transactions are subject to the prior approval requirement and how the process of approval operates. We understand that the proposed "liberalization" would involve removing the prior approval requirement for most of these transactions. Nonetheless, both sets of questions are relevant to evaluating the current state of Korea's exchange system and the questions on the approval process will continue to apply to categories that remain subject to the requirement. The questions concerning transfers by non-residents, deferred payment, and the exchange rate, also continue to apply.

As always, please feel free to call if you have any questions.

Attachment

cc Mr Johnston
Mr Kahn

LEG Mr Hagan (o/r)
Mr Leckow

98 JUN -9 AM 9 05

**Questionnaire
Korean Exchange System**

June 8, 1998

1 "Restricted" transactions to be liberalized The paper from the Korean Institute of Finance (the "paper") refers to 20 transactions for which payments and transfers are currently "restricted" (which will be reduced to five) We understand from Mr Yang's letter, that these payments and transfers are largely those that require prior approval¹ and that the liberalization plan involves removing the need for the prior approval We would appreciate clarification of (a) which transactions require approval and (b) the approval process²

(a) (i) The letter and the regulations (Article 2-24) refer to "admitted" transactions Is an "admitted" transaction one that is permitted even without prior approval and where are these listed? Are these the same as those permitted under the External Trade Act (could we get a copy of that Act)?

(ii) Could we please get a further explanation of the following items on the list from Mr Yang's letter (1) Items no (7) and (8) payments relating to "guarantees" -- (do they refer to financial guarantees by banks?), (2) Item no 10 payments of expenses for negotiations an confidential use, (3) Item no 14 "payment without having any relation to creation of credit, etc between the said resident and non-resident "

(iii) **Services** The paper refers to "individual licenses" for payments for consulting services, commissions for trade brokerage and research and development services (p 5) Payment for these transactions are identified in Mr Yang's letter as requiring prior approval (items (3), (4), and (9)) and the regulations require prior approval of the Minister of Finance and Economy for payment of "consulting service fees related to financing and insurance Business and proxy exercise of management" (Article 6-15-4(1)) Is this approval requirement the same as the licensing requirement set out on page 5 of the paper? Under what circumstances are payment (or licenses) for services approved?

¹Letter from Dohnson Yang, Deputy Director, Foreign Capital Management Division, International Finance Bureau, Ministry of Finance and Economy, to Mr J Dodsworth, June 1, 1998

² Under the regulations, certain current transactions are specified for prior approval either by (a) the head of a trading foreign exchange bank, (b) the head of the *designated* trading foreign exchange bank, (c) the Governor of the Central Bank, or (d) the Minister of Finance and Economy Covered transactions appear to include, for example, current transactions above certain limits and certain specific transactions such as interest, dividend and rental income, consulting service fees related to financing and insurance business and proxy exercise of management, and payment related to the purchase and sale of goods not prescribed in the External Trade Act

(b) Please answer the following questions concerning the approval process

(i) Under the regulations, certain transactions must be approved by the head of a *designated* trading foreign exchange bank -- what is a *designated* trading foreign exchange bank? Will there continue to be a distinction between such banks and other foreign exchange banks after the proposed liberalization?

(ii) In general (1) Is each entity responsible for approval *required* by law to approve requests for a payment once the person making the request has established that the payment is for a *bona fide* current international transaction (e.g., not for transferring capital)? (2) Are such approvals routinely granted in practice? (3) How long does processing the request take for each kind of approval? (4) Are these rules the same as those on "procedure for permission, etc." in Article 7-3 of the regulation?

(iii) Specific questions on **travel expenses** (1) What is the purpose of the "declaration" that must be made even for payments within the limits (Article 6-22)? (2) It appears that "additional" expenses above the specified limits may be made by credit card (Article 6-21), is this the only means for payment of additional amounts? For example, when residents can prove that transactions above the limit are *bona fide* payments associated with travel, can the resident seek approval to purchase of foreign exchange or make a payment by transferring the additional amount through the banking system? (3) Do similar rules apply for travel abroad for extended stay such as for study (e.g., an "overseas sojourner" as defined in Article 6-17)?

(iv) Certain aspects of **emigration expenses** could involve *current* payments, such as payments to shipping companies, rather than the transfer of capital out of Korea. Are all such *current* payments approved irrespective of the limits stated in Item 17 or the list in Mr. Yang's letter?

(v) The list in Mr. Yang's letter contains two categories (items nos. 12 and 13) on transfers for "**profit, interest, dividend, allotment money, etc.**", depending on whether they relate to transactions that are specified in Article 21(1) of the foreign exchange law, which require prior approval (1) For transactions that are specified in Article 21(1), are transactions for which prior approval has not been obtained lawful in Korea? Are transfers of profit, interest, etc., permitted even if prior approval for the transaction had not been obtained? (2) Are the transactions that are not listed in Article 21(1) lawful transactions in Korea? On what basis are transfers of profit, interest, etc., relating to these transactions approved?

2 Transfers by Non-residents

(a) What is the difference between non-resident won currency accounts and non-resident free-won accounts?

(b) (1) Are non-residents freely permitted to **credit these accounts** with proceeds of current international transactions. Non-resident *won currency accounts* may be credited with “domestic currency domestically acquired by nonresidents” (Article 10-34(1)) and these amounts may be used to buy foreign exchange (Article 10-35(2)). The articles on *nonresident free won* accounts (Articles 10-35-2 through 10-35-4) specifically refer to the “proceeds of current international transactions”, is there a difference in meaning intended between the descriptions of the two accounts? (2) May such amounts be transferred? Mr Yang’s letter refers payment of interest or dividend income to *won currency accounts*, may such income also be credited to *free won* accounts?

(c) Are non-residents freely permitted to **transfer abroad the interest earned** on *both* the non-resident accounts transferrable abroad? Interest on *won currency accounts* appears to be transferrable because it is listed in Article 2-45 among permissible sales of foreign exchange and it is listed among the circumstance for “disposal for buying foreign exchange” (Article 10-35(2)(c)). However, there is no provision authorizing transfer interest from *free won* accounts.

(d) What is meant by the payment limit of nonresidents noted in the regulations as “recognized foreign means of payment acquired or held”? (Article 6-5(2))

3 Deferred Payment Several provisions in Chapter 3 of the regulations require permission from the Governor of the Bank of Korea for payments that follow the import or the provision of a service beyond a specified period of time (e.g., Articles 7-12, 7-15, 7-24 through 7-32)

(i) Do residents require permission in order to enter into a contract for the import of goods or services that provides for deferred payment, or is permission only required to make the *payments* associated with such contracts? In what circumstances would permission to make such payments be refused?

(ii) Are there separate restrictions on short-term financing for imports?

4 Exchange Rate The paper refers to the daily quotations under the Market Average Exchange Rate System, which it states “do not reflect the most recent market conditions” (p. 9). Is this quoted rate used for any current international transactions (e.g., governmental transactions)?



Office Memorandum

cc FOSS
KM
SC
DS

98 JUN -9 AM 9 48

To Ms Tseng

June 9, 1998

From Manuel Gutian

Subject **Korea--Draft Letter on Capital Account Liberalization**

Thank you for sending me the above draft, on which I have only a few observations. At a general level, the letter seems to add little to what is already in the Letter of Intent, except for a general recommendation to expedite as much as possible the implementation of the regulatory measures included in the LOI.

While I have no problem with such a recommendation, I am somewhat skeptical of its effect. A strengthened prudential framework for banks' liquidity management should play a preventive role in the future. It cannot do much to solve existing maturity mismatches inherited from the past. Solving this problem will require access to long term finance. In Korea's case, access to international markets will initially be mostly at the short end of the maturity structure, and will only lengthen gradually as confidence is enhanced. In this connection, it would be helpful for the letter to emphasize the importance of the issuance of equity and long term bonds in the domestic and foreign markets, as a way to deal with the maturity mismatch problem.

There is a sense in the letter, particularly in the third paragraph, that we lack an understanding of the implications of the specific liberalization measures but that we have to make sure anyway that it is safe to proceed. This does not strike me as particularly helpful, if we have a specific concern--and it is not clear to me what that is--then we should identify it along with the proposed solutions. Finally, in that same paragraph, it is not clear why allowing foreigners to borrow from local financial institutions to invest in local securities markets would add to the vulnerability to short-term capital flows.

cc Mr Boorman
Mr Balñó
Mr Downes
Mr Johnston
Ms Milne



Office Memorandum

cc FOSS
KMM
SC
DJS

To Ms Tseng
From I R Dodsworth RD
Subject Foreign Exchange Law

June 8, 1998

Please see attached from MOFE

60 JUN 8 1998

< Lists of current transactions >

- ① The cases where any residents intends to make payment etc related to purchase and sale of goods, which is not proscribed in the External Trade Act
- ② Payment of price for utilization and use of facilities and real estate in foreign countries or price for rights thereon which are not directly related to business activity,
- ③ Payment of price for consulting services falling under one of the following subitems
 - a) Business not related to financing and insurance, and cases related proxy exercise of management
 - b) Cases only limited to consulting which is related to financing and insurance However the following cases shall be excluded
 - i) Price for services related to financing and insurance directly incidental to admitted capital transactions and import and export and
 - ii) Price for services related to insurance under provision of the laws and decrees concerning insurances
- ④ Payment of expenses for maintenance and activities directly incidental to research and development projects of the said overseas subsidiaries in the case of overseas subsidiaries established by residents.
- ⑤ Payment of disposal price of real estate excluding those which rent by non-residents for themselves, relatives and employees
- ⑥ Payment of sales proceeds, interest and dividend of securities acquired by non-residents from the inheritance and bequeath, and by non-residents as national from residents

- ⑦ Advance to customers in accordance with provision of collateral and guarantee related to credits exceeding US \$ 200,000
- ⑧ Payment of guarantee money deposition money etc for the purpose of guarantee and collateral other than those for providing performance warranty for the said transactions or act or in replacing issuance of guarantee in order to perform admitted transactions or acts by a resident
- ⑨ Payment of commissions for various brokerage consignment, representation, conciliation, proxy exercise, assistance, etc and exceeding 10/100 of the amount for the subject transaction or act or US \$ 50 000, excluding the cases of commission payment following the brokerage or representation directly incidental to export and import of goods,
- ⑩ Payment of expenses for negotiations and confidential use
- ⑪ Payment for the purchase of lottery tickets and other acts similar thereto
- ⑫ Payment for the transactions or acts for the purpose of capital income such as profit, interest dividend, allotment money, etc which are transactions or acts other than capital transactions falling under the provisions of each item of Paragraph (1) of article 21 of the Law
- ⑬ Payment of capital income such as profit, interest, dividend, allotment money etc acquired by the transactions or acts other than capital transactions falling under the provisions of each item of Paragraph (1) of article 21 of the Law.

- ⑭ Payment without having any relation to creation of credit etc , between the said resident and non-residents, and
- ⑮ Payment of interest or dividend income to domestic Won currency deposit and trust accounts (excluding Won account)
- ⑯ Payment of overseas travel expenses(Basic expenses US \$ 10,000)
- ⑰ Payment of overseas emigration expenses (US \$ 1 Million per family with 4 persons Householder US \$ 400 000, Members of Household US \$ 200,000)
- ⑱ Payment exceeding US \$ 5 000 per case for the purpose of donation
- ⑲ Withdrawal of domestic property by overseas Koreans
(the withdrawal limit US \$ 1 Million, procedure declaration to the head of the designated trading foreign exchange bank)
- ⑳ Payment recognized to have the possibility of interfering with the maintenance of international peace and public orders and payment related to acts against virtuous public morals and social orders such as crime gambling etc



Office Memorandum

15856
2/A
cc FOSS
D5
SC

To Mr Tanzi

June 5, 1998

From Walter Mahler *wm*

Subject **Korea Back-to-Office Report—Technical Assistance, Second Quarterly Review Under the SBA and 1998 Article IV Consultation**

From April 18-May 2, 1998, I participated in an APD mission to Korea headed by Ms Wanda Tseng. It had been envisaged that I would work parallel to the mission and concentrate on providing technical assistance on ways to obtain a better and more timely measure of the fiscal balance from below-the-line. However, soon after I arrived, the person in charge of the budget work for the mission had to leave suddenly because of his mother's serious operation. Ms Tseng asked if I could help with the mission's work on the budget, which I did. While my participation in some of the mission's meetings and work left me with much less time to devote to the technical assistance work, I was able to make considerable progress in describing the problems of measuring budget financing on a timely basis.

Given the significant delay in writing this BTO as a result of my delayed return to the office, I will briefly describe the budget outlook at the conclusion of the mission, but will focus more on my assessment of the Korean prospects for the rest of this year, and urge that the sharp decline in real GNP which appears probable for 1998 should be countered by moving beyond a cyclically neutral fiscal stance for 1998 to a significant fiscal stimulus.

Recent economic developments

Considerable progress has been made in alleviating the external financing crisis. The short-term external debt of domestic financial institutions has been restructured and the new sovereign bond issue was favorably received by the market. The significant inflow of funds into the stock and bond markets contributed to a relatively stable exchange rate in recent months, but foreign direct investment has remained weak. Inflation is close to 10 percent, but is not likely to rise much further. However, the real economy has deteriorated more than expected. Unemployment has more than doubled during the first four months of 1998 to 6.7 percent, and bankruptcies among small- and medium-sized enterprises have continued at a high level. Domestic consumption and investment have declined sharply. The mission projected that real GNP would decline by 1-2 percent in 1998. However, subsequent data and developments suggest a sharper decline, I believe a real decline of 4-5 percent of GDP is likely.

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1998 budget

The supplementary budget presented in March had provided for a deficit in the consolidated central government balance equal to 1.2 percent of GDP, compared to the 0.2 percent of GDP surplus in the November pre-crisis budget. It was estimated that the cyclical impact of the crisis would have worsened the consolidated budget balance by 1.6 percent, and the exchange rate depreciation would have worsened the balance further by 1.0 percent of GDP. In addition, the crisis triggered increased discretionary expenditure of 1.7 percent of GDP in the form of interest costs for bank restructuring and higher social safety net expenditure. This worsening of the balance by 4.3 percent of GDP was offset by measures in December and March totaling 2.9 percent of GDP. About two-thirds of this adjustment was the result of expenditure cuts in government salaries and all ministries' budgets except those related to social expenditure, the remainder resulted from increases in tax rates on gasoline and special excises and broadening of the income tax and VAT tax bases. The revised program prepared by the mission projects a deficit of 1.7 percent of GDP as a result of a further adverse cyclical impact from slower growth. About half of the 0.5 percent of GDP impact was estimated to be on the expenditure side and half on the reverse side. The authorities were very concerned about showing much deterioration in the fiscal outlook so soon after the supplementary budget in March, although they recognized the need to avoid a significant contractionary fiscal stance. The mission would have supported a somewhat larger budget deficit.

New tax measures

During the mission, the Government announced plans to reduce the number of national taxes from 17 to 10 during the 1999-2001 period. Under the plan, taxes on excess land income, asset revaluation and unfair income will be scrapped and the telephone tax will be incorporated into the VAT. The education and special rural development taxes will be incorporated into the basic excises on petroleum products. It was expected to present a tax reform bill to Parliament in September or October, incorporating these desirable simplifications.

In early May, a 30 percent increase in the transportation tax on gasoline and diesel went into effect, while provincial registration taxes on vehicles were reduced sharply. These measures were intended to be revenue neutral with offsetting transfers from the central government. The not very worthy primary purpose of this adjustment was to reduce the cost of owning cars and thereby encourage domestic sales, while simultaneously discouraging the use of cars.

Policy concerns

It was very interesting to work with the APD mission and to get a first-hand view of the situation from a number of old friends who have held prominent positions in Korea. Unfortunately, I came away much more pessimistic about the short-term prospects for the Korean economy than either the mission or most of my Korean friends. The quality of the officials providing economic advice to the President is weak. Many of them have little

experience dealing with the bureaucracy or the business community. There is a considerable timorousness in providing advice to the President. This has been furthered by the “witch hunting” effort led by public prosecutors to investigate the Minister of Finance and another prominent economic advisor at the time the crisis emerged. The abolition of the post of Deputy Prime Minister has meant that there is nobody in the system with the clout to effectively coordinate economic policy.

The three main tasks at present are strengthening the banking sector, corporate restructuring, and labor market adjustment. All three are difficult in terms of strategy and pace. Most worrisome of all is how to handle the labor market problem. The continuation of high interest costs and the currently envisaged fairly rapid restructuring of commercial banks and the chaebols will lead to further significant increases in the unemployment ratio. Given that implicit lifetime employment has become the norm for most large firms, and that Korean labor has had an unprecedentedly rapid increase in real wages during the past 30 years, political acceptance of this adjustment will be difficult to sustain as the situation worsens. The government will need to present a better multifaceted vision of how this problem is being handled. So far there has been a slight reduction in nominal wages in the private sector, while government salaries were cut 10 to 20 percent. Each aspect of the current approach to the labor market problem needs to be much bolder. There is a need for broader, easier and longer provision of unemployment benefits coverage. There is a need to set up a “public works” system which temporarily provides modest wage earning opportunities to both blue and white collar labor, while yielding something of use to the society. This program would be better targeted to helping the relatively poor, than unemployment benefits. There is also a need to greatly enhance retraining facilities for blue and white collar labor. Finally, there is a need to encourage a further significant reduction in nominal wages in all sectors (perhaps with a larger cut at the top than at the bottom of the wage scale), this will enhance the working capital of enterprises, slow down unemployment and enhance equity between those that continue to have jobs and the unemployed. All four of these measures will work toward increasing the budget deficit and will provide desirable fiscal stimulus. Enhanced expenditure to strengthen banks and facilitate increased lending to corporations will also be necessary to keep real income growth and employment from declining excessively.

Social safety net

With effect from March 1, 1998, the coverage of the unemployment insurance system was extended to firms with 5 or more employees (compared to 30 or more since end-1997). In addition, the contribution period required for benefit eligibility was lowered to 6 months from 12 months, the minimum duration was raised from 1 month to 2 months (the maximum duration remained unchanged at 7 months) and the minimum benefit level was raised from 50 percent of the minimum wage to 70 percent. About 70 percent of the labor force remains outside the scheme (including workers in firms with less than 5 workers, temporary, part-time and daily workers, self-employed and public sector employees). The social safety net also includes a special loan scheme of about W1.6 trillion for urgent personal needs in the form of

medical, schooling or funeral expenses, various retraining program totaling over W700 billion and about W600 billion for cash benefits to low income persons

As economic growth and unemployment continue to worsen, I think the whole issue of social safety net expenditure will become a major focus of the next mission. While the World Bank has initiated work in this area, I think the Fund should take a role in helping to design sensible schemes. My own view is that not enough attention has been given to the problems related to greatly expanding the unemployment scheme. Even though the present scheme only covers 30 percent of the work force, it appears to be very difficult administratively to extend the coverage. The average size of firms with less than 5 employees is just 2 employees and these are mostly family firms. When the employees are related to the employer it is difficult to police against fraud. While the scheme could be expanded to cover public sector employees, employment in this sector in Korea is comparatively lean and there is not much talk of reducing employment in this sector. The main change I would recommend to expand coverage is to reduce the importance of period of contribution as a factor for access to the scheme and for magnitude of benefit. In a largely new scheme trying to address an emergency, I believe that more weight should be given to period of employment. Even with a 6 month contribution period, the extension of the scheme to firms with 5 to 30 employees on March 1, will have no impact until September 1, by which time most of the unemployment in this sector will probably have already occurred, so the increased effective coverage will be modest.

Budget targets

In the current circumstances in Korea, there appears to be no need to introduce a performance criterion in the form of a ceiling on the budget deficit. During the remainder of 1998, the Fund staff is likely to be in the position of urging the authorities to have a higher deficit than they themselves wish. Hence in the present circumstances a performance criterion should probably take the form of a floor, rather than a ceiling on the deficit. However I think it is preferable to have no performance criterion on the budget balance, but rather just continue to have an agreed target for the budget deficit.

As indicated earlier, a higher deficit should be sought not by reducing tax rates, but by further increasing expenditure to strengthen the capacity of commercial banks to increase loans to corporations and expenditure on unemployment benefits, retraining, increasing employment on public works projects and social welfare expenditure for the poor. Introducing the novel idea that the Fund is explicitly seeking significant fiscal stimulus under one of its programs would help overcome the prevalent image that the IMF always seeks to constrain the budget deficit under its programs. With monetary policy constrained by exchange rate considerations, fiscal stimulus appears necessary to avoid a sharp decline in real GDP.

Technical assistance

The objective of the technical assistance mission was to try to set up a reporting system to monitor the fiscal position from below-the-line so that the fiscal balance could be made into a performance criterion. For this purpose, it was considered important to have all of the necessary data reported within six weeks of the end of a quarter. I worked closely with the Bank of Korea and the Ministry of Finance and Economy (MOFE) staff handling budget financing data. There are problems with the data from both sources. It is not possible to measure changes in the stock of government securities outstanding from the BOK's financial sector accounts because they measure only holdings by deposit money banks and other financial institutions but exclude holdings by individuals, corporations, and foreigners. Hence it will be necessary to measure net government bond financing from the MOFE accounts.

At present, the only complete reporting of budget data takes place at the end of the fiscal year (same as calendar year). The data must be reported by law by February 20, and the accounts are finalized by March 10. Thus, in order to meet the six week reporting target after the end of the year, the law would need to be changed. There is no legal requirement for quarterly reporting and it is estimated that about 5 percent of the 6,500 sub-branch offices of ministries do not make quarterly reports. Almost all of the underreporting affects the expenditure total, so there is some underestimation of the magnitude of the deficit at the end of each quarter.

This partially incomplete data is usually available with an eight week lag. So far, quarterly data collection has not been given much importance by the authorities. To get more complete data provided within the desired six week period at the end of quarter would require the IMF and MOFE to give such data major importance. If the Fund team were to consider improvement of the data an important priority, it could be done. To implement such an improvement in the collection system would require a few months and introduction of some form of penalty for non-reporting. I am preparing a report recording my findings on this subject.

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