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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 97/118

2:30 p.m., December 9, 1997

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Executive Board Attendance

S. Fischer, Acting Chairman

Executive Directors	**Alternate Executive Directors**
A.A. Al-Tuwaijri	S.M. Al-Turki
	R. Fernandez
	M. Askari-Rankouhi, Temporary
	H. Kaufmann, Temporary
	W.-D. Donecker
	A. Giustiniani, Temporary
	P.A. Akatu, Temporary
A. Kafka	
W. Kiekens	
K. Lissakers	
	S. Rouai, Temporary
	A. Lushin, Temporary
	J. Shields
A.S. Shaalan	
M.R. Sivaraman	
E. Srejber	
G.F. Taylor	O. Kwon
	T. Brizuela, Temporary
J. de Beaufort Wijnholds	
K. Yao	
	H. Ono
	O. Sein, Temporary
Zhang Z.	
A.G. Zoccali	

A. Mountford, Acting Secretary
S. Bhatia, Assistant

Also Present
Asia and Pacific Department: H. Neiss, Director; F.C. Adams. External Relations Department: P.C. Hole, Deputy Director; H.P. Puentes. Fiscal Affairs Department: K-Y. Chu. Legal Department: F.P. Gianviti, General Counsel; S. Hagan. Monetary and Exchange Affairs Department: C. Pazarbasioglu. Policy Development and Review Department: J. Ferrán, Deputy Director; R.H. Nord. Research Department: Z. Chen. Secretary's Department: R.S. Franklin, P. Gotur. Treasurer's Department: M.G. Kuhn. Western Hemisphere Department: C. Cha. Office of the Managing Director: B.V. Christensen, O.J. Evans—Office of Internal Audit and Inspection: E. Brau, Director. Advisors to Executive Directors: S.S. Farid, C.M. Gonzalez, J. Jonáš, R. Kannan, B. Konan, E. Rodriguez. Assistants to Executive Directors: J. Chelsky, D.A.A. Daco, J.P. Leijdekker, Lu A., D. Merino, I. Moon, L. Palei, O. Schmalzriedt, Zubir bin Abdullah.

1. REPUBLIC OF KOREA—REQUEST FOR PUBLICATION

The Executive Directors continued from Executive Board Meeting 97/117 (12/8/97) their consideration of a request by the Korean authorities to publish the staff paper on the Republic of Korea's request for a Stand-By Arrangement (EBS/97/222, 12/3/97; Cor. 1, 12/4/97; and Sup. 1, 12/4/97).

Mr. Kwon stated that two days earlier one of the Korean newspapers had published details of the program, which indicated that the press had obtained the entire staff paper (EBS/97/222). Following that, there had been much of speculation on the program and pressure from the public for further information. He regretted to inform the Board that his authorities had, therefore, released the staff paper to the press. Nevertheless, his authorities wished to make a formal request to the Board for release of the staff paper.

Mr. Wijnholds noted that Table 7 of the staff paper indicated that short-term external debt was about US$65 billion, while the press was reporting that the short-term external debt—including offshore debt incurred by domestic banks—was $100 billion. In order to avoid confusion, it was important to clarify the exact size of the short-term debt.

The staff representative from the Asia and Pacific Department observed that $65 billion figure referred to the onshore debt, as reported by the Korean authorities. The $100 billion figure referred both to onshore and offshore debt. Until recently, the staff had information on the onshore debt, but had not had complete information on offshore debt.

Ms. Lissakers, noting that the onshore debt data might also include domestic banks' liabilities to offshore banks and to affiliated companies, wondered whether there was some double counting in the debt figures.

The staff representative from the Asia and Pacific Department replied that the staff had in fact been trying to determine the extent of double counting. For example, a substantial portion of the offshore debt data was unallocated and was not reflected in the Bank for International Settlements (BIS) data. The staff was trying to determine the liabilities of domestic Korean banks to offshore Korean banks in order to gauge the extent of double counting. At present, however, the staff did not have a precise estimate of the extent of double counting. The presumption was that the short-term external debt was, at maximum, $100 billion.

Mr. Wijnholds asked how the staff obtained information on the offshore debt.

The staff representative from the Asia and Pacific Department said that the staff working at headquarters had initially obtained that from information from BIS data. Subsequently, the staff had received broad confirmation from the authorities; however, the details remained to be clarified.

Mr. Wijnholds remarked that it would appear that the Korean authorities had not been forthcoming with the information.

Ms. Lissakers commented that it should not be assumed that the Korean authorities were not being fully cooperative. It was understandable that the authorities faced some difficulty in obtaining the information from individual banks, as banks themselves often did not have a clear picture of their total liabilities. On the data itself, she was puzzled by the BIS data, which showed that total bank-to-bank claims were $67 billion, which was inconsistent with the data from the Korean authorities.

The Acting Chairman observed that he had asked the staff at various stages of the mission whether the authorities were being cooperative, and the staff had informed him that they had been getting full cooperation from the authorities right from the beginning. During his own brief visit, particularly to the central bank, he had found the authorities to be very forthcoming. The staff would explore further the question raised by Mr. Wijnholds on the short-term debt figures.

Mr. Wijnholds, noting that the circumstantial evidence did not point to a high degree of cooperation, said that he would like further clarification on the matter. He also asked for further information on the legal aspects of the interest rate ceiling.

Mr. Donecker expressed deep concern over the fact that the authorities had released the staff paper without prior Board approval. While the Board supported the authorities' motivation to inform the public about the program, that could have been done by releasing the letter of intent, issuing a press information notice, or in some other form, with the assistance of the Fund's External Relations Department. The authorities should not have gone ahead and released the staff report—which was a confidential Fund document—without Board consent. That had cast a shadow over the authorities' willingness to cooperate with the Fund, and was regrettable.

Mr. Kiekens also expressed regret that the authorities had released the report without Board approval. He saw little merit in discussing the issue further.

Ms. Lissakers agreed with Mr. Kiekens that it would not be useful to discuss the matter further. It was very important that the authorities understand the importance of consulting closely with the Fund in making their decisions, given the extent of financial resources committed and policy advice by the Fund and the international community, and the fact that they were trying to help Korea minimize damage to its own economy and to the world economy. There was an obligation on the part of the central bank, the ministry of finance, and the political leadership to keep the Fund continuously informed of their policy intentions that had a bearing on the program. The effectiveness of the program and of the confidence building efforts could be seriously undermined if there were misunderstandings between the authorities and the Fund.

The Director of the Asia and Pacific Department stated that the original figure on the short-term debt that the staff had obtained from the authorities was $65 billion. That figure referred to the short-term debt of domestic banks. In addition, the overseas branches of Korean commercial banks had also incurred debt. While the authorities did not have precise information on the size of those debts, the initial estimate was that those debts were about $60 billion. However, there was probably some double counting, and the authorities were trying to get an accurate estimate of the size of the total short-term debt. The preliminary view was that the total short-term debt was probably $65 billion—the debt of domestic banks—plus about $50 billion—the debt of overseas branches of commercial banks. However, no final estimate was available as yet.

Mr. Wijnholds asked the staff for information on the legal provisions relating to the interest rate ceiling and the plans for recapitalization of two commercial banks. He asked whether the letters by the presidential candidates, pledging support to the Fund-supported program, were available.

The Director of the Asia and Pacific Department observed that the staff mission had discovered on the previous day that, under Korean law, interest rates could not rise above 25 percent. The staff was trying to ascertain the steps that would need to be taken under the law in order to remove the interest rate ceiling. If removal of the ceiling required approval by the National Assembly, it would have to wait until after the elections, that is, until December 19 at the earliest. It was possible that a presidential decree would be sufficient to remove the ceiling. The authorities had taken the decision to recapitalize the banks without consulting the Fund staff. The staff was trying to ascertain the conditions under which such support from the central banks would be justified. The conditions could include the following: creditors would bear part of the financial burden; management of the banks would be changed; and operational guidelines for those banks would be established.

Ms. Lissakers asked whether the staff had any information on the financial condition of the two banks.

The Director of the Asia and Pacific Department observed that the staff had noted earlier that some sort of intervention was needed to address the problems of the two commercial banks. The staff had proposed the following rehabilitation plan: the banks would need to submit a recovery program within two months, which would then by assessed by the supervisory authority—that is, the Ministry of Finance, until the creation of a new supervisory authority—in consultation with the Fund. If the recovery plan of the bank was approved, the bank would have four months to implement it. Implementation would be closely monitored by the supervisory authority, in consultation with the Fund and Bank staff. After four months, the supervisory authority would make a decision—in consultation with Fund and Bank staff—as to whether the bank was viable. If they considered that it was not, the bank would be closed down.

Subsequent to writing letters stating their full support for the program, the presidential candidates, in a television discussion, had tried to distance themselves from the Fund-supported program, the Director of the Asia and Pacific Department noted. However, none of the candidates had said that he would not support the program; all three candidates continued to support it in principle.

Mr. Wijnholds, Mr. Shaalan, and Ms. Lissakers asked whether staff or management had copies of those letters and whether they could be circulated to the members of the Board.

The Acting Chairman responded that the letters had been in the Managing Director's possession, and were probably still with him. He would look into the matter and inform the Board accordingly.

Mr. Kiekens remarked that the most important task ahead was to resolve the problem of removing the interest rate ceiling. The Board should be kept informed on the issue.

Ms. Lissakers asked for further information on the nature of that law.

The Acting Chairman observed that the law was probably similar to anti-usury laws that existed in other countries.

Management would return to the issues raised by Directors, the Acting Chairman concluded. The message of the Board on the need for cooperation between the authorities and the Fund had been heard by Mr. Kwon and would be passed on to his authorities.

DECISION TAKEN SINCE PREVIOUS BOARD MEETING

The following decision was adopted by the Executive Board without meeting in the period between EBM/97/117 (12/8/97) and EBM/97/118 (12/9/97).

2. EXECUTIVE BOARD TRAVEL

Travel by Executive Directors as set forth in EBAM/97/191, Supplement 1 (12/5/97); and EBAM/97/192 (12/5/97) is approved.

APPROVAL: July 7, 1998

REINHARD H. MUNZBERG
Secretary