

FIVE BANKS FINALLY CLOSED DOWN IN KOREA

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The Korean Government recently took the historic step of ordering five commercial banks to close down due to a lack of capital adequacy. The Financial Supervisory Commission (FSC) announced the list of five non-viable banks to be closed and seven conditionally-approved banks on June 29. This was done after having examined the "management normalization" plans submitted by these 12 commercial banks whose BIS (Bank for International Settlements) capital adequacy ratios were below the recommended 8% standard. The Korean Government's move aims to achieve the creation of strong banks and disposal of weak banks in the market.

The five non-viable banks have been ordered to shut down and merge with better banks which were selected by the FSC, while the seven banks given conditional approval need to carry out harsh restructuring including the dismissal and reshuffling of management, employee layoffs, branch closures, and reduction of paid-in-capital. These seven banks are

required to submit another feasible plan of better management to the FSC by the end of July. Otherwise, they may not be able to avoid the same fate as their five predecessors.

The five nonviable banks are Daedong, Dongnam, Dongwha, Kyunggi and Chungchong; these are to be merged by the so-called P&A (purchase and assumption) method with Kookmin, Housing & Commercial, Shinhan, KorAm, and Hana, respectively. The seven conditionally approved banks are Korea Exchange, Chohung, Commercial Bank of Korea, Hanil, Peace, Kangwon, and Chungbuk. Under the P&A formula, the acquiring banks will take over the assets and liabilities of the liquidated banks, which will be dissolved. The FSC said that deposits by clients will be perfectly protected, and loans, commercial paper and other securities related to small firms will continue to be extended. In other words, to avoid possible disorder in the financial market, the FSC let ailing banks continue their deposit-related business even if they are suspended or will be

<Table 1> The Five Non-Viable Banks and Their Acquiring Banks

Non-Viable Banks (Acquiring Banks)	Daedong (Kookmin)	Dongnam (Housing&Com)	Dongwha (Shinhan)	Kyunggi (KorAm)	Chungchong (Hana)
BIS Ratio(%)	4.54 (9.78)	4.54 (10.29)	5.34 (10.29)	6.69 (8.57)	7.05 (9.29)
Tot. Asset(Bil.Won)	7,715 (54,400)	10,056 (46,962)	12,968 (43,585)	8,894 (16,434)	4,829 (22,944)

merged.

The FSC's method of shutting down these five banks, however, did not necessarily receive a warm welcome from all sides. The most serious problem was found in a seemingly microcosmic but nonetheless essential part—i.e., the takeover procedure by the acquiring banks of the ailing banks' computer data and transaction materials. For example, many workers at the acquired ailing banks refused to work or operate computer facilities in due manner for several days. Another intrinsic problem of this method lies in the "healthy banks care for ailing banks" principle. As many critics point out, the five acquiring banks' management should be recognized for their superior management rather than be "punished" by taking over ailing banks with the risk of weakening their own asset-liability structures. Outside observers were quick to catch this problem: U.S. credit rating agencies are going to review the credit profiles of the five acquiring banks in light of the uncertainty of the true quality of assets to be acquired.

However, as is widely understood, the primary object of the liquidation of these ailing banks is to accelerate financial restructuring. Everyone has stressed that the restructuring of financial institutions, especially the banking sector, is the most important and urgent task to

solve the current economic crisis. Even though the current restructuring method of the banking industry has been criticized with respect to the scale and the process, the bank closures will have a major impact on the restructuring direction of the whole financial industry. This was just the first step to make the Korean financial industry more efficient and competitive in the earliest future.

According to what the Korean government has announced so far, the schedule for financial restructuring will be pushed even faster than was originally planned. Merchant banks and leasing companies (about July), insurance firms (about August) and securities companies (about September) are waiting for other major steps. After analyzing leasing companies' financial status, the government will liquidate about 10 of them whose debts surpass their assets, have them taken over by a third party, or establish bridge leasing companies. For the insurance industry, a committee will be established to evaluate the management normalization plans prepared by 18 life and 4 non-life insurance companies. After finishing the evaluation, the FSC will issue a liquidation order to ailing insurers before the end of August. Also the FSC's final decision on ailing securities companies is expected to be made no later than this coming December, if not earlier. **VIP**

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〈Table 2〉 The Conditionally Approved Banks

	Korea Exchange	Chohung	Commerical. Bank of Korea.	Hanil	Peace	Kangwon	Chungbuk
BIS Ratio(%)	6.79	6.50	7.62	6.90	5.45	5.37	5.92
Tot. Asset (Bil.Won)	62,319	55,600	48,552	53,854	8,359	3,869	3,139