

East Asia and Pacific Law

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I. Developments in Korea

Without question, 1997 will be remembered as a watershed year for Korea in the international arena. While the year began with the Korean Ministry of Finance and Economy (MOFE) working slowly to break down barriers to foreign trade and investment, by year-end the International Monetary Fund (IMF) and the Korean financial crisis had prompted the Korean Legislature and the MOFE to demolish most obstacles wholesale. Unfortunately, the financial crisis left a wave of economic destruction in its wake.

A. BANKING AND FINANCE

Early in 1997, the Hanbo Chaebol (including Hanbo Steel Corporation) was forced into a bankruptcy with over \$6 billion in debt. Subsequently, Sammi Steel and another large Chaebol also went bankrupt. Later in the year, several other Chaebols, including Kia Motors, went into bankruptcy or, in the case of Kia Motors, government rehabilitation.

The fallout for Korean commercial banks was devastating. First, in response to the Hanbo bankruptcy, the Federal Reserve Board (FRB) halted all U.S. applications for Korean banks as it reexamined whether Korea exercised "comprehensive supervision" over its banks. The experience with Hanbo caused the FRB to realize that Korea did not have a "one loan to one borrower" rule that aggregated related borrowers after Korea First Bank lost half of its capital in the Hanbo bankruptcy. The Basle "core principles" require aggregation. After a series of meetings with the FRB over the summer, the MOFE and the Office of Bank Supervision announced that loans to all affiliates of the top thirty Chaebol would be aggregated for lending limit purposes and that Korean banks must reduce overline exposure by the year 2000. In response, the FRB approved, in September, the application of the Korea Housing Bank to open a branch; the gate had been shut too late. Several more Chaebols and many small companies failed. By December, representatives of the FRB or of another regulator were stationed daily

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in every Korean bank branch and agency in the United States, keeping track of potential liquidity problems and bad loans. By early 1998, Korean banks were withdrawing from the United States. Approximately twenty percent of the Korean bank loans were alleged to be past due and in default. The Korean commercial banks themselves had technically defaulted on their foreign borrowings.

B. INVESTMENTS

Under pressure from the IMF, Korea dropped substantially all foreign ownership restrictions on Korean stocks and bonds by early 1998. Hostile mergers were expected to be permitted, although the MOFE primarily sought a way to allow Chaebols to "trade" non-core subsidiaries so that each Chaebol could focus more closely on specialized industries.

Although the adoption by Korea of the Real Name Statute had been a step forward in terms of financial transparency, the FRB (prodded by the U.S. Congress) insisted that Korean banks adopt strict anti-money laundering procedures. However, the financial crisis caused the Korean National Assembly to take a step back by adopting authority for the government to issue "bearer bonds." Fortunately, the rules in the United States stopped a Korean government plan to raise U.S. dollars using the Korean bearer bonds.

C. TRADE

Although Korea, until late in the year, was running an annual deficit with the United States of about \$20 billion, the U.S. Trade Representative and the U.S. Department of Commerce pushed hard to force Korea to remove trade barriers, especially those that slowed the export of U.S. automobiles and movies to Korea. The Trade Representative started a year long process threatening to impose trade sanctions against Korea on October 1, 1997, the same day as the first meeting of the U.S. Department of Commerce and the Korean Ministry of Trade Committee on Business Cooperation.

Under the duress of the financial crisis, the United States dropped some old dumping charges on Korean manufactured television sets, but refused to undo the threat of dumping charges against the Korean semi-conductor industry. That industry had been devastated by competitive price declines (from \$60 per chip in 1993 to \$5 by 1997) and in turn the semi-conductor industry losses devastated the Korean economy. The major Chaebols (LG, Samsung, Hyundai) had transferred production to the United States, in order, among other reasons, to avoid the dumping charges. However, the Korean financial crisis wreaked havoc with the financial capability of the Korean chip-makers to continue their U.S. expansion plans.

II. Developments in Japan

A. FINANCE

Seven years after the "bubble" burst on the Japanese real estate market we have the "Big Bang." For generations, the finance, insurance, and securities industries in Japan had seemed stable, secure, and indomitable. Then, in 1997, things started to change. Nissan Mutual Life Insurance Co. went bankrupt on April 25th, Sanyo Securities Co., Ltd. filed for protection under the Corporate Reorganization Law on November 3rd, Hokkaido Takushoku Bank, Ltd. went bankrupt on November 17th, and Yamaichi Securities Co., Ltd. went out of business at the end of the month. The demise of the latter two was extremely significant. Hokkaido Takushoku was the first large city bank to fail in Japan since the war (even though the Ministry of Finance had permitted some smaller banks to go out of business in recent years) and Yamaichi

Securities was one of the "big four" securities houses in Japan. Clearly, some major revision to business-as-usual is needed.

"Japan, Inc." has been coined as the expression to symbolize the economic leadership that Japan enjoys in the world and particularly in Asia. The virtual meltdown of the neighboring economies in Thailand, Malaysia, Indonesia, and finally Korea makes the continued stability of the Japanese economy all the more important to the world today. Japanese Prime Minister Hashimoto led the government of Japan to move in several ways to restore confidence in the Japanese financial system. The Ministry of Finance (MOF) is to make public funds available for protecting depositors in the form of 10 trillion yen in government bonds and 20 trillion yen in government guarantees. In addition, the financial base of the Deposit Insurance Corporation of Japan (DIC) will be strengthened by the infusion of 7 trillion yen in government bonds and the enforcement powers of the DIC will be strengthened. Also, the functions of the Resolution & Collection Bank will be expanded to cover credit unions and other financial institutions as well as banks. Further, the MOF is requiring banks to downgrade assets in their portfolios to market values, which has resulted in much securitizing or selling of assets to meet mandated ratios in light of the new laws requiring more complete disclosure. Talk of tax legislation did not result in any action by the end of the year. More work remains to be done.

B. CIVIL AVIATION

Since our report a year ago, an agreement has been reached between Japan and the United States on regulations for the carrying of passengers and cargo. Northwest Airlines, Federal Express, and United Airlines now possess unlimited opportunities to fly between any point in the United States and any point in Japan. Previously, for example, Northwest could only fly to Tokyo, Osaka, and Okinawa from sixteen cities in the United States and to Nagoya and Fukuoka from Honolulu. Additional flights per week between the two countries are now allowed. Practical limitations on landing slots at major airports in Japan limit the benefit of this achievement due to the current single runway configuration in Tokyo, Osaka, and elsewhere. When second runways are added at such places, this new agreement provides that International Air Transport Association (IATA) allocation procedures will be used for assigning the additional capacity. Then, the additional flights provided for in this agreement will be utilized.

Perhaps more important is the right the specific U.S. carriers have now received to carry passengers and cargo to all points through and beyond Japan to any point in the Asia-Pacific region, including Oceania. The agreement also provides opportunities for code-sharing with other airlines flying to and from Japan and through Japan to Asia. While complete freedom to reduce prices is not allowed, the agreement now permits more competitive pricing.

On the Japanese side, All Nippon Airways gains unrestricted access to the United States—a right previously reserved only to Japan Airlines. The agreement will permit additional U.S. airlines to travel these same routes in future years. Whether the United States obtained a favorable resolution of this long-standing negotiation can be determined by listening to the howls of protest from the executives of the airlines in Japan. One final note is that this agreement with Japan marks the end of a loudly proclaimed policy that Washington would only sign "open skies" agreements with other countries and would not settle for anything less.

