KIEP

Working Paper 00-13

The Liberalization of Banking Sector in Korea: Impact on the Korean Economy

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EXECUTIVE SUMMARY

Since the 1990s, the international financial environment has changed fast in terms of globalization, diversification, deregulation and innovation. The development of information and telecommunications technology has led banking institutions to shift from the traditional lending and borrowing activities to multi-financial projects and development of new financial products. Financial engineering has generated various derivatives and international financial transactions have, thereby, been diversified, with the various loosening restrictions on the financial industry.

On the 21st century, the financial industry will have achieved a unified international financial market, due to international financial liberalization and cross-border services under the WTO New Round. With more competition and removal of entry barriers in the international financial market, developed countries have promoted M&As in the financial industry and universal banking system.

After financial crisis, important steps were taken to increase foreigners' access to the banking sector in Korea such as subsidiary and ownership of banks. The benefits of liberalization in banking sector is as follows: to facilitate the exchange of goods and services; to facilitate risk management; to mobilize resources; to obtain information, evaluate firms, and allocate capital; and to provide corporate control. However, there are possible negative effects such as increase in unemployment, higher foreign capital occupancy of the local market, more influence of foreign capital on domestic market and intervention in domestic corporate. Also, freer capital flows have the effect of smoothing consumption over time, and it has to be recognized as the benefit of the liberalization.

We investigated the trend in penetration of foreign banks into the Korean market. Given the regulatory restriction, it has been confirmed that the extent of the penetration remained limited. Foreign banks in Korea have been engaged in foreign currency lending business to Korean corporations and banks, which was funded by their parent offices. Since the share of foreign bank has been too minor to bring about serious changes in charter values of Korean banks and the competitive environment of the Korean banking sector, we focused on their behavioral patterns. We found that their foreign currency lending was neither pro- nor counter-cyclical in contrast to their Korean currency lending which was pro-cyclical. Also interestingly, foreign currency lending of Korean banks turned out to be pro-cyclical.

Foreign banks in Korea were able to provide rather stable foreign currency lending service irrespective of macroeconomic fluctuation of the Korean economy. Foreign banks have more cushions to absorb cyclical shocks specific to the Korean economy than Korean banks. Hence, we argue that allowing commercial presence of foreign banks should be expected to be beneficial in this regard.

It is too early to make a comprehensive assessment of the impact of the liberalization of banking service. However, we conjecture that the ongoing restructuring and entry of foreign banks will make the domestic banks more competitive. In order to survive, management should be independent and efficient. In other words, The Korean banking services should establish the responsible management system and asset soundness. Also, financial infrastructure should be established through improvements in accounting, credit ratings and payment system. The range of banking services needs to be enlarged through development of various products and management skills, along with M&As and joint business with other banks. Consistent market liberalization will more rapidly drive financial globalization. This will lead to the advanced financial institutions as in developed countries.

Contents

I. Introduction

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On the 21st century, the financial industry will have achieved a unified international financial market, due to international financial liberalization and cross-border services under the WTO New Round. With more competition and removal of entry barriers in the international financial market, developed countries have promoted M&As in the financial industry and universal banking system.

After financial crisis, the financial development in banking sector is a very important and urgent task for Korea and other crisis-stricken Asian countries. The banking system plays a key role in the functioning of a market economy. How well developed the banking system is seems to have an important role on resource allocation and economic growth.

This paper discusses the liberalization of banking services and its impact on the Korean economy. It focuses on banking services because banks occupy the central position in the financial sector. The purpose of this paper is to provide the useful implication on the following question in Korea: Whether lending behaviors of foreign banks in Korea were different from those of domestic banks in terms of business cycles?

This paper is organized as follows. Following the introduction, Chapter 2 reviews Korea's liberalization of banking service and discusses the deregulation of financial market and cross-border trade, commercial presence in the banking sector. Chapter 3 deals with the behavior of foreign banks in terms of asset and liability composition. This paper briefly discusses the costs and benefits of liberalization on banking sector and analyzes the cyclical property of foreign banks in Chapter 4.

II. Review of Liberalization of Banking Sector in Korea

The 1997 economic crisis brought about fundamental changes in various aspects of economic policy in Korea including the banking services. Regarding the policy stance toward banking services, the crisis stands as an important moment. It transformed the policy stance from lukewarm to fully open. Therefore, the liberalization of banking sector deals with two modes of cross-border and commercial presence, distinguishing the pre-crisis from the post-crisis period.[1]

1. Liberalization in the Pre-crisis Period

A. Cross-Border Trade

Before the crisis, the policy on cross border trade was not made on its own merit but was decided as a by-product of capital account liberalization policy, and cross border trade in financial services was not bound in the GATS. Specifically, for the banking sector the cross-border trade was not allowed (and still is not) under the banking law, which followed a positive system and had no provisions regarding cross-border trade. Only limited cross-border trade was allowed under the Foreign Exchange Management Act. In fact, cross-border trade has taken place as a part of permitted capital transactions.

With respect to capital account liberalization, the policy stance was dictated by the concerns about the current account balance. This was because exchange rates were under discretionary control of policy makers as in other developing countries. In the absence of equilibrating forces through exchange rate adjustment, accommodation of current account balances naturally called for policy intervention. Under the circumstances, the Korean government was cautious in introducing policy measures that might have entailed significant changes in capital flows. In particular, when current

[1] GATS identifies four different modes of trade. In the first two modes the provider of services stays home. In Mode 1 (cross-border), the service is delivered across borders to consumers in the trade partner country; in Mode 2 (consumption abroad), consumers come to the service provider. In the other two modes the service providers come to the country of the consumers. And, in Mode 3 (commercial presence), the providers establish a branch or subsidiary; in Mode 4 (presence of natural person), the providers are natural persons. The balance of payments statistics covering the transactions between residents and nonresidents, leaves out Mode 3, which is the main mode of financial service trade.

account recorded chronic deficits as in the 1990s, it was reluctant to take measures which would allow more capital outflows.

Hence, any kind of cross border trade that would lead to capital outflows was not allowed, and liberalization began in areas where capital inflows rather than outflows would follow. Moreover, even with those areas the extent of liberalization differed according to concerned agents. Cross-border trade by individuals was left closed. Only cross border trade by the corporate sector and the financial sector that would incur more capital inflows was liberalized. That is, foreign currency borrowing by the corporate and the financial sector, and portfolio investment by foreigners were the only transactions considered. In addition, various quantity restrictions were attached to these partial liberalization measures.

With respect to portfolio investment, a significant step was taken in 1991. Effective from January 1992, foreigners were allowed to purchase Korean stocks up to 3 percent of the outstanding shares of each company for each individual, with the provision that no more than 10 percent of a company could be owned by foreigners. Only foreign currency denominated debt instruments were liberalized. Overseas issuance of foreign currency denominated bonds by domestic firms was deregulated in 1991, but the government exerted discretionary quantity controls. Also, commercial loans from foreign financial institution by the corporate sector were allowed in 1995, but restrictions on the uses of funds remained and government approval was required. Among capital transactions by the corporate sector, the trade related short-term financing was relatively free. The restrictions on deferred import payments and receipt of advance payments for exports were lifted step by step without additional discretionary control throughout the 1990s.

Relative to the corporate sector or individuals, the government allowed banks to enjoy more freedom in borrowing from foreign banks. Foreign borrowing by banks was allowed throughout the 1990s and no explicit quantity restrictions were imposed. Though it was known that the government exerted informal control in the early 1990s, the unofficial guidance disappeared in 1994. Accordingly, in terms of cross border trade, foreign currency borrowings by the corporate and financial sector were partially open.

B. Commercial Presence

In the early 1980s when the current account was still in chronic deficit, the Korean government allowed a number of foreign banks to enter the Korean market in order to help attract foreign capital. However, they were allowed to open only branches but not subsidiaries, and throughout the 1990s little change was made regarding the commercial presence of foreign banks in Korea. In the case of securities companies, the government authorized operation of foreign companies in 1992 when the Korean stock market was opened partially, but again they were permitted to open only branches.

Regarding commercial presence, a potentially important development occurred in 1996 on Korea's accession to the OECD. In order to fulfill its obligations as a member of the OECD, the Korean government announced in September a blueprint that gradually remove barriers to foreign portfolio investment and foreign direct investment in financial services from OECD countries. The following summarizes the 1996 OECD commitments:

- Foreign banks and securities firms from OECD countries would be permitted to establish subsidiaries in Korea by 1998.
- Aggregate foreign investment ceilings for investors from OECD countries were scheduled to be phased out by 2000.
- Foreign investors from OECD countries would be allowed to establish and hold 100 percent ownership of any type of financial institution by December 1998.
- Foreign investment consulting firms from OECD countries would be able to offer their services without establishing a commercial presence in Korea.

However, the actual liberalization process of the banking service sector was accelerated by the unexpected events of the 1997 crisis.

2. Liberalization in the Post-crisis Period

A. Deregulation of Financial Markets

The liberalization of banking services is closely related to capital movements. Deregulation of financial markets establishes grounds for the liberalization of banking services.

1) Domestic Stock and Bond Markets

In order to promote inflows of foreign capital, Korea opened its domestic bond market at the end of 1997 and proceeded to complete the opening of the domestic stock and money markets. Ceilings on stock investment by foreigners were completely lifted in May 1998 with the exception of investment in state-owned enterprises as shown in Table 1.

Table 1. Gradual Repeal of Limits on Stock Investment by Foreigners

(unit: %)

Date	Non State-Owned Companies	State-Owned Companies
January 1992	10	8
December 1994	12	8
July 1995	15	10
April 1996	18	12
October 1996	20	15
May 1997	23	18
November 1997	26	21
December 1997	55	25
May 1998	100	30

Source: Financial Supervisory Service

The trading of the corporate bond and government bond was completely opened to foreigners at the end of 1997 as shown in Tables 2 and 3. Foreign investment in the bonds of non-listed companies was allowed in July 1998. The markets for commercial papers (CP) and certificates of deposit (CD) were partially opened in February 1998 and were completely opened in May 1998. In addition, restrictions on investment in domestic securities by foreigners have been eliminated along with the requirement that domestic subsidiaries of foreign companies should obtain government approval when introducing more than $1 million from abroad.

Table 2. Opening of the Bond and Money Markets

Date	Instruments
July 1994	Non-guaranteed convertible bonds issued by small and mid-size companies
June 1997	Non-guaranteed convertible bonds issued by large companies, and non-guaranteed bonds issued by small and mid-size companies
December 1997	Corporate bond and government bond
February 1998	CPs and trade-bill
May 1998	All money market instruments including CDs and Repos

Source: Ministry of Finance and Economy

Table 3. Liberalization of Bond Markets

				Jul. 1994	Jan. 1997	Jun. 1997	Nov. 1997	Dec. 12, 1997	Dec. 23, 1997	Dec. 30, 1997	May 25, 1998	Jul.1998
Corporate Bonds	SMEs	NG	Straight	X	X	Aggregate 50%	⇒	No limits				
			CB	Aggregate 30% (individual 5%)	Aggregate 50% (individual 10%)	⇒	⇒	No limits				
			BW, EB	X	X	X	Aggregate 50% (individual 10%)	No limits				
		G	-	X	X	X	X	Aggregate 30% (individual 10%)	Aggregate 30%	No limits		
	Large Enterprises	NG	Straight	X	X	X	X	Aggregate 30% (individual 10%)	Aggregate 30%	No limits		
			CB	X	X	Aggregate 30% (individual 5%)	⇒	Aggregate 50% (individual 10%)	Aggregate 50%	No limits		
			BW, EB	X	X	X	X	Aggregate 50% (individual 10%)	Aggregate 50%	No limits		
		G	-	X	X	X	X	Aggregate 30% (individual 10%)	Aggregate 30%	No limits		
Government Bond				X	X	X	X	X	Aggregate 30%	No limits		
Listed Bond Over-the-Counter Trading				X	X	X	X	X	X	X	Allowed	
RP Trading				X	X	X	X	X	X	X	Allowed	
Non-Listed Bond				X	X	X	X	X	X	X	X	Allowed

Note : NG and G stand for non-guaranteed and guaranteed bond, respectively. X denotes ‘not allowed’ and ⇒ ‘same as before’. CB, BW and EB stand for convertible bond, bond with warranty and Eurobond, respectively.

Source: Financial Supervisory Service

2) Foreign Exchange Market

As of July 1998, the government lifted the freeze on medium-term foreign loans in order to reduce the burden on businesses seeking foreign capital. The requirement that commercial borrowing from abroad should exceed $1 million was eliminated as well. Furthermore, the restrictions on the types of goods and duration of credit were also relaxed for import and export credits.

In April 1999, Korea abolished the restrictive "Foreign Exchange Management Act" and replaced it with the "Foreign Exchange Transaction Act". The allowed capital transactions are as follows:

- Offshore issuance of securities and foreign borrowing with a maturity of less than one year
- Offshore investment in foreign financial markets, foreign insurance markets and foreign real estate markets by domestic firms and financial institutions
- Establishment of domestic savings deposits (including trust deposits) with a maturity in excess of one year by nonresidents
- Issuance of won-denominated (maturities over one year) and foreign-currency-denominated securities by nonresidents
- Transactions of derivatives through domestic financial institutions

From 2001, foreign exchange transactions by individuals such as won-based domestic deposits with maturities of less than one year by nonresidents will be liberalized. The government will also allow individuals to freely deposit their money in foreign-based banks, buy foreign securities and foreign real estate. At this stage, the level of liberalization in Korea will be close to that of the OECD countries.

B. Deregulation of the Banking Service

1) Cross-Border Trade

Cross-border Trade is gaining popularity in WTO negotiation. The global financial market has undergone dramatic changes in recent years, characterized by the integration of financial markets, increasing cross-border flows of capital and deepening interdependency among financial markets. Furthermore, advances in information technology have not only led to the proliferation of cyber banking but also have brought new high-tech financial products into the market. Korea has greatly liberalized its market to draw foreign investment and competition under the principle of national treatment. However, the cross-border trade in financial services is mostly prohibited by relevant laws. Especially, the banking law in Korea deals with only commercial presence, not cross-border trade. Since the banking law in Korea follows a positive system, cross-border trade in the banking sector is not allowed. Although cross-border trade is prohibited by the current banking law, the Foreign Exchange Transaction Act allows limited cross-border trade. Therefore, the cross-border trade in banking sector is still partially opened.

The cross-border trade in the securities sector is not allowed since domestic securities law allows trading only through commercial presence in Table 4. For investment trust companies (ITC), mutual funds are allowed to trade without commercial presence. Therefore, the cross-border trade in ITC is partially opened. The provision of advisory and agency services on a cross-border basis has been permitted since December 1998. The cross-border trade in life insurance service has been liberalized. For example, cross-border reinsurance was fully liberalized in April 1998. However, non-life insurance services are still reserved for only resident insurance companies, except for marine export/import cargo, aviation and hull insurance.

Table 4. Liberalization of Financial Institutions as of 2000

	Bank	Security	Investment Trust Company	Investment Advisory	Life Insurance	Non-Life Insurance
Branch	Open	Open	Open	Open	Open	Open
Subsidiary	Open	Open	Open	Open	Open	Open
Joint Venture	Open	Open	Open	Open	Not Open	Not Open
Cross-Border Trade	Partially Open	Not Open	Partially Open	Open	Open	Aviation, Hull (open)

Source: Korea Institute of Finance (2000), "Main Issues in International Financial Market"

In order to prepare for liberalization in cross-border trade in financial services, a mechanism to protect customers and investors is needed. Domestic prudential regulation will be very difficult, especially related to e-commerce transactions. Therefore, reinforcement of supervisory functions and systematic preparation is necessary.

2) Commercial Presence

Important steps regarding commercial presence were taken in the spring of 1998 to increase foreigners' access to the financial sector in Korea. The authorization of foreign banks and securities firms to establish subsidiaries started from April 1998, as shown in Table 5. In addition, 100 percent foreign ownership of Korean institutions was allowed in the same month and foreign nationals were allowed to become directors of Korean banks in May.

The branch of a foreign bank is treated as an independent financial institution. Its operations are similar to those of subsidiaries of foreign banks, including retail businesses. There are no restrictions on establishing subsidiaries of foreign banks in Korea. The establishment of a new commercial bank, whether domestic or foreign-owned, requires only the permission of the Financial Supervisory Commission (FSC). The minimum capital required is 100 billion won for establishing a nation-wide commercial bank and 25 billion won for a regional bank. In addition, foreign banks in Korea have been allowed to have local branches in the domestic market since March 1998. However, the foreign exchange position is still regulated: the maximum allowed oversold position spot foreign exchange is $ 5 million or 3 percent of capital, whichever is greater.

For the ownership of banks, the prior limits of 4 percent in a nation-wide bank, 8 percent in a bank converted from other financial sector institutions and 15 percent in a regional bank were mitigated by allowing the acquisition of shares in excess of those limits with approval from, or prior notice to, the FSC. Foreign ownership of up to 100 percent was permitted in April 1999, although subject to additional review by the FSC in line with the increase in stakes beyond certain predetermined thresholds. Also, laws were enacted to strengthen the power of boards of directors of banks and to enhance transparency in dealings with shareholders. Foreigners have been permitted to become directors of bank boards since May 1998. Therefore, any foreign bank meeting the conditions, which are applied equally to domestic banks, is allowed to enter the market.

There were 61 branches of foreign banks and 26 foreign representative offices as of the end of December 1999. The foreign shares of domestic banks as of the end of 1999 are shown in Table 6. The Korea First Bank was sold in September 1999 to New Bridge Capital of the U.S. and foreigners are participating in the management of Housing & Commercial Bank, KorAm Bank and Foreign Exchange Bank.

Table 5. Liberalization of Foreign Participation in the Korean Financial Sector

Equity Participation in Existing Korean Institutions	Subsidiary	Branch	Representative Office
Regional Commercial Bank, no need to report for up to 15%; Commercial Bank, no need to report for up to 4% and must report to Financial Supervisory Commission for share between 4% and 10%. FSC approval required each time share exceeds: 10%, 25% and 33%	No restrictions as of April 1998	No restrictions since the General Banking Act was enforced in 1954	No restrictions since the General Banking Act was enforced in 1954

Table 6. Foreign Shares of Domestic Banks as of the end of 1999

(unit: %)

Bank	Government Share	Major Foreign Investor
Cho Hung	80.05	-
Hanvit	74.65	-
Korea First	49.00	New Bridge(51%)
Seoul	95.68	-
Korea Exchange	35.92	Commerz Bank(23.6%)
Kookmin	6.48	Goldman Sachs(18%)
Korea Housing & Commercial	14.50	ING Group (10%)
Shinhan	-	Korea-Japan (49.43%)[1)]
KorAm	-	BOA(16.8%)
Hana	-	IFC(3.3%)
Peace	-	-

Note: 1) as of April 12, 2000
Source: Financial Supervisory Service

Table 7 shows Korea's WTO commitment in Banking Business in terms of cross-border trade and commercial presence. However, Korea imposes the foreign bank capital restriction not based on the parent bank but the local bank. The reason for this is that parent banks are located outside the jurisdiction of the Korean supervisory authority. If parent banks were to be liquidated or bankrupt, it would be highly difficult for domestic depositors to be insured. Moreover, this regulation is fully in line with the Basle Core Principles for Effective Banking Supervision, which allows for prudential regulation of foreign banks branches based on the circumstances of the host countries' financial institutions. Therefore, in order to protect depositors, Korea allows the capital of branches of foreign banks to be based on local not parent banks. This is similar to the systems used in Germany, Turkey and Singapore.

Table 7. Korea's WTO Commitment in Banking Business as of April 1999

(cross-border supply, commercial presence)

Limitations on Market Access	Limitations on National Treatment
Cross-border supply	***Cross-border supply***
Unbound	Unbound
Commercial presence	***Commercial presence***
- Horizontal limitations on banking services	None
Commercial presence is permitted only for foreign banks. Foreign banks are allowed to establish subsidiaries in Korea, either through new establishment or through the acquisition of an existing bank. A person may own up to 4 percent of the stocks of a bank and 15 percent of the stock of a provincial bank without the special authorization of the relevant authorities.	
The foreign exchange position is regulated.	
The oversold position of spot foreign exchange is $5 million or 3 percent of capital, whichever is greater.	
- Limitation on Deposit and Related Services	
The maturity of CDs shall be more than 30 days.	
Deposits for specific purposes, such as housing subscription deposits, may be handled only by designated institutions.	
- Limitations on loan and related services	
Foreign currency loans are restricted with respect to ceiling and uses.	
Mandatory lending to small and medium-sized companies is required.	
- Limitations on foreign exchange services	
Underlying transaction and documentation requirements apply to foreign exchange transactions.	
Underlying documentation requirements are not applied in the case of forward transactions.	
- Limitations on trust services	
Real estate trust business is prohibited.	
To handle a trust business, approval (two types) is required from the Ministry of Finance and Economy both for engaging in businesses other than the main banking businesses and for engaging in the trust business.	

III. The Characteristics of Foreign Bank Operation

1. Domestic Banks

Before the financial crisis, the domestic financial banking operated under government regulation and protection. However, Korean banks have faced a great challenge since the government started the drive for restructuring after the crisis. The government-led restructuring aimed to recover stability in the financial system and promote soundness and efficiency in banking institutions. M&A and liquidation began in June 1998 with five insolvent banks; a large amount of public fund has been put into banking institutions that were deemed viable. In addition, management reform carried out as such that it would boost profitability, and international supervisory standards were introduced. The recent financial reforms focus on the promotion of financial soundness.

Such banking restructuring indicates that the Korean government recognized the limitations of the domestic financial system and shifted the reform measures to meet global standards. The Korean government is actively following international trends such as deregulation, liberalization and prudential supervision. The Korean financial industry has a significant influence on corporate business. As of the end of 1999, the financial industry comprised 7.8% of GDP, as shown in Table 8.

Table 8. Weight of the Financial Industry in GDP

(unit: billion won)

Year	Financial Industry	GDP	Weight (%)
1995	24,763.3	377,349.8	6.6
1996	27,990.7	418,479.0	6.7
1997	29,897.6	453,276.4	6.6
1998	30,348.3	444,366.5	6.8
1999	37,907.1	483,777.8	7.8

Source: Bank of Korea

However, banking institutions have too many nonperforming loans(NPLs). As of the end of 1999, those insolvent loans were calculated at 5.13 billion won. This figure is down from September 1999, but is still high. With the "Forward Looking Criteria", those NPLs are estimated at around 6.67 billion won. The problem in the Korean financial banking sector lies in the absence of managerial transparency and independence. Accordingly, undesirable practices such as loans with collateral and compensating deposit have not been substantially reduced. As of the end of 1998, collateral loans in domestic banks occupied 60.8 percent of total loans, which is much higher than 37.4 percent for U.S. commercial banks and 51.7 percent for foreign banks in Korea (See Table 9).

Table 9. Type of loan (as of the year-end)

(unit: %)

	1996	1997	1998		
			Domestic banks	Foreign banks	U.S. banks (as of January 1999)
Total lending					
Collateral-lending	58.4	58.7	60.8	51.7	37.4
(guarantee-lending)	(9.4)	(10.6)	(16.0)	(29.8)	(−)
Credit-lending	41.6	41.3	39.2	48.3	62.6
Loans to SME					
Collateral-lending	64.1	66.4	67.5	-	-
Credit-lending	35.9	33.6	32.5	-	-

Source: Bank of Korea

Federal Reserve Bank, 1999, *Survey of Terms of Business Lending*

2. The Performance of Foreign Banks[2]

A. Foreign Penetration

Branches of foreign banks in Korea steadily increased over fifteen years from the

[2] In this paper, "foreign banks in Korea" means Korean branches of foreign banks. Korea did not allow full penetration of foreign banks before the crisis of 1997 and so, the definition comprises all the banks in Korea over which the controlling authority was exercised by foreign banks. It may be necessary to emphasize that such banks as Shinhan and KorAm, where foreign ownership has been considerable, will not be considered as "foreign banks" in this paper. Foreign ownership or investment in Korean banks has been accelerated after the crisis of 1997 and naturally, attention to possible impacts of foreign ownership has been increasing. We choose to separate this issue from the penetration of foreign banks into the Korean banking sector.

late 1970s to the 1980s, from 9 in 1975 to 69 in 1990, as shown in Table 10. However, opening of branches of foreign banks became sluggish thereafter. In fact, the number of branches in operation declined to 66 in 1998. The stagnant pattern cannot be solely attributed to the eruption of the financial crisis in 1997, since the net decrease in the number of branches had already begun in 1994.

Table 10. Branches of Foreign Banks in Korea

Year		'67-'75	'76-'80	'81-'85	'86-'90	'91	'92	'93	'94	'95	'96	'97	'98	Sub-total
Branches	Newly opened	9	24	20	24	6	5	2	1	-	-	5	2	98
	Closed	-	-	1	7	5	2	1	3	1	4	4	4	32
	Subtotal	9	24	19	17	1	3	1	(2)	(1)	(4)	1	(2)	66
Repre-sentative Offices	Newly Opened	9	17	17	13	5	2	4	-	2	1	3	2	85
	Closed	2	5	16	19	6	2	3	1	-	2	4	2	17
	Subtotal	7	12	1	4	(1)	-	1	(1)	2	(1)	(1)	-	23
Total		16	36	20	21	-	3	2	(3)	1	(5)	-	(2)	89

Source: Financial Supervisory Service, *Bank Management Statistics*, Various Issues.

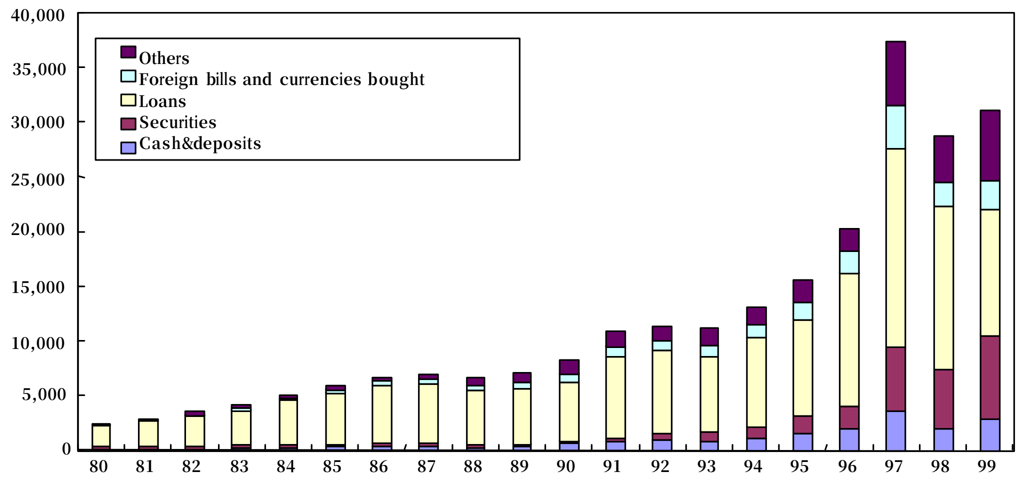
Over the past two decades, foreign banks in Korea have grown by 15.5 percent on average each year. Solid as the overall growth was, the pace of growth each year was rocky. During the early 1980s, foreign banks in Korea displayed strong asset growth, recording a growth rate of 24.3 percent on average, outpacing the 16 percent growth for Korean banks. However, the pace of growth slowed down to 9.4 percent in the late 1980s and 6.4 percent in the early 1990s. In fact, foreign banks in Korea even showed negative growth in 1992 and 1993. However, foreign banks in Korea have resumed growth since 1994, and for the four years from 1994 to 1998 the average growth rate reached 22.3 percent.

B. Asset Composition

The asset composition of foreign banks displayed three features. First, before the crisis, loans were the dominant component of total asset, though their share was in decline as shown in Figure 1. In the early 1980s, loans accounted for 79 percent of total

Figure 1. Asset Composition of Foreign Banks in Korea

(unit: billion won)



Source: Bank of Korea, *Monthly Bulletin*, Various Issues.

Table 11. Asset Composition of Foreign Banks in Korea: Average Shares

(average, %)

	1981-1985	1986-1990	1991-1995	1996	1997	1998	1999
Deposits	5.4	5.7	8.6	10.0	9.6	7.1	9.3
Securities	5.8	3.7	6.3	10.1	15.7	18.9	24.5
Loans	78.8	73.5	63.1	60.5	48.5	51.8	37.2
Foreign bills & currencies bought	3.6	7.8	9.2	9.8	10.4	7.9	8.3
Others	6.4	9.3	12.7	9.6	15.9	14.4	20.7
Total	100	100	100	100	100	100	100

Source: Bank of Korea, *Monthly Bulletin*, Various Issues.

assets, falling to 61 percent in 1996 as shown in Table 11. Second, before the crisis, foreign banks' share of trade financing increased steadily, rising from 3.6 percent in the early 1980s to 9.8 percent in 1996.

Third, the crisis set off dramatic changes. The share of loans decreased drastically to 37 percent in 1999. The reduction is due to an increase in holdings of securities and "others" which include call loans. In particular, it seems that foreign banks increased investment in government bonds and monetary stabilization bonds.[3]

The largest component of loans is composed of three factors: domestic currency loans to corporations, foreign currency loans to corporations and foreign currency loans to banks (namely, interbank foreign currency loans). Hence, two groupings are possible: one by currency and the other by borrowers and three characteristics can be found.

First, foreign currency loans have been the leading component for most of the last two decades in Figure 2. Domestic currency loans expanded robustly until 1990, exceeding the growth rates of foreign currency loans. In consequence, its shares steadily rose from 35.8 percent in 1981 and reached 55.7 percent in 1988, outweighing foreign currency loans. The dominance of domestic currency loans continued in the following years, recording a high of 58.1 percent in 1990. Thereafter the trend turned around and foreign currency loans began reclaiming its share, rising to over 70 percent for the years before the crisis as shown in Table 12.

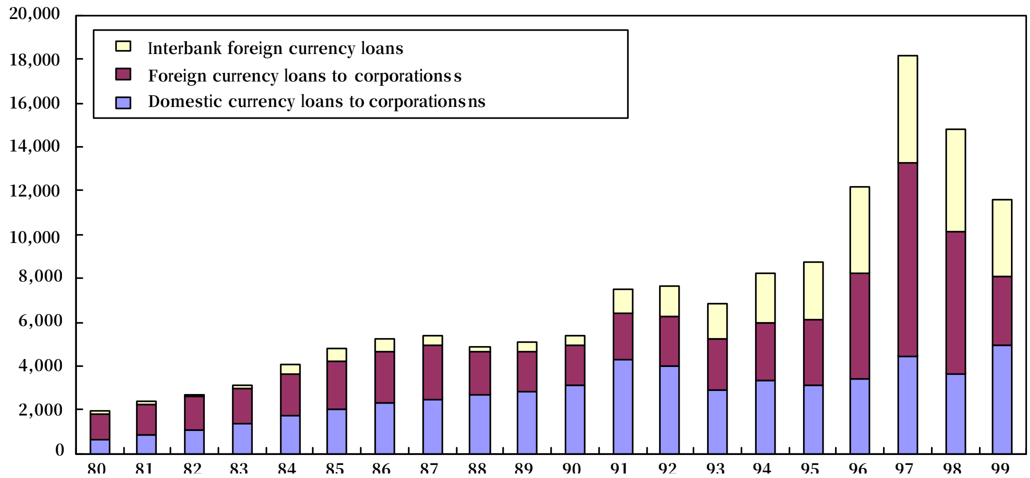
Second, though corporations have always been the leading borrowers, borrowings of Korean banks from foreign banks in Korea increased noticeably in the 1990s. The share of interbank loans, which remained below 10 percent in the 1980s, rose to over 30 percent in the late 1990s (See Table 13).

Third, an interesting change took place after the crisis. Both foreign currency loans to corporations and banks shrank considerably, dragging down total loans. In contrast, domestic currency loans increased from 4,480 billion in 1997 to 4,954 billion won in 1999.

[3] Investment in government bonds increased from 397 billion won in 1998 to 1,022 billion won in 1999. Investment in "unspecified" securities also increased from 2,500 billion won to 3,969 billion for the same period. Most of the increase is known to be enlarged holdings of monetary stabilization bonds.

Figure 2. Loan Composition of Foreign Banks in Korea

(unit: billion won)



Source: Bank of Korea, *Monthly Bulletin*, Various Issues.

Table 12. Loan Composition of Foreign Banks in Korea (by Currency)

(average, %)

	1981-1985	1986-1990	1991-1995	1996	1997	1998	1999
Won	40.8	52.1	45.7	28.1	24.7	24.7	42.9
Foreign currency	59.2	47.9	54.3	71.9	75.3	75.3	57.1
Total	100	100	100	100	100	100	100

Source: Bank of Korea, *Monthly Bulletin*, Various Issues.

Table 13. Loan Composition of Foreign Banks in Korea (by Borrowers)

(average, %)

	1981-1985	1986-1990	1991-1995	1996	1997	1998	1999
Banks	6.9	7.8	22.5	32.2	26.7	31.6	29.9
Corporations	93.1	92.2	77.5	67.8	73.4	68.4	70.1
Total	100	100	100	100	100	100	100

Source: Bank of Korea, *Monthly Bulletin*, Various Issues.

C. Liability Composition

There are about six funding sources for foreign banks in Korea. Interoffice borrowings, foreign currency deposits and foreign currency borrowings are made for mobilizing foreign currency funds. For domestic currency funding, capital, deposits and call money (classified as "others") have been rendered available. Examining the composition of these factors in the past decades reveals the following three features.

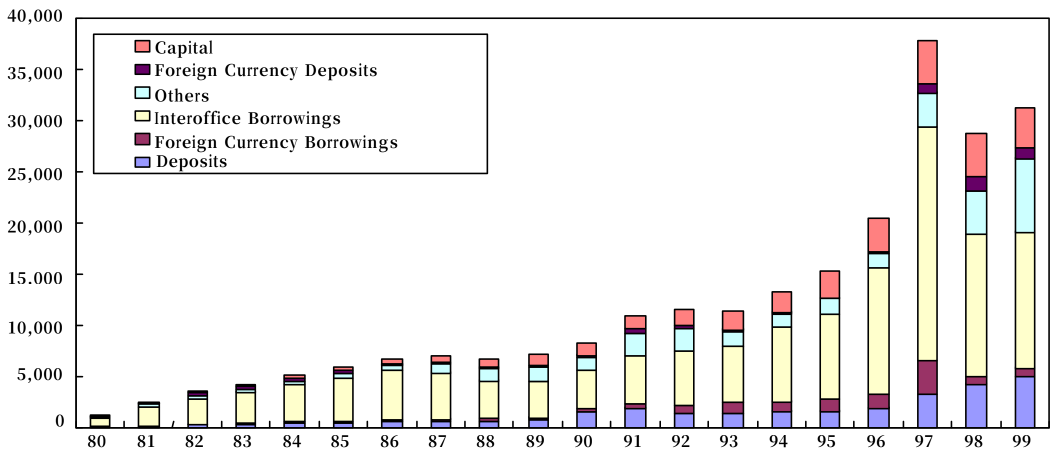
First, as to foreign currency funding, interoffice borrowings have always been the dominant source, as shown in Figure 3. Foreign currency deposits and borrowings remain minor throughout the period. In fact, interoffice borrowings have taken the largest share, even when foreign currency and domestic currency funds are combined.

Second, with respect to domestic currency funding, capital and deposits have been equal sources, exhibiting similar movements over the time.

Third, trend in the composition of foreign currency funding and domestic currency funding displays the same pattern found in the asset composition. In the 1980s, foreign currency funding was dominant, accounting for about 80 percent of total liabilities as shown in Table 14. Growth of foreign currency funding was relatively slow in the early 1990s, its share decreasing to about 58 percent. Thereafter, foreign currency funding recovered and its share rose to around 70 percent in 1996 and 1997 until the crisis. After the crisis, however, interoffice borrowings have been decreasing in absolute value while domestic currency deposits have been increasing, causing a drastic reduction in the share of foreign currency funding to about 49 percent in 1999.

Figure 3. Liability Composition of Foreign Banks in Korea

(unit: billion won)



Source: Bank of Korea, *Monthly Bulletin*, various issues.

Table 14. Liability Composition of Foreign Banks in Korea: Average Shares

(Average, %)

	1981-1985	1986-1990	1991-1995	1996	1997	1998	1999
Deposits	6.9	10.8	12.9	9.3	8.6	14.8	16.0
Foreign Currency Deposits	5.2	2.3	2.0	0.5	2.3	5.0	3.4
Foreign Currency Borrowings	2.1	3.2	6.7	6.8	8.6	2.6	2.70
Interoffice Borrowings	72.5	58.1	49.5	60.3	60.5	48.5	42.6
Others	7.8	15.2	14.5	7.2	8.8	14.5	23.1
Capital	5.4	10.4	14.5	15.9	11.2	14.6	12.2
Total	100	100	100	100	100	100	100

Source: Bank of Korea, *Monthly Bulletin,* various Issues.

D. Profitability

Throughout the 1990s, for which official data are available, foreign banks in Korea outperformed Korean banks by considerable margins. From 1993 to 1999, average ROA and ROE of foreign banks in Korea were 1.76 percent and 14.59 percent, respectively (See Table 15). On the contrary, those of Korean banks were –0.59 percent and –9.98 percent, respectively. Of course, the poor performance is partly due to the financial crisis and later effects. However, it is notable that even in the early 1990s the profitability of Korean banks was quite lower.

Table 15. Profitability of Foreign Banks in Korea

(unit: %)

	1993	1994	1995	1996	1997	1998	1999
ROA	1.21 (0.62)	1.39 (0.62)	1.24 (0.38)	1.61 (0.32)	4.00 (-1.06)	1.78 (-3.61)	1.08 (-1.42)
ROE	9.55 (5.90)	10.96 (6.09)	10.28 (4.19)	12.51 (3.80)	34.79 (-14.18)	14.82 (-52.53)	9.22 (-23.13)

Note: Numbers in ( ) are those of Korean commercial banks.
Source: Financial Supervisory Service, *Bank Management Statistics,* Various Issues.

3. Evaluation

Based on the descriptive analysis in previous pages, it can bee seen that despite a long presence of over twenty years, foreign banks have yet to take roots in Korea's financial market as "banks". We note the following two points.

First of all, their major funding sources have been interoffice borrowings and capital, implying heavy reliance on home bases. Reflecting this, local funding has always been minor. Deposits taken in the Korean currency were always minor, hovering around 10 percent on average. The picture remains the same, even when foreign currency deposits are taken into account. Deposits played a very limited role as a funding source, irrespective of the type of currency. Second, as a result, operation in foreign currency has been a dominant part of business. Focusing on lending, the historical average of foreign currency loans over the last two decades comes close to 60 percent and there is no clear sign of change yet.

In sum, the banking services through "commercial presence" in Korea was not much different from "cross-border" trade. It only facilitated capital inflows into the Korean economy, rather than allowing foreign intermediaries to fully participate in the Korean financial market. Given the limited localization of foreign banks, it may not be surprising to observe their overperformance compared to Korean banks. After all, foreign banks must have been in a position to take advantage of interest rate differentials between their home countries and Korea.

IV. Effect of Foreign Entry

1. General Discussion

This chapter discusses the impact of the liberalization of banking services, comparing the benefits of banking services to those of goods trade and what it takes for the liberalization to succeed in realizing the benefits.

Banking industry of Asian countries was hardly opened, causing great inefficiency. Financial institutions were slow to develop, vulnerable to external shock, and they incurred high cost. Banks offer many different kinds of business services such as accepting deposits, lending, underwriting and brokerage, at various rates and fees. In doing so, they perform five basic functions, according to Levine

(1996): to facilitate the exchange of goods and services; to facilitate risk management; to mobilize resources; to obtain information, evaluate firms, and allocate capital; and to provide corporate control. Obviously, these are critical functions in the working of a market economy, and the externalities involved in the provision of financial services are substantial.

In addition, financial opening would lead Asian countries to deliver public finance to more productive investment. Asian countries generally show high savings rates; financial opening will prevent any government-led nontransparent investment, as happened with the absence of proper international regulatory institution.

Table 16. Benefits and Costs of Foreign Bank Entry

Benefits	Costs
- facilitate the exchange of goods and services - Facilitate risk management - Mobilize resources - Evaluation of firms - Provide corporate control	- Short-term rise in unemployment - Possible dominance of foreign banks - More influence of foreign capital on domestic market - Intervention in domestic corporate management

There are certainly possible negative effects such as increase in unemployment, higher foreign capital occupancy of the local market, more influence of foreign capital on domestic market and intervention in domestic corporate (See Table 16). As seen from Table 17, local banks are in the process of reducing the number of branches and personnel in Korea. Kookmin Bank and Housing & Commercial Bank show that their branches increased in number since these two banks merged with other banks in 1998. Korea First Bank laid off more than 200 employees in the first half of 2000. Accepting recommendations from Goldman Sachs, its largest shareholder, Kookmin Bank will lay off more than 1,000 employees. The profit rate of Korea First Bank, recently acquired by New Bridge Capital, sharply increased from -7.94 percent at the end of 1998 to -3.21 percent at the end of 1999.

Table 17. Restructuring of Domestic Banks

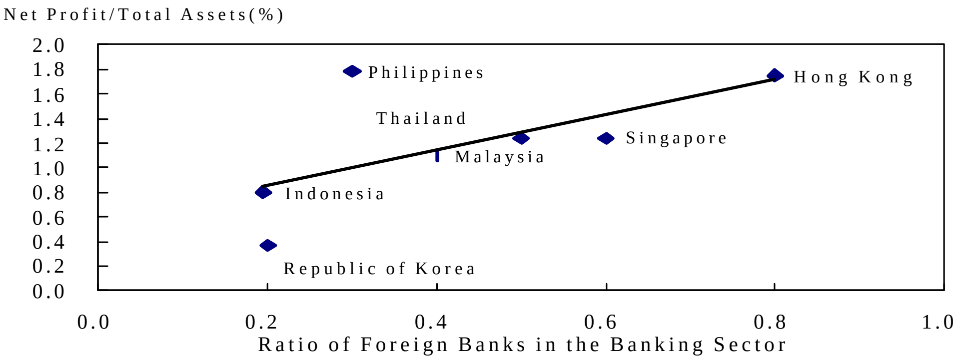
Year	Category	Domestic Banks			
		Korea First	Foreign Exchange	Kookmin	Housing & Commercial
1997	Number of employees (persons)	7,990	8,705	13,515	12,195
	Number of branches (units)[1]	413	400	511	499
	Profit rate (%)[2]	-4.61	-0.15	0.31	0.36
1998	Number of employees (persons)	4,870	5,910	11,230	8,538
	Number of branches (units)[1]	339	326	546	545
	Profit rate (%)[2]	-7.94	-1.85	0.16	-0.68
1999	Number of employees (persons)	4,815	5,747	11,453	8,973
	Number of branches (units)[1]	335	280	587	537
	Profit rate (%)[2]	-3.21	-1.80	0.16	1.02

Note: 1) The number of branches include the number of local offices and branches.
2) Profit rate is based on ROA.

Source: Financial Supervisory Service

The possible negative effects from the entry of foreign financial institutions can be offset or at least minimized if local financial institutions are able to embrace advanced management techniques and compete fairly. Singapore already removed limitations on foreign investment in local banks and introduced various incentives for foreigners including tax benefits. As a result, foreign financial participation in Singapore is outstanding; there are 140 foreign banks in Singapore, compared to 10 local banks. This fact made an appeal to Southeast Asian branches of foreign financial institutions and brought them from Hong Kong to Singapore. In 1999, the total sum of foreign exchange trade in Singapore amounted to $14 billion, the fourth most active market in the world; it is already ahead of Hong Kong.

Figure 4. Relation between Foreign Banks Entry and Net Profit (1995)



Source: Claessens and Glaessner. 1998. "Internationalization of Financial Services in ASIA" World Bank.

Clasesens and Glaesser (1998) indicated that the profitability of financial institutions has a positive relation with the degree of market opening (See Figure 4). They argue that the incentives to diversity and provide a wider range of noninterest related products and services increase where there are more foreign banks. In the Case of Argentina, Clarke, Cull, D'Amato and Molinari (1999) showed that foreign banks entered specific areas where they have a comparative advantage, putting pressure on the domestic banks already focusing on those types of lending. Foreign financial institutions concentrated on mortgage lending, where they had comparative advantage. This brought keen competition among the mortgage lending firms and increased indirect costs. Profitability of local financial institutions plummeted and, accordingly, short-term negative effects from financial opening appeared.

On the other hand, the entry of foreign financial institutions helped consumers enjoy various service benefits, since foreign financial institutions offered diverse financial services, which local firms were not able to. Moreover, as local financial institutions had a chance of acquiring advanced management techniques, a solid basis for improving long-term profitability was provided. Using bank level data for 80 countries, Claessens, Demirguc-Kunt and Huizinga (1998) found that the larger foreign ownership share of banks significantly reduces domestic bank profitability and overall expenses but foreign bank entry improves the functioning of national banking markets, with positive welfare implications for banking customers. In the cases of Argentia and Mexico, Goldberg, Dages and Kinney (2000) found that foreign banks generally had higher loan growth rates, with lower volatility of lending. Also, diversity in ownership through foreign banks seems to contribute to greater stability of credit in times of crisis and domestic financial system weakness.

2. The Role of Foreign Entry: Cyclical Properties of Foreign Bank Lending

This section investigates the effects of foreign entry in Korea. When allowing foreign entry into a domestic industry, the major expected effect is the gains from competition. Other potential benefits of liberalization may also be considered. Some economists argue that foreign bank presence would enhance the stability of available lending by diversifying the capital and funding bases supporting the supply of domestic credit.[4] Keeping the argument in mind, we investigate whether the lending behaviors of foreign banks in Korea is different from that of Korean banks in terms of business cycles.

A. Cyclical Properties

We examine cyclical properties of foreign currency loans and domestic currency loans while controlling price effects. For this purpose, we run regressions of growth rates foreign and domestic currency loans on nominal GDP growth rates and interest rate differentials between Korea and the U.S. We used the Data from the *Monthly Bulletin* (MB), issued by the Bank of Korea. From MB, we extracted foreign currency loans and domestic currency loans of Korean city banks and foreign banks in Korea. The sample period is from 1981 to 1999 and all the data are quarterly.

In Korea, foreign currency loans of banks have been made only for corporations, although domestic currency loans are also for households. Because MB does not distinguish household borrowings from corporation borrowings, all the following analyses are subject to the feature. Also data in MB are not for individual banks but are consolidated. Hence, in the analysis we treat all foreign banks in Korea as one foreign bank and all the Korean banks as one Korean bank. In other words, we do not take into account bank-specific factors. Therefore, for example, the impact of the entry of a foreign bank or Korean city bank will not be taken into special consideration.

All regressions were run separately for foreign banks and Korean banks. Interest rate differentials were computed by subtracting federal fund rates and depreciation rates of the Korean won against the U.S. dollar from call rates in Korea. Federal fund rates were from International Finance Statistics(IFS), and call rates and exchange rates were from the Bank of Korea. All regressions were repeated with four sample periods: 1981 - 1996, 1981 - 1999, 1990 - 1996, and 1990 - 1999. Such sample periods were chosen to control any possible anomalies or changes due to the crisis in 1997 and any possible differences between the 1980s and the 1990s.

We document basic statistics in Table 18. It shows that standard deviations are larger in the 1990s, when the crisis period is included. An interesting pattern emerges when comparing foreign banks with Korean banks. With respect to foreign currency loans, standard deviations of Korean banks are considerably larger in all samples. On the contrary, standard deviations of foreign banks are computed to be larger across the samples for domestic currency loans. Therefore, when relying on simple standard deviations, it can be said that Korean banks provided more stable lending service in domestic currency while foreign banks did so in foreign currency.

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[4] For example, see Goldberg, Dages and Kinney (2000).

Table 18. Basic Statistics: Mean and Standard Deviation

	FX loans of FB		FX loans of KB		DC loans of FB		DC loans of KB	
	Mean	S.D	Mean	S.D.	Mean	S.D.	Mean	S.D.
Feb.' 81-Apr.' 96	2.38	5.72	6.31	17.80	2.83	6.58	4.51	4.44
Feb.' 81-Apr.' 99	1.74	9.55	5.31	17.78	2.95	7.07	4.62	5.10
Jan.' 90-Apr.' 96	3.71	6.21	9.38	25.40	0.99	8.08	4.74	5.09
Jan.' 90-Apr.' 99	2.10	12.24	6.59	23.50	1.75	8.51	4.87	5.99

Note: "FB" stands for foreign banks, "KB" for Korean city banks, "FX loans" for foreign currency loans, and "DC loans" for domestic currency loans.

B. Empirical Results

We report the first set of regressions with domestic currency loans in Tables 19 and 20. Since we are interested in cyclical properties, we restrict discussion to the relationship between loan growth rates and nominal GDP growth rates. For the case of foreign banks, coefficients to nominal GDP growth rates are estimated to be statistically significant across the four periods. Besides, the relationship is positive, which suggests that domestic currency loans of foreign banks are pro-cyclical. In the case of Korean banks, no significant relationships are found in any sample periods.

Table 19. Domestic Currency Loans (by Foreign Banks)

	Feb.' 81-Apr.' 96	Feb.' 81-Apr.' 99	Jan.' 90-Apr.' 96	Jan.' 90-Apr.' 99
GDP Growth	0.56 (0.00)	0.32 (0.01)	0.96 (0.01)	0.31 (0.09)
Interest Rate Differential	-0.40 (0.05)	-0.16 (0.03)	0.35 (0.49)	-0.14 (0.14)
$\bar{R}^2$	0.14	0.11	0.20	0.07
D-W statistic	2.11	2.21	2.02	2.25

Note: 1. Numbers in ( ) are p-values.
2. Coefficients on constants are not reported for simplicity.
3. $\bar{R}^2$ is the adjusted R^2

Table 20. Domestic Currency Loans (by Korean Banks)

	Feb.' 81-Apr.' 96	Feb.' 81-Apr.' 99	Jan.' 90-Apr.' 96	Jan.' 90-Apr.' 99
GDP Growth	-0.02 (0.89)	0.05 (0.63)	0.09 (0.72)	0.11 (0.44)
Interest Rate Differential	0.05 (0.74)	0.07 (0.20)	0.23 (0.52)	0.07 (0.27)
$\bar{R}^2$	-0.03	-0.00	-0.06	-0.00
D-W statistic	1.79	1.88	2.19	2.16

The second set of regressions is done with foreign currency loans, summarized in Tables 21 and 22. Interestingly, opposite results are obtained. In the case of foreign banks, GDP growth rates did not show any significant explanatory power. However, the relationship between GDP growth rates and foreign currency loan growth rates becomes significantly positive, though weak, when the regression is done with Korean banks.

Table 21. Foreign Currency Loans (by Foreign Banks)

	Feb.' 81-Apr.' 96	Feb.' 81-Apr.' 99	Jan.' 90-Apr.' 96	Jan.' 90-Apr.' 99
GDP Growth	-0.14 (0.42)	0.12 (0.39)	-0.44 (0.15)	0.21 (0.34)
Interest Rate Differential	-0.13 (0.51)	-0.52 (0.00)	-0.43 (0.31)	-0.53 (0.00)
$\bar{R}^2$	0.02	0.36	0.07	0.39
D-W statistic	1.98	1.50	1.79	1.36

Note: Lagged growth rates of foreign currency loans are included to raise D-W statistic. Its coefficient is not reported for simplicity.

Table 22. Foreign Currency Loans (by Korean Banks)

	Feb.' 81-Apr.' 96	Feb.' 81-Apr.' 99	Jan.' 90-Apr.' 96	Jan.' 90-Feb.' 99
GDP Growth	0.29 (0.61)	0.38 (0.24)	2.05 (0.06)	0.90 (0.08)
Interest Rate Differential	-0.28 (0.65)	-0.52 (0.01)	-5.32 (0.00)	-0.61 (0.02)
$\bar{R}^2$	-0.02	0.11	0.32	0.16
D-W statistic	1.99	1.96	1.12	1.17

Note: Lagged growth rates of foreign currency loans are included to raise D-W statistic. Its coefficient is not reported for simplicity.

In interpreting the results, we need to understand the nature of the estimated equation. Obviously, the equation can be seen as both loan supply and demand functions in a simple form. Since we performed OLS estimation, the obtained estimates are mixture of demand and supply factors. We make two postulations. First, we postulate that income elasticity of loan demand is positive. Second, we postpulate that the correlation between interest differentials and GDP growth rates is not substantial. The first postulation seems harmless since there is no reason to expect otherwise. The second may be controversial. The defense that we provide is the following: interest rate differentials used in the regression can be considered as a country-risk premium. At least in theory, it is difficult to reason for either a pro or counter cyclical country risk premium. The question needs to be resolved empirically and our case shows at least the empirical results on Korea.

Accepting the two postulations, the fact that some loans did not show any cyclical properties should be attributed to supply factors. Specifically, we may reason that in those cases banks do not adjust loan supply in response to the business cycle and, as a result, equilibrium loan amounts do not display the pro-cyclical property of the demand side. It is interesting to note that foreign currency loans did not show any cyclical properties for foreign banks. Likewise domestic currency loans for Korea banks. This suggests that foreign banks provided a stabilizing role as far as foreign currency loans are concerned.

V. Conclusion

After financial crisis, important steps were taken to increase foreigners' access to the banking sector in Korea such as subsidiary and ownership of banks. The benefits of liberalization in banking sector is as follows: to facilitate the exchange of goods and services; to facilitate risk management; to mobilize resources; to obtain information, evaluate firms, and allocate capital; and to provide corporate control. However, there are possible negative effects such as increase in unemployment, higher foreign capital occupancy of the local market, more influence of foreign capital on domestic market and intervention in domestic corporate. Also, freer capital flows have the effect of smoothing consumption over time, and it has to be recognized as the benefit of the liberalization.

We investigated the trend in penetration of foreign banks into the Korean market. Given the regulatory restriction, it has been confirmed that the extent of the penetration remained limited. Foreign banks in Korea have been engaged in foreign currency lending business to Korean corporations and banks, which was funded by their parent offices. Since the share of foreign bank has been too minor to bring about serious changes in charter values of Korean banks and the competitive environment of the Korean banking sector, we focused on their behavioral patterns. We found that their foreign currency lending was neither pro- nor counter-cyclical in contrast to their Korean currency lending which was pro-cyclical. Also interestingly, foreign currency lending of Korean banks turned out to be pro-cyclical.

Foreign banks in Korea were able to provide rather stable foreign currency lending service irrespective of macroeconomic fluctuation of the Korean economy. Foreign banks have more cushions to absorb cyclical shocks specific to the Korean economy than Korean banks. Hence, we argue that allowing commercial presence of foreign banks should be expected to be beneficial in this regard.

It is too early to make a comprehensive assessment of the impact of the liberalization of banking service. However, we conjecture that the ongoing restructuring and entry of foreign banks will make the domestic banks more competitive. In order to survive, management should be independent and efficient. In other words, The Korean banking services should establish the responsible management system and asset soundness. Also, financial infrastructure should be established through improvements in accounting, credit ratings and payment system. The range of banking services needs to be enlarged through development of various products and management skills, along with M&As and joint business with other banks. Consistent market liberalization will more rapidly drive financial globalization. This will lead to the advanced financial institutions as in developed countries.

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국문요약

90 년대 들어와 국제금융환경은 글로벌화, 금융수요의 다양화, 규제완화, 금융혁신 등의 급격한 변화를 보이고 있다. 글로벌화 차원에서 금융기관들은 정보통신기술의 발달로 인해 전통적 대출형태에서 벗어나 업무영역의 확대 및 신금융상품의 개발에 치중하고 있다. 금융공학의 발달로 국제금융거래가 다양화되고 대형화되는 양상을 보이고 있으며, 전세계적으로 금융산업에 대한 규제를 완화하고 철폐하는 추세가 확대되고 있다.

21 세기의 금융산업은 WTO 뉴라운드 등으로 각국의 금융시장개방과 국경간 서비스가 확대되어 세계금융시장의 단일화가 이루어질 전망이다. 또한 금융시장의 경쟁이 심화됨에 따라 선진 각국은 자국의 금융산업의 경쟁력을 제고하기 위해 겸업화를 추진하고 있으며, 금융업종간 진입장벽이 철폐됨에 따라 합병 ·인수를 통한 금융기관의 대형화가 가속화될 전망이다.

한국은 금융위기이후 은행의 지분참여나 현지법인설립 등 은행부문에 외국인 참여를 증대시키는 조치들을 취하여 왔다. 외국은행의 국내 시장 진출에 대한 분석결과 한국에 진출한 외국은행은 국내 기업이나 금융기관에 대한 외화대출 부분에 주로 관심을 두어 왔다. 아직까지는 외국은행의 지분이 국내은행의 가치나 경쟁환경에 커다란 변화를 줄 정도로 크지는 않기에, 본 논문은 외국은행의 영업행태에 초점을 맞추었다. 계량분석결과, 외국은행의 외화대출은 경기순환적이거나 경기역행적인 것은 아니었다. 반면 국내은행의 외화대출은 경기순환적 형태를 띠고 있다.

이는 한국에 있는 외국은행이 한국경기의 변동에 관계없이 안정적인 외화대출을 할 수 있는 것을 보여준다. 한국경제에 경기변동의 충격이 있을 때 외국은행은 국내은행보다 더 잘 이러한 충격을 흡수할 수 있는 역할을 하고 있다는 것을 보여주고 있다. 이러한 관점에서 외국은행의 진출은 국내경제에 도움을 주고 있다고 할 수 있다.

아직은 은행산업의 자유화에 대한 완벽하고 충분한 평가를 하기에는 이르다. 그러나 은행의 구조조정과 함께 외국은행의 진출 등으로 경쟁이 보다 심화될 것으로 예상된다. 국내은행이 이러한 경쟁에서 살아남기 위해서는 경영의 자율성이 확보되어야 한다. 금융인프라 구축을 위해 회계, 신용평가, 지급결제 등 시장하부구조의 선진화, 전자금융의 확충 등이 요구되며, 시장개방을 지속적으로 추진하여 은행산업의 선진화를 달성해야 할 것이다.

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ISBN 89-322-4093-0
89-322-4026-4(세트)