Korea: Financial and Corporate Restructuring

Presentation at the Egyptian Center for Economic Studies

May 17, 2001

Ira Lieberman
World Bank

Outline

- Korea’s Vulnerable Corporate Sector.
- Model for restructuring.
- Initial response to financial crisis
- Government corporate restructuring program.
  - objectives
  - institutional structure.
  - workout process.
- Risks to restructuring process

Characteristics of Korea's Corporate Sector

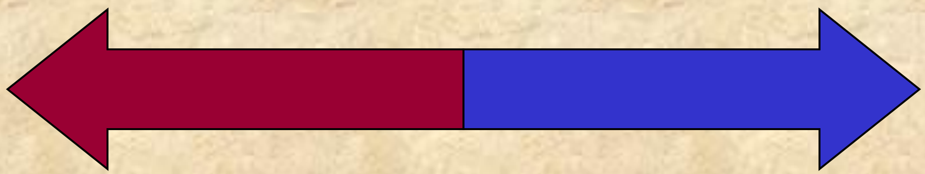
- Dominated by chaebol, other large corporate groups.
- Largest groups try to control wide variety of business lines.
- Chaebol generally family controlled, but publicly listed.
- Illegality of holding companies complicates ownership structure.
- Heavy government involvement.

Kia Group:
The Good, the Bad, and the Ugly

Affiliate	Sales (Won bn)	Net Profit/ Loss (Won bn)	TL / Equity
Kia Motors	6.607	7	427%
Asia Motors	1.679	-29	512%
Kia Intertrade	880	1	-3465%
Kisan Construction	703	-7	729%
Kia Heavy	508	1	943%
Kia Motors Service	420	1	290%
Kia Steel	321	-90	2726%
Kia Precision Works	292	1	216%
Total	12.091	-119	524%

Source: SDCWDR

Model for Corporate Restructuring



Defensive Restructuring 1-3 Years

- Financial re-engineering.
- Sell Assets and non-core lines of business.
- Down-size, reduce costs.
- Conserve, maximize free cash

Offensive Restructuring 3-7 Years

- Clearly articulate mission and strategy.
- Change corporate organization, governance, and culture.
- Emphasize shareholder value.
- Structural change, focus on core business.

Corporate Financial Restructuring: Options and Instruments

- Debt maturity extension
- Recapitalize interest.
- Reduction of interest rate.
- Dept reduction.
- Grace period/ freezing of debt.

- Debt/ equity swaps.
- Convertible debentures
- New financing:
  - during stand-still.
  - as part of restructuring

Objective: to Lower debt service requirements in line with debtor's projected cash flow

Corporate Governance Reform

Unholy Trinity | Arm's-Length Relationship

Unholy Trinity

- Family Controlled sprawling conglomerates.
- Non-transparent accounting.
- Trampling on non-family shareholders.
- Interlocking ownership with financial sector.

Arm's-Length Relationship

- Broaden ownership.
- International standards of accounting and auditing.
- Protection of shareholder rights.
- Prudential regulation of financial sector.

Conclusions

- Ownership realignments are occurring (insolvency, sales, swaps, new issues, spin-offs).
- Volume of corporate distress requires voluntary approaches – would otherwise overwhelm courts.
- Positive incentive (e.g., tax breaks) alone are not enough to induce voluntary restructuring.

Conclusions

- Credible threat of bankruptcy/ foreclosure facilitates Voluntary effort.
- Direct government pressure on debtors and indirect pressure via banks facilitates voluntary efforts.
- Substantial debt/ equity swaps inevitable.
- Need to respond to regulatory issues and provide mechanisms for banks to exit or manage converted equity.