

Showdown over South Korea: Save the day, not the banks

by Marcia Merry Baker

As 1997 came to an end, some of those New Year's noises weren't firecrackers, but warning shots fired over the heads of bankers around the world, to convince them to roll over their billions in loans to South Korea, and make way for 1998. Or else.

On Christmas Eve in Washington, U.S. Treasury Secretary Robert Rubin held a press conference at which he announced plans for an emergency package of \$10 billion for South Korea to help deal with the financial crisis of the world's eleventh-largest economy; Rubin pointedly stated that "not a nickel" would be paid to bail out *private* creditors around the world. Asked by a reporter, if banks were expected to "take a haircut" on bad loans, Rubin said, "I wouldn't spend a nickel to help private investors or private creditors."

The U.S. government emergency actions were prompted by the breakdown situation in South Korea as of mid-December, and the obvious inefficacy of the \$57 billion bailout package announced in Seoul on Dec. 3 by International Monetary Fund (IMF) Managing Director Michel Camdessus. As of Christmas week, South Korea was on the edge of default, and suffering economic dislocation.

South Korea's currency, the won, on Dec. 23 crashed to a new historic low of 1,962 to the dollar (compared with 1,715 the day before); the key composite stock market index closed 7.5% down, the largest-ever one-day fall in percentage terms; and Korean producers were having to pay, through the yield on their corporate bonds, an impossible 31% on borrowed money. Joblessness hit a 15-year high. Construction and output were plunging; and \$10-15 billion in short-term debt was due in a week.

After Rubin's Dec. 24 message, top bankers conferred in both publicized and secretive confabs. Finally, as of 1998, the short-term loan payments due from South Korean entities to the major world banking syndicates, were rolled over, at least

until the end of January or into February. There were some prominent cases of bank resistance and reluctance, notably in London, and also, Tokyo, but the immediate hour of crisis passed. No chain reaction of defaults throughout the world financial system was detonated as of the turn of the year—*this time*. Now, the issue is what lies ahead, and not only in South Korea.

Nations first; speculators last

Secretary Rubin's year-end action bought time, and pointed in the right direction for putting the interests of nations first, and speculators last. In announcing the \$10 billion package, he said that there is "an enormous stake in reestablishing financial stability in South Korea and enabling South Korea to get back on a solid economic track." He added, "And one of the things that they've got to get is security."

On the role of the banks, Rubin was emphatic: "Part of getting that time"—for South Korea to return to economic stability—"would be for the banks to extend their maturities." As to how they would extend them, Rubin said it was up to them to determine.

It should be noted that Rubin's Dec. 24 statements were all but blacked out of the U.S. media, except for EIR News Service. Not one TV camera filmed the press conference, and no full transcript exists. (Excerpts are given below, see *Documentation*). However, in Europe, on Dec. 27, at least three leading dailies quoted Rubin's "not a nickel" formulation—the *Süddeutsche Zeitung*, the *Berliner Zeitung*, and the *Neue Zürcher Zeitung*. The *Süddeutsche Zeitung*'s Washington correspondent, Peter de Thier, noted, "With his go-it-alone decision, Rubin definitely took the initiative out of the hands of the IMF," in particular, because the loan was granted "de facto without conditionalities," in contrast to IMF practices. Writing a similar piece for the *Berliner Zeitung*, Thier

reported that the \$10 billion emergency credit was the consequence of a “dramatic policy shift by U.S. Secretary Rubin,” deliberately announced while Congress was out of session for the holidays.

But neither the \$10 billion emergency mobilization, nor the one-time private bank rollovers, will themselves solve the crisis in South Korea. The situation there is part of the *systemic world financial breakdown*.

What is outstanding in South Korea itself, is that the disastrous impact of recent months of compliance with so-called IMF remedies, shows exactly what should *not* be continued as the approach to the world crisis.

Statistics released on Dec. 29 in South Korea show a breakdown process. Domestic machinery orders fell 34.6% in the year to November, after having risen by 29.8% in the previous year. In November, domestic construction orders fell 23.3%, compared to a 48.5% rise in November 1996. Gross Domestic Product dropped by 2.6% in 1997, with the prospect of at least a 2.2% drop in 1998. Unemployment is officially expected to hit 6%.

LaRouche: What next?

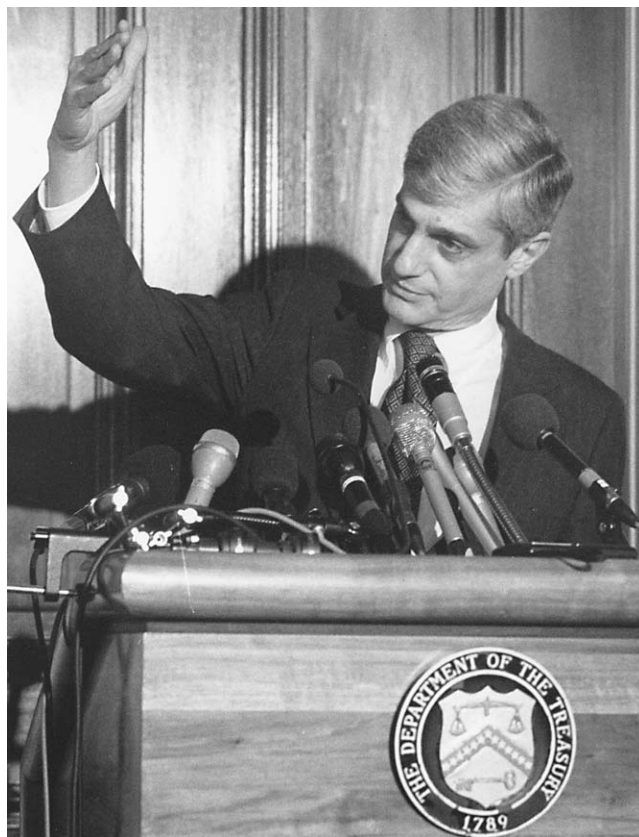
Lyndon LaRouche, interviewed on Dec. 30, by the “EIR Talks” international radio broadcast, commented on the Korean and world situation, as of the closing hours of 1997.

“So, what you have to look at: There are three issues here, actually four. Three issues up front, that are negative. First of all, which has happened as a result of what Rubin did, is that the banks around the world had a Christmas present thrown under their tree, which I don’t think they particularly appreciated. . . .

“Once we buy time, in a sense, by freezing the obligations of the banks, the Korean banks, in that way, by turning them into longer-term, or medium- to long-term maturities, that buys time, maneuvering room, and, in a sense, it separates the debts of the Korean banks from the private corporate interests of Korea. The problem is, there’s been highly disorderly speculative activity, financial activity, on the part of some of the major trading companies in Korea. They have *uncounted indebtedness*—we just don’t have it—because a lot of it lies in the futures or, a.k.a., derivatives area, and it’s very difficult to trace out. . . .

“So, the position is implicitly, that down the line, it’s going to come to a question of whether the foreign creditors—who can’t get at the Korean government, because it’s not involved, it’s not guaranteeing this; they can’t get at the Korea banks, the major banks, because their situation is secured—go in to try to get at the corporations, the private corporations, the private interests.

“Well, in that case, there are alternatives, which the Korean government, presumably with the encouragement of the United States and others, will take to reorganize the obligations, financial obligations, of the companies, that is, to put them under the protection, the bankruptcy protection of the Korean government. . . . A bankruptcy protection will be sup-



U.S. Treasury Secretary Robert Rubin: “not a nickel” to bail out the private creditors.

plied to corporations, the corporations will continue to function, as in, say, U.S. Chapter 11 bankruptcy proceedings. The managements will be there. They will not sell their children into slavery to pay off the debt. A lot of the debt will simply be frozen, and much of it, later, written off.

“But that doesn’t solve the *final* problem. The final problem is the fact that the, as I said, the crisis is largely artificial. A great structural weakness was built into the international financial economic system over a period of 30 years, especially since 1971-72, with the inauguration of the so-called floating-exchange-rate insanity as monetary policy. And that’s going to have to end.

“But the problem is, largely, that a group of British-centered [speculators]—including Soros, who is a British asset; he’s based in Anglo-Dutch interests in the West Indies, for example— . . . these British-controlled speculators . . . have been running a hedge-fund operation against Asian countries. . . .

“What would happen if we don’t pay attention to these [speculative] markets? That the price of the currency is a pegged currency? And whatever George Soros and his friends do is irrelevant! . . .

“We had such a system before in the 1950s, for example, the postwar period. We had limited convertibilities of currency. We had *pegged* currencies. We had capital-movement

controls, and it worked. . . . We're going to have to go back to that. . . .

"All right. So, the next phase, is how do we get the world economy functioning above breakeven level. The aggravating problem is that today, with the collapse of world trade, associated with the crisis which is going on today, in South-east Asia, today in East Asia, now in Korea, which will hit Brazil tomorrow, which is hitting eastern Europe, as in the case of Czechia, which is going to hit Russia, etc., that the world is operating below a breakeven point. So, we have to have an industrial expansion program, including agricultural foodstuffs, trade expansion, which means we need large-scale projects to restimulate the world economy, to bring economies back above breakeven."

Documentation

On Dec. 24, 1997, Treasury Secretary Robert Rubin and Assistant Treasury Secretary Lawrence Summers gave a briefing at the Treasury Department, on the Asian financial crisis. They discussed the purpose and arrangements for an expedited \$10 billion extension to South Korea. It was stressed that private creditors were expected to make their own arrangements on debt owed to them; the private creditors would not get any of this emergency money. An official transcript is not available. The following are excerpts from the partial transcript prepared by the Federal News Service, of Rubin's exchange with reporters at the briefing.

Rubin: [Our action so far] has been driven fundamentally with an underlying sense by the view that we have our economic and national security interests at stake here. [We are concerned about] national security ramifications. . . . It is in our economic and national security interests that financial stability be restored to Korea, to make this best serve our national interest.

Q: Mr. Secretary, are the private banks being made whole here, or are they making some share of the sacrifice?

Rubin: Dave, they're going to have to work out their own arrangements with their debtors. Creditor banks — you're talking about the creditor banks?

Q: Yeah.

Rubin: Yeah. They're going to have to work out their own arrangements with the debtors. And this is a process that really is just beginning.

Q: But when you say that this is being taken in the context of a significant voluntary extension of maturities of existing claims, you obviously have some sense of what their — are you insisting that the private banks take a haircut? Or are you — or are we just talking about extending maturities? Are large uninsured creditors being made whole or not?

Rubin: David, I think it depends on what terms they work out. I really mean that.

I think the key. Look, let's go at it differently: What are you trying to accomplish? What you're trying to accomplish is taking an economy that's grown for 30 years that really had a remarkable record, and now is running into very serious problems for reasons that we've all talked about and analyzed and so forth. And what you want to do is get some time to get back on track. I, at least, think — I think that the underlying strengths here are very substantial, and there's no reason why Korea can't grow at a — excuse me, a very healthy rate again. But they clearly have a lot to do. And one of the things they've got to get is security. Part of getting that time would be for the banks to extend their maturities. On what terms can they extend them and whether they [inaudible], if the present value is lower or not lower than the current present value, is something they're going to have to work out. That's not our business.

Q: Now, may I follow this up? . . . You have distinguished between public sovereign debt and private debt in the past. And we are in the circumstance now where there's a prospect of private sector defaults on Korean debt. There's the talk, a lot of talk about that. Are you — aren't you — isn't the United States and the IMF giving Korea money which will essentially be used to prevent private sector creditors from default?

Rubin: David, I'd say that it's a by-product of [inaudible]. I wouldn't — I'll speak myself. I wouldn't spend a nickel to help private investors or private creditors. . . . On the other hand, I think you have an enormous stake in reestablishing financial stability in South Korea and enabling South Korea to get back on a solid economic track. . . .

Now, since the prime problem here in many respects is the short-term credit of the banks, clearly as official money has gone to the Bank of Korea, is going to the Bank of Korea, an effect of that has been the private sector creditors or private sector Korean banks to receive payment for short-term credits. . . . What this envisions is a situation that takes that pressure off the South Korean banks by extending maturities to whatever period that extensions may be. The terms with which they do that . . . are something they are going to have to work out; and the role that the government plays, the government of Korea plays. Those are two issues. There are probably — Undoubtedly, there are other issues. But those are issues that the banks are going to work out, the Korean banks, and perhaps the Republic of Korea. . . .

The commercial banks are now going to have to work with themselves. This is really their undertaking. This will have to be their undertaking. They're going to be working amongst themselves over whatever period of time it takes to put in place what is described here. . . . They have now got to accomplish that by working amongst themselves. And I think [that you should] perhaps discuss with them how they are going. Well, this is the beginning of a process, not the end of a process, with them.