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# Seoul Swallows IMF's Medicine But If Left With a Bitter Taste

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SEOUL, South Korea -- On a spring-like day in mid-November, as financial panic seized Asia, the International Monetary Fund's managing director and his chief Asia negotiator undertook a clandestine mission to Seoul. For fear that word of an IMF visit might leak out -- setting off yet more jittery speculation in the financial markets about Korea's economic plans -- the two registered under Korean names in a hotel on the city's outskirts and ate their meals in their rooms.

In the midst of this oddly furtive atmosphere, Korea's central-bank governor and finance minister made pilgrimages to the hotel to hear the same message: Korea's finances are crumbling, and it is time for IMF intervention.

"Their first reaction was to say, 'You're crazy; our system works,'" recalls Michel Camdessus, the IMF's 64-year-old managing director. "They were having an identity crisis along with an economic crisis."

The ensuing story of IMF power and Korean resistance is filled with incongruities. IMF bureaucrats wield enormous power over millions of lives and make markets flutter across Asia. Yet they feel frustrated because they are treated as second-stringers by their greatest ally and taskmaster, the U.S. Treasury.

The IMF prescriptions invariably involve awful pain -- layoffs, bankruptcies, bank closures -- on the theory that amputating diseased institutions can save sickly economies. The Koreans, convinced by 30 years of rapid growth that they have devised a new industrial model, were shocked by such IMF dictates.

Imagine the American reaction if a foreign power had forced the U.S. government to boot Chrysler Corp. and Lockheed Corp. into bankruptcy in the 1970s. Korea's elites have thus whipped through an emotional cycle of denial, despondency and, finally, resignation.

The IMF efforts in Korea have involved a messy clash of cultures, beliefs and proud institutions. After the November meeting, Korea's finance minister was ready to start negotiations. Then he was abruptly forced out of his job in an unrelated imbroglio, after his proposed package of economic-reform bills was voted down in the Korean parliament. His successor was Lim Chang Yuel, Korea's delegate to the IMF in the late '80s, viewed as a strong nationalist who could stand up to IMF leadership.

True to that image, Mr. Lim initially sent signals through the press that he would bypass the IMF by going to Japan and the U.S. for money. But neither country was prepared to help unless Korea turned to the IMF first. Even so, says Shin Hyun Chul, director of international relations for the Bank of Korea, the central bank, Mr. Lim's underlings blocked the bank from providing information the IMF needed before it could approve a loan to Korea.

But by Nov. 21, with the value of the won plunging and Korea tottering on bankruptcy, Mr. Lim was left with no alternative but to place the onetime star performer of the "Asian Miracle" in IMF hands. "We're losing our confidence, losing our pride and losing control of our economy," says Chung Mong Joon, a Seoul lawmaker whose father founded the conglomerate Hyundai Group.

Korea began installing reforms -- removing legal obstacles, for instance, to laying off workers. By contrast, Indonesia, which got similar IMF advice -- to close shaky banks, dismantle monopolies and end subsidies to the politically well-connected -- resists strongly and toys with a risky foreign-exchange system that could drive it further into financial turmoil.

Heading the IMF effort here is Hubert Neiss, a 62-year-old Austrian with a flat-top haircut and modest demeanor. As chief of the IMF's Asia-Pacific department, he has had plenty of experience with Asian calamities, such as advising Philippine President Corazon Aquino after the Marcos dictatorship fell in 1986.

But his department failed last autumn to warn of Korea's impending peril. As the economies of Thailand, Malaysia and Indonesia were crumbling in mid-October, he dispatched a seven-person IMF team to make its annual checkup of Korea. Its foreign reserves were plunging, but the visitors didn't spot an emergency. "They said we should handle our problems 'promptly,'" says Hur Kyung Wook, a Finance Ministry official. "'Promptly" isn't the same as 'urgently.'" Mr. Neiss acknowledges: "The mission did point out weaknesses and urged action. But in retrospect, this could have been more dramatic."

Nonetheless, Korean officials were convinced they could withstand Asia's economic storms, with the new finance minister embodying the "Korea knows better" school of thought. When at the IMF a decade ago, Mr. Lim balked at having South Korea contribute to a loan program for poor countries until the fund took seriously Korea's call for a bigger say in fund votes. This tough-guy pose endeared him to colleagues back home, who figured he could stave off IMF pressure as finance minister. He describes it differently. "I always try to stick to principles when negotiating," Mr. Lim writes in a six-page description of his role.

During December negotiations, the IMF contends, Mr. Lim tried to sandbag the fund's boss. As Mr. Camdessus headed down a walkway at the Seoul airport, accompanied by Mr. Lim's deputy, he was handed a schedule: a quick press conference, followed by 45 minutes of negotiations, followed by a visit with the president, followed by a signing ceremony.

Startled by its brevity, Mr. Camdessus promptly canceled some of these meetings -- sending markets tumbling on news of "failed" talks -- and insisted that the sheltered economy accept more foreign investment. "Unless you agree with all the items I have on my piece of paper," Mr. Camdessus says he informed Mr. Lim, there wouldn't be a bailout. But the 53-year-old finance minister calls it a misunderstanding: "We understood that Mr. Camdessus's one-day stopover was a courtesy call," he says, and he insists that he had faxed him a copy of the proposed schedule a day before Mr. Camdessus landed.

The market reaction magnified IMF power, forcing Mr. Lim to accept the fund's main points, according to officials on both sides of the negotiations. In exchange for a $58.5 billion loan package, Korea agreed, for the first time in its history, to close banks, fire workers and managers, end politically motivated loans and let foreigners buy its financial and industrial powerhouses.

As a concession to Mr. Lim, the fund agreed that foreign takeovers should be "friendly," not hostile. A brutal Japanese colonization early this century left many Koreans suspicious that any foreign investment might lead to imperialism. Mr. Lim says he's no xenophobe; as trade minister, he tried to woo Dow Corning Corp. to make a substantial investment, though the deal ultimately unraveled. But as the stock market plunged, he feared that foreigners could unfairly scoop up weakened Korean firms; in December, a majority stake in Korean Air Lines Co. was worth only the $165 million cost of a single Boeing 747.

"Korean firms simply did not have the ability to respond to these [hostile bids] as they might have under more normal circumstances," Mr. Lim says.

The Koreans also agreed to another Camdessus demand: getting the three presidential candidates to endorse the IMF deal. At first, President Kim Young Sam strongly objected: "This is my program. Why do you need the next individual?" Mr. Camdessus quotes him as arguing, to which the IMF chief replied: "So the rest of the world will know" it will continue after election day. (Under the new government, Mr. Lim will also be replaced shortly as finance minister.)

Despite this demonstration of power, many IMF officials feel overshadowed by the U.S. Treasury. Prior to the Asian crisis, Mr. Neiss had never been interviewed on television in 31 years at the IMF. After thumbing through a Time magazine article crediting Treasury Secretary Robert Rubin for the "Rubin Rescue" of Korea, he was nonplused. "When I tell my wife about the negotiations, she'll say to me, from reading the press, 'Someone else did the negotiations,'" he says during a long flight to Korea.

With 18% of the votes at IMF board meetings, Washington usually gets its way on key issues, sometimes prompting Seoul to bypass the fund. When Kim Ki Hwan, Korea's roving ambassador for economic affairs, wanted the IMF to accelerate loans and persuade industrial nations to make more money available, he flew to Washington to get U.S. Treasury Deputy Secretary Lawrence Summers on his side. Korea would make more concessions, Mr. Kim explained -- he called it IMF-Plus -- if Mr. Summers would help it get extra funds. Figuring that was sufficient, and it was, he didn't bother to travel four blocks farther to IMF headquarters, where officials also favored giving Korea extra aid.

These days, the IMF has from six to 10 economists in Seoul, shuttling from the palatial Hilton, where they sleep, to the granite compound of the Bank of Korea downtown or the sprawling campus of the Finance Ministry farther away. These bureaucratic boundaries isolate them from the sometimes palpable resentment of ordinary Koreans, who joke bitterly that "IMF" really stands for "I Am Fired" or "I Am an F [student]."

At Samsam Merchant Bank, to be closed under IMF-backed reforms, the scene in mid-January is surreal. Though layoffs were still next to impossible in Korea, that is changing under an IMF dictate. For now, Samsam's 130 workers get paid, though many have nothing to do; some sit at desks and drink coffee, others take long lunches, and some stay home. To save money for his pending unemployment, Lee Heung Woo, Samsam's chain-smoking labor representative, has pulled his six-year-old daughter from a private kindergarten and told her nine-year-old sister she can't take ice-skating lessons. But he won't lead Samsam workers into the streets for fear that somehow "the IMF will take our funds."

The IMF team shifts uneasily between its conflicting roles as consultant and cop. IMF economists trudge nightly to a warren of cubicles at the Bank of Korea, where plates of Korean dumplings are scattered about and fax machines hum through the night. They examine spreadsheets tracing the flow of dollars in and out of the country. At IMF urging, banks that draw more than $10 million from central reserves are interrogated by Korean regulators, with the message that their dollars must come from the commercial market, not the central bank.

Enforcement can be brutal. In one instance, local bankers were dressed down by Korean regulators in view of the foreigners -- a serious breach of local etiquette. When another banker pleaded at midnight with IMF officials for extra dollars to keep his bank afloat, "we were happy to listen, but we weren't sympathetic," says Robert Kahn, an IMF economist who helped design the tracking system.

Other IMFers oversee the disposition of Korea's financial system. Back in December, Korean officials were so reluctant to lay off workers that they promised to shut only one merchant bank, and wouldn't name it. Some said it wasn't fair to shutter banks for decisions made at government behest. The IMF team interpreted this as stonewalling. "We were told repeatedly, 'No bank was ever closed in Korea,'" says William Albrecht, a retired U.S. bank examiner hired by the IMF to pore through Korean bank records. "The implication was: 'We're not about to start now.'"

During a tense meeting in a Hilton conference room, IMF negotiators pressed for more bank closures, using an Albrecht analysis showing that at least a dozen were insolvent. The Koreans eventually agreed that markets would sink if more weren't closed, and ordered about half of the country's 30 merchant banks suspended and two commercial banks restructured for sale to foreigners. "We realized our hands are pretty much tied," says Mr. Hur of the Finance Ministry.

Still, Korean bankers seethe at what they consider kid-glove treatment of foreigners who pressed loans upon them when times were good, but aren't being penalized when times are bad. "No country can stand for that," insists Cho Sung Jin, deputy president of Korea Exchange Bank. In response, the IMF and industrial nations pressured reluctant Western banks to keep money in Korea and accept lower interest rates than they would earn elsewhere. "If I were a Korean on the streets of Seoul, possibly I'd have the same resentment and antibank sentiments," acknowledges Mr. Camdessus. "But the [Western] banks will take a hit."

By now, Korean officials have learned to deal with the IMF and no longer accuse it of being an American stooge. Under new president Kim Dae Jung, ire is turning against the outgoing government.

Koreans have also learned to lobby the fund, which has favored interest rates of 25% to 30% since January to boost the won's value. Hoping the IMF will ease up, the Finance Ministry had Korean economists prepare studies showing how this damages local banks. And when Mr. Neiss recently met a group of small-business men, Finance Ministry handlers left the room so the businessmen could complain directly that interest charges were killing them.

Well-placed complaints to Korean journalists didn't hurt either. "The local press made us sound very, very wicked," says Wanda Tseng, Mr. Neiss's deputy. The campaign made a difference. Mr. Camdessus has urged authorities to bolster Korea's paltry unemployment benefits, even at the risk of budget deficits, and Mr. Neiss has agreed that interest rates can drop as the won strengthens.

Koreans also have seen they can outlast the IMF. Once the fund completes its loans, its power is gone -- leaving Korea to proceed at its own pace. By year end, the fund will have lent about $18 billion of its pledged $21 billion. (Other agencies and governments provide the rest.) "All of their leverage is gone next year in terms of money," Mr. Hur says. "After that, the IMF makes $250 million a quarter in loans. That's peanuts."

—-- *Michael Schuman contributed to this article.*