A UNIFIED FINANCIAL SUPERVISORY MODEL IN SOUTH KOREA:

Origins and Evolution

Myung-koo Kang

Introduction

During the past decade, the Korean financial regulation and supervision framework has undergone a great transformation. After the Asian financial crisis in late 1997, the Korean government has integrated sector-based financial supervisory agencies into a single function-based, unified financial supervisory agency and started to place more emphasis on managing system-wide financial distress, particularly after the credit card companies’ liquidity crisis in 2003. This change in the financial supervisory framework reflects the shift in both the functions of supervisory agencies and the development in the financial markets. Moreover, it reflects the Korean government’s efforts to engineer the transformation of the Korean financial system from a bank-based system into a more market-based one.

This decade-long Korean experience poses various intriguing questions in regard to the transition to the unified financial supervisory model and its supervisory advantages: What determined the shift to the unified financial supervisory model? Is the unified model better for financial supervision? What needs to be done to enhance financial supervision? This chapter will attempt to answer these questions by highlighting three fundamental points. First, contrary to the conventional view that emphasizes the pressure from market participants, the shift to a unified financial regulation and supervision was driven not by market demand, but by a political decision that involved the Ministry of Finance and Economy (MOFE), which played the central role, and the Bank of Korea (BOK) as well as existing supervisory entities as auxiliary participants in the decision-
The evolution of the supervisory framework was also a path-dependent process reflecting the strong tradition of a developmental state in which the MOFE had been a dominant player in terms of economic policymaking and reform agenda-setting, while the BOK’s independence was weak.

Second, crisis-driven exogenous shocks served as a tipping point in the shift of the financial supervisory framework. The first shock was the Asian financial crisis in 1997, which triggered the shift to a unified supervisory model. Policymakers in Korea tried to emulate the international best practices to catch up with the European model of unified financial supervision, especially the case of the British experience. Korean economic bureaucrats utilized the crisis to reactivate the country’s failed and politically sensitive reform agendas, such as establishing a single unified regulator. The second crisis was credit card companies’ liquidity crisis in 2003, which triggered the shift of supervisory focus from the soundness of individual financial institutions (“microprudential supervision”) to the management of systemic risks of the entire financial system (“macroprudential supervision”). After the crisis, the traditional sector-based supervision gradually shifted to the function-based supervision.

Third, despite their remarkable achievement in maintaining consistency and consolidating financial supervision, the supervisory authorities have critical unresolved issues related to the dual structure of the supervisory agency (the Financial Services Commission and the Financial Supervisory Service), the legal status of its staff, and the legal power of regulatory sanctions. It is still empirically controversial whether a unified financial supervisory model is better than non-unified models. Due to the differences in levels of development in financial service industries and other relevant factors (e.g., institutional, political, and economic factors), we need to take a comprehensive approach that considers the synergistic and complementary nature of various factors in designing a new financial supervisory framework.

In the first section, we will briefly review the preexisting financial regulatory framework and the process of establishing a unified financial supervisory agency during the 1997-1998 financial crisis. We will then review the specific evolution process of a unified financial regulatory framework and its remaining challenges. Finally, broader implications of the Korean case and some lessons will be discussed.

**Establishing a Unified Supervisor**
Determining the Transition Process

Financial regulation and supervision frameworks vary widely from country to country (Central Bank Publications 2009). Due to the diverse dynamics and nature of financial service industries in each country in addition to various other factors (e.g., political, legal, and institutional factors), the specific structure and manner in which regulatory authorities regulate and supervise financial markets vary accordingly. For instance, according to one survey, as of 2004, 33 out of 100 countries had adopted a single regulator model to supervise the banking, securities, and insurance sectors while in 41 countries, banking, securities, and insurance sectors are regulated by multiple regulators. In other cases, a single agency supervises two types of financial institutions—for example, banks and securities firms, banks and insurers, or securities firms and insurers. Moreover, the same survey found that, in 48 out of 100 countries, central banks supervise banks, whereas in other 47 countries, bank supervision falls under the responsibility of an independent regulatory agency, separate from the central banks.

However, during the past two decades, a notable trend has emerged in the wave of financial supervisory reforms. More countries have been adopting a unified financial regulatory framework by creating a single financial supervisory agency. For instance, Singapore created a unified supervisory agency in 1982 and Norway in 1986. Since then, Nordic countries and other European countries have followed the trend (Taylor and Fleming 1999; Ferran 2003) including Iceland (1988), Denmark (1988), Sweden (1991), Britain (1997), Germany (2002), Austria (2002), and Belgium (2004). Outside Europe, Korea (1998), Australia (1998), Japan (2001), and other countries created a single unified financial supervisory agency. It is likely that more countries will follow this trend (Central Bank Publications 2009).

This leads to a question of what has determined this supervisory consolidation and unification trend? One of the prevalent explanations is that it is a response to the blurring and conglomeration trends in the financial sector. In the global financial markets, traditional business boundaries among banking, insurance, and securities have been blurred while new kinds of financial conglomerates have emerged as a result of financial globalization and liberalization (Group of Ten 2001). Another plausible explanation is the institutional tradition in which how much central banks have been involved in financial supervision. For instance, countries in which central banks have been traditionally less involved in supervision are more likely to adopt a unified model of supervision (Masciandaro 2004; Masciandaro 2006; Masciandaro 2007; Masciandaro, Quintyn et al.
Thirdly, economic size can have an impact on this shift. For example, the smaller the overall size of the economy, the more likely the country is to adopt a unified supervision model (Masciandaro 2006). Finally, a country’s legal tradition can have a significant impact on the shift. Those countries where the legal frameworks are characterized by German and Scandinavian—common law—roots are likely to move toward a unified financial supervision model (Masciandaro 2006; Mwenda 2006).

However, political factors such as bureaucratic politics and the role of politicians in designing a new financial supervisory framework have been understudied (Masciandaro 2006; Masciandaro and Quintyn 2008). One of many reasons for this is that market fundamentalists’ views, which promote the idea of less government intervention being more desirable, have been dominant in the discussions of financial supervisory reforms. Since the early 1980s—especially after the ascent of neoliberalism as a prevailing discourse in the political economy—government withdrawal from the market in general, and deregulations for the financial markets in particular, has gained more popular support and come to be a kind of shared understanding among policymakers (Caprio, Honohan, and Stiglitz 2001; Stiglitz 2004; Stiglitz 2002). One of the fundamental assumptions made by market fundamentalists is that more competition will bring about more innovation, thereby producing a greater good for the entire community. In the debate regarding the designing of a new financial supervisory framework, many studies have emphasized “market-friendly” regulation and supervision, assuming that less regulation will produce a better outcome in the financial markets (Demirgüç-Kunt and Detragiache 1998). However, the current global financial crisis vividly highlights that such a claim does not fit the reality.

The Korean case, as will see in the following section, highlights the fact that bureaucratic politics under a financial crisis was a critical trigger that enabled the swift change to the unified financial supervisory model in 1998 and the evolution of financial supervisory governance over the past decade.
Preexisting Financial Supervisory Framework

The Korean financial supervisory functions were divided into two authorities before the establishment of a unified financial supervisory agency in 1998: the Ministry of Finance and Economy (MOFE; currently the Ministry of Strategy and Economy) and the Bank of Korea (BOK). The MOFE supervised most financial institutions (e.g., non-bank, insurance, and securities-related institutions) except for the commercial banking sector through its supervisory agencies—namely, the Securities Supervisory Board (SSB), the Insurance Supervisory Board (ISB), and the Non-Bank Supervisory Authority (NSA). It also supervised specialized banks such as the Korea Development Bank. Meanwhile, the BOK, as a central bank, regulated and supervised commercial banks through the Office of Bank Supervision (OBS). However, in reality, the MOFE was responsible for the entire financial supervision. The minister of the MOFE was not only the deputy Prime Minister in charge of orchestrating monetary, fiscal, and other major economic policies, but also the chairperson of BOK’s Monetary Policy Committee. In addition, traditionally, the tenure of the BOK governor was not legally guaranteed, and BOK’s independence as a central bank—even in monetary policymaking—had been weak due to MOFE’s interference. As such, the existing financial
supervisory framework reflected the history of the modern Korean financial system, especially during the high economic growth period from the early 1960s to 1979.

During the high economic growth period from 1961 to 1979, Korea consolidated its bank-centered financial system. The government tried to create a monolithic banking structure in which the government hierarchically subordinated the private banking sector and firms under government control. Starting in 1961, the Korean government nationalized all commercial banks under the priority loan system; policy loans accounted for the majority of bank loans and received extremely low or negative interest rates. Those who had the access to this rationed capital gained an automatic windfall due to the borrower-subsidized interest rates, which created a perennial over-demand for subsidized credits; consequently, the government became vested with remarkable powers concerning rationing capital (Cho 1997). Meanwhile, through the government-guaranteed foreign borrowing system, the Korean government served not only as a gatekeeper of domestic financial markets against foreign capital, but also as a distributor of foreign capital (Bahl, Kim, and Pak 1986; Hellmann 1993; Vittas and Wang 1991). It was under these circumstances that in the early 1980s, the Korean government started to follow the global trend of financial liberalization (Amsden and Euh 1993).

Since the early 1980s, the Korean government has focused on gradually liberalizing its financial markets as the economy became increasingly internationalized and foreign pressure for opening domestic markets increased (Kim 1986). During the 1980s, the government loosened regulations on the banking sector, encouraged the development of the non-banking sector, and ultimately carried out reforms in foreign exchange. Specifically, nationalized commercial banks were gradually privatized while control over interest rates was loosened as well. For instance, in 1982, the government officially abolished preferential lending rates and placed bank loan rates uniformly at 10 percent.

Meanwhile, the government continued efforts to develop the non-banking financial sector. Historically, the Korean government tried to encourage the development of non-banking financial institutions (NBFIs) to absorb funds from informal curb markets into the formal financial system. In the early 1970s, the government promoted the establishment of NBFIs to compete with the curb market. Deposits in these institutions grew 48 percent per annum from 1975 to 1984. Nonetheless, the size of the curb market in terms of its liabilities was estimated to be approximately one quarter to one third of total money flows (Kim 1985: 34). Therefore, in accordance with banking liberalization,
the government also made efforts to absorb additional funds from the curb market into the formal financial system through NBFIs. To this end, looser rules were applied to interest rates and ownership of NBFIs. This financial deregulation process gained political momentum starting in 1993, when the first civilian (since 1961) administration under Kim Young-sam took political power after three decades of successive military dictatorships.

However, the supervisory framework had not kept pace with the financial liberalization. First, the functions of supervision had not developed in accordance with speedy financial deregulation. Second, banking standards were more lax compared to international standards. Such standards were further relaxed after financial deregulation. For example, accounting standards did not require consolidated statements encompassing the parent bank and its subsidiaries. In particular, no regulation explicitly defined quantities of short-term loans from banks in foreign currencies and offshore funds, although these activities accounted for more than 60 percent of domestic financial institutions’ short-term external liabilities in 1996. Banks did not have to report their financial transactions by overseas branches. Under these circumstances, in 1995 and 1996, several chaebols, including Hanbo, Sammi, and Kia came to be on the verge of bankruptcy, leading the government to initiate financial regulatory reform.

The Establishment Process: Bureaucratic Dominance

In response to the mounting bankruptcies in the corporate sector, the government set up the Presidential Committee for Financial Reform (PCFR), composed of 31 experts selected from the business, finance, and academic sectors, to reform the financial system in January 1997. Initially, financial supervisory reforms such as establishing a unified financial supervisory agency were not a part of the immediate reform agenda. Such reforms were defined as medium- to long-term reform agendas. However, due to the mounting debt problems among larger chaebols, such reforms became immediate reform agenda items (Financial Supervisory Service 2004: 19). After a comprehensive study, the PCFR suggested a number of policy recommendations that were “essential components of the post-crisis reform program, including prescriptions to strengthen prudential regulation” (Lim and Hahm September 2004). The PCFR proposed consolidating the four financial supervisory authorities—ISB, ISB, NSA, and OBS—into a single supervisory agency. Originally, the PCFR intended to reduce the MOFE’s regulatory power and prepared a reform plan to reinforce BOK’s power. However, the MOFE lobbied the president through the presidential economic secretariats,
and the original plan was drastically changed to strengthen the interests of the MOFE. MOFE’s strategy was to establish a new supervisory agency under its influence and integrate all scattered supervisory functions into that agency. The revised bill was submitted to the National Assembly in August and passed in December 1997 at the peak of the financial crisis.

In the middle of the financial crisis, the Act on the Establishment of Financial Supervisory Commission and Other was passed in the National Assembly; according to the newly passed law, the Financial Supervisory Commission (FSC) was established on April 1, 1998, under the influence of the MOFE. The FSC ultimately led to the establishment of the Financial Supervisory Services (FSS) as an executive arm of its own in January 1999. Accordingly, eight months after the establishment of the FSC, four of the formerly separate supervisory authorities—namely, OBS, SSB, ISB, and NSA—were unified into the FSS. Although the FSC and FSS are nominally two organizations, functionally they play a unified role in regulating and supervising financial institutions in the banking, insurance, and securities markets. In addition, the Securities and Exchange Commission, which supervised the securities market, was absorbed into the FSC as the Securities and Futures Commission (SFC), which was responsible for overseeing the securities and futures markets.

The FSC/FSS and SFC work functionally as a unified supervisory agency in charge of prudential supervision of the three main segments of financial sectors—namely, banking, insurance, and securities markets. All types of financial institutions in Korea fall under the supervision of these organizations (see [Table 1]).
### Table 1 Financial institutions under the supervision of FSC & FSS (As of the end of 2000 & 2008)

<table>
<thead>
<tr>
<th>Financial Institutions</th>
<th>Number$^{(1)}$</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2000</td>
</tr>
<tr>
<td><strong>Banks</strong></td>
<td></td>
</tr>
<tr>
<td>Commercial Banks</td>
<td></td>
</tr>
<tr>
<td>Nationwide Commercial Banks</td>
<td>11</td>
</tr>
<tr>
<td>Regional Banks</td>
<td>6</td>
</tr>
<tr>
<td>Foreign Bank Branches$^{(2)}$</td>
<td>43</td>
</tr>
<tr>
<td>Specialized Banks$^{(3)}$</td>
<td>5</td>
</tr>
<tr>
<td><strong>Non-Bank Financial Institutions</strong></td>
<td></td>
</tr>
<tr>
<td>Mutual Savings Banks</td>
<td>163</td>
</tr>
<tr>
<td>Merchant Banking Corporations</td>
<td>9</td>
</tr>
<tr>
<td>Credit-Specialized Financial Companies</td>
<td></td>
</tr>
<tr>
<td>Credit Card Companies</td>
<td>7</td>
</tr>
<tr>
<td>Leasing Companies</td>
<td>19</td>
</tr>
<tr>
<td>Installment Finance Companies</td>
<td>20</td>
</tr>
<tr>
<td>New Technology Venture Capital Companies</td>
<td>6</td>
</tr>
<tr>
<td>Credit Unions</td>
<td>1,330</td>
</tr>
<tr>
<td><strong>Insurance Companies</strong></td>
<td></td>
</tr>
<tr>
<td>Life Insurance Companies</td>
<td>23</td>
</tr>
<tr>
<td>Non-Life Insurance Companies</td>
<td></td>
</tr>
<tr>
<td>Property &amp; Liability Insurance Companies</td>
<td>15</td>
</tr>
<tr>
<td>Reinsurance Companies</td>
<td>1</td>
</tr>
<tr>
<td>Guarantee Insurance Companies</td>
<td>1</td>
</tr>
<tr>
<td><strong>Securities-Related Companies</strong></td>
<td></td>
</tr>
<tr>
<td>Securities Companies</td>
<td>64</td>
</tr>
<tr>
<td>Asset Management Companies</td>
<td>32</td>
</tr>
<tr>
<td>Investment Advisory Companies</td>
<td>127</td>
</tr>
<tr>
<td>Futures Companies</td>
<td>14</td>
</tr>
<tr>
<td>Financial Holding Companies$^{(4)}$</td>
<td>-</td>
</tr>
</tbody>
</table>

1) Based on authorization, including foreign financial institutions branches  
2) Based on the number of banks  
3) Korea Development Bank, Export-Import Bank of Korea, Industrial Bank of Korea, National Agricultural Cooperative Federation, and National Federation of Fisheries Cooperatives  
4) Financial holding companies were introduced in October 2000. 


This creation process was path-dependent,$^{30}$ meaning BOK’s independence had been weak in monetary policymaking and bank supervision from the government control. This reflects the strong tradition of the “developmental state,” in which the pilot economic bureaucracy initiated and orchestrated economic policies of the government (Johnson 1982; Amsden 1989; Woo-Cummings 1999). The MOFE had beaten the BOK in the struggle to dominate financial supervisory functions. In reality, the FSC was an extension of the MOFE in the composition of its personnel as well as its functions. Almost all of the core staff at the FSC were recruited from MOFE officials (H.-B. Kim 2006), especially from the Bureau of Financial Policy; consequently, the FSC’s power increased in scope as well as in its power to wield policy tools for enforcement purposes. Meanwhile, BOK’s bank supervision authority was relinquished, resulting in its monetary policymaking function being
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separated from bank supervision. From the MOFE’s point of view, the establishment of the FSC was a success of strengthening its overall financial regulation and supervision power.

**The Financial Crisis, the IMF, and Bureaucratic Politics**

Compared to other cases that established a unified financial regulator, the Korean case took place over a very short period of time, but in a very decisive way. For instance, in the Japanese case, the initial plan for establishing an independent and unified supervisory organization was suggested in 1996, and the Financial Supervisory Agency was established in May 1998. As a result, the Japanese agency evolved into an even more powerful agency—the Financial Services Agency—in January 2001. This process was very gradual compared to the Korean case. Why, then, was the practice so much faster and smoother in the Korean case?

Two factors should be noted: the pressure from the International Monetary Fund (IMF) and the temporary political vacuum that enabled the predominance of bureaucrats—specifically MOFE officials—to reactivate their failed reform agendas. Unlike in other cases of financial supervisory transition, in the Korean case, the IMF’s involvement worked as an important structural condition that enabled the Korean government to weaken resistance from domestic economic actors and set the pace and direction of financial supervisory reform. In the Korean case, the IMF reform package—agreed upon on December 5, 1997, in return for receiving $57 billion of emergency funds from the IMF—was unusually comprehensive and extensive in its scope and policy details.

Although financial restructuring was the core of the IMF program, corporate sector reforms—specifically, reforms regarding the *chaebol*—and other reform policies were included in the agreed-upon policy matrices, including trade and financial service liberalization, privatization of public enterprises, tax reform, and even increased flexibility of the labor market (Timothy 1999). Moreover, the IMF demanded strict monitoring of the Korean government’s financial restructuring measures by applying structural performance criteria. Over three years, the IMF program had a total of 21 structural performance criteria—an average of seven per year; these criteria had to be observed according to the specified timeframe.

Under the circumstances, the government tried to utilize IMF pressure to reactivate its failed economic reform agendas, including the creation of a unified financial supervisory agency. The crisis provided the MOFE with a good opportunity to impose these failed policies while attributing the blame to the IMF. In fact, many of the agreed-upon policy measures with the IMF had already been
proposed by the Korean Development Institute, a think tank of the MOFE, and were identical except for the specified timeframe. The following statement from the IMF report clearly demonstrates how the Korean bureaucracy tried to take advantage of IMF conditions to impose previously failed, unpopular policies:

The measures outside the two core areas (the financial and corporate sectors), however, were not subject to structural performance criteria, and accounted for a relatively small share of the structural measures listed in the extensive policy matrices. Indeed, these reforms were typically part of the government’s broader policy agenda and in many instances were inserted into the policy matrices at the request of the Korean authorities to demonstrate their resolve to enhance flexibility and growth potential of the economy (Chopra & Kang et al.: 50).

The political situation made it difficult to engage in the system of checks and balances of the Korean bureaucracy in the National Assembly. In the midst of negotiating with the IMF about specific measures for structural reforms, a presidential election was held in mid-December 1997, which the ruling party lost. Consequently, between December 1997 and the official inauguration of the new government in late February 1998, the Korean government was in a state of transition. The newly elected president and his party could attribute the entire responsibility for the financial crisis to the former regime, leaving them relatively free from public criticism or anger about accepting the IMF conditions. In short, no politically accountable force existed to check the initiative of the Korean bureaucracy in negotiating with the IMF.

**Evolution of Financial Supervisory Governance**

**Shift from Micro- to Macro-prudential Supervision**

Traditionally, financial supervision has focused on supervising the soundness of individual financial institutions, which is often called “microprudential supervision,” to maintain financial stability. The main objectives of microprudential supervision were to limit idiosyncratic risks of individual financial institutions to protect financial consumers. In regard to supervision methods, it applies standardized supervisory criteria such as the Bank for International Settlement (BIS) ratio for banks, regardless of the characteristics of individual financial institutions. By evaluating the management performance of individual financial institutions, supervisory authorities try to make timely adjustments. The implementation style of supervisory controls is basically a bottom-up
process, and economic conditions are recognized as exogenous to the business operations of individual financial institutions (Borio 2003; Crockett 2000).

However, recently supervisors have begun to put more emphasis on the system-wide financial distress originating from common macroeconomic factors, such as terms of trade deterioration, large capital inflows and outflows, asset market bubbles, herding, and sudden changes in market sentiment and expectations. Moreover, due to the progress in financial technology—both information technology and sophisticated financial products (e.g., derivatives)—it has become increasingly difficult to detect and monitor the new financial systemic risks. Furthermore, the problem of pro-cyclicality has emerged in the lending behavior of banks and other financial institutions (Borio, Furfine, and Lowe 2001; Kaminsky, Reinhart, and Végh 2004). In fact, when the economic conditions enter into an upswing phase of the business cycle, financial institutions are more likely to expand their lending; this credit expansion can create an asset bubble, which will eventually burst. Therefore, if financial institutions can restrain their lending collectively, it can reduce the cost of the burst bubble. However, no such market mechanism can resolve the collective action problem among financial institutions. Under these circumstances, it is insufficient to maintain financial stability by relying on traditional microprudential supervisory methods.

Meanwhile, the main objective of macroprudential supervision is to maintain the financial stability of the entire financial system. This approach applies market-responsive supervisory standards by analyzing risk factors according to changes in the macro-financial environment. Accordingly, the implementation style of supervisory controls is a top-down process in which the supervisor sets prudential controls in terms of the probability and costs of systemic distress and applies certain criteria to financial institutions. Using this approach, standards can be applied flexibly depending on the market conditions while economic conditions are recognized as endogenous variables influenced by collective business operation by individual financial institutions (see [Table 2]) (Borio 2003; Crockett 2000).
In the Korean case, the 1997 financial crisis provided a historical lesson that the macroprudential supervision is essential for maintaining financial stability. However, even after the establishment of the unified supervisory framework, practices of financial supervision had not substantially changed in the sense that the supervisory agency put more emphasis on the soundness of individual financial institutions. One of the critical issues involved in consolidating the macroprudential supervision was to resolve the conflicts of interests among major regulators such as the MOFE, the BOK, and the FSC/FSS. The MOFE is in charge of macroeconomic policymaking and the BOK monetary policymaking, whereas the FSC/FSS emphasized the soundness of individual financial institutions more. The problem of this division of labor was explicitly revealed in the liquidity crisis of credit card companies in 2003.

In the course of recovering from the financial crisis of 1997, the MOFE tried to increase domestic consumption to boost the economy by encouraging credit card usage. To promote the usage of credit cards, the MOFE tried to provide various economic incentives such as tax deductions, the elimination of caps for cash advances, and raffles using credit card receipts as tickets. However, the supervisory regulations for non-bank credit specialized financial companies such as credit card companies and leasing companies were much less strict than those for the banking sector. Under such circumstances, credit card companies issued cards without properly checking applicants’ credit history; furthermore, the FSC/FSS could not properly supervise this process. The BOK, targeting more stability in price levels, provided an inconsistent analysis—fluctuating between...

The mounting problem in the credit card industry was not detected early enough, and the delinquency ratio outstanding for more than a month increased from 3.8% in 2001 to 8.8% by the end of 2002 and then to 11.1% by January 2003 (C.-L. Kim 2006). Loan losses grew, and borrowings held by credit card companies stood at 88.8 trillion won as of March 2003. The number of credit defaulters—those who had not repaid 300,000 won or more in debts from financial institutions for more than three months after maturity—soared (see [Table 3]), ultimately escalating into a liquidity crisis.

<table>
<thead>
<tr>
<th>[Table 3] Major indicator of credit card industry</th>
</tr>
</thead>
<tbody>
<tr>
<td>999</td>
</tr>
<tr>
<td>Number of Cars in Issue (in millions)</td>
</tr>
<tr>
<td>Average Number of cards per (economically active) person</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Number of credit defaulters (in 10,000)</td>
</tr>
<tr>
<td>Credit card related defaulters (in 10,000)</td>
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<tr>
<td></td>
</tr>
<tr>
<td>Card Cash Loan* (KRW trillion)</td>
</tr>
<tr>
<td>Credit card usage amount out of the total private consumption expenditure</td>
</tr>
<tr>
<td>* Card cash loan = Cash advance + Card loan</td>
</tr>
</tbody>
</table>

This liquidity crisis heightened awareness of the significance of macroprudential supervision. The focus of financial supervision has gradually shifted to monitoring the soundness of the entire financial system. After the liquidity crisis, the FSS and the BOK tried to strengthen the macroprudential supervision. The FSS established the “Macro-Prudential Supervision Department,” comprised of 23 members in four teams, to monitor the financial markets and formulate appropriate preventive measures and early warning systems. In addition, the BOK strengthened the functions of the “Financial System Stability Department,” composed of 68 members in eight teams, whose main functions was to promote collaboration on supervisory issues at home and abroad and to monitor financial institutions for emergency credit extension.
The FSS attempted to introduce and implement an enhanced risk management plan after the liquidity crisis in 2003. A good example is the introduction of limitations in mortgage lending in 2006. In 2005 and 2006, housing prices escalated and mortgage loans also soared. Under the circumstances, the FSS investigated mortgage loans and took preemptive measures to ease the overheated housing market. For example, those who wanted to buy a house in a speculative zone were permitted to apply for a loan only once. The loan-to-value ratio was also dropped from 60% to 40%. Moreover, in March 2006, the debt-to-income ratio was introduced, which was to be applied to any house whose value exceeded KRW600 million in an effort to prevent excessive tilting toward mortgage loans. Consequently, mortgage loans in the commercial banking sector gradually slowed (Kim C.L. 2006).

<table>
<thead>
<tr>
<th>Type of Market Failure</th>
<th>Systemic Instability</th>
<th>Asymmetric Information</th>
<th>Market Misconduct</th>
<th>Anticompetitive Behavior</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regulatory Area</td>
<td>Macroprudential</td>
<td>Microprudential</td>
<td>Business</td>
<td>Enhancing competition</td>
</tr>
<tr>
<td></td>
<td>surveillance</td>
<td>supervision</td>
<td>supervision</td>
<td></td>
</tr>
<tr>
<td>Objectives</td>
<td>Financial stability</td>
<td>Individual institutions</td>
<td>Consumer protection</td>
<td></td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th>Sub-sectors</th>
<th>Banks</th>
<th>Insurance Companies</th>
<th>Securities Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Bank of Korea, Ministry of Strategy and Economy, FSC</td>
<td>FSC/FSS SFC</td>
<td>FSC/FSS SFC</td>
</tr>
</tbody>
</table>

Source: Author's modification of Chihak and Podpiera (2006), table 1, to the Korean context.

Currently, the macroprudential supervision is carried out through cooperation among the BOK, the Ministry of Strategy and Economy (MOSE, a reorganized MOFE), and the FSC. The FSS is in charge of microprudential supervision to minimize the problem of asymmetric information in the markets and business supervision to correct market misconduct to protect consumers (see [Table 4]). Ultimately, given that macroeconomic policymaking, monetary policymaking, and financial supervision functions are separated among government authorities, sharing supervisory information and responsibility as well as cooperating among relevant financial authorities is crucial for the successful implementation of macroprudential supervision.
From Sector-based to Function-based Supervision

The Korean government—specifically, the MOFE—launched a reform project to consolidate existing laws on capital markets into a single, more unified law in March 2003. In fact, various kinds of laws—about 14 different laws—on capital markets existed, including the Securities and Exchange Act (1961), Futures Transaction Act (1995), Trust Business Act (1961), and Merchant Bank Act (1995). This project lasted until the end of 2004, when the government proposed a bill to consolidate financial markets and the National Assembly passed the Financial Investment Services and Capital Market Act, which went into effect in February 2009. This act was modeled after the Financial Services and Market Act 2000 of the British government.

[Figure 2] Consolidation of laws on capital markets (2009)

The act consolidated approximately half of the fourteen separate laws on the capital markets and made several notable changes. One notable change was the shift from sector-based to function-based regulations, thereby allowing the same financial functions to be governed by the same regulations regardless of the type of financial institutions. In addition, the act enabled the expansion of financial institutions’ business scopes. For instance, financial investment companies could now provide all six financial services—dealing, arranging, asset management, asset custodian management, and discretionary and nondiscretionary investment advisory services. The act further
relaxed entry barrier regulations. Consequently, financial institutions are likely to have more flexibility in product development, especially when diversifying financial products and services. Finally, the act sought to remove firewalls among financial sectors and ease the market entry and exit processes, thereby creating more competition within and across different financial industries. For instance, the act lifted the legal limitation on financial institutions’ executives from serving more than one position; it also enforced a “negative” regulator system, which in principle allows all new entries, and streamlined the approval process for new products.\textsuperscript{29}

In short, the act emulated the Anglo-American model of financial supervisory framework in line with the so-called global trend of consolidating capital markets. Thus, the Korean government tried to shift the specific, rule-based approach to a more principle-based supervision that puts a greater emphasis on self-discipline and self-compliance of financial institutions.

Meanwhile, the Korean government has tried to lessen the separation between industrial and financial capital. Traditionally, the Korean government has not allowed financial holding companies and restricted “non-financial business operators” from taking ownership in the banking sector. This restriction stemmed from one of the government’s efforts to separate industrial capital from financial capital as well as control the corporate sector by intervening in banks’ credit allocation. However, in response to the blurring and conglomeration trends in the financial sector, the Korean government allowed the establishment of financial holding companies in October 2000 by passing the Financial Holding Companies Act in the National Assembly. Nonetheless, the Korean government did not allow a “non-financial business operator” (NFBO) to take ownership of a bank holding company. A NFBO was not allowed to own more than 4% of the voting shares of a bank holding company. However, this restriction was lowered with the amendment of the Financial Holding Companies Act in October 2009. Currently, NFBOs are allowed to own up to 9% of the shares and become the largest shareholder or participate in management after FSC approval.\textsuperscript{30}

The government has tried to rationalize the necessity of consolidating existing laws on capital markets into a single statute and lower the barriers between industrial and financial capital by emphasizing the limits of the existing regulatory framework. For instance, under existing laws, regulatory definitions on “securities” were not sufficient or flexible enough to promote new financial products among financial investment services providers. Moreover, the government claimed that financial regulation should reflect financial markets; as a representative example, the government—specifically the MOFE—emphasized the blurring sectoral distinctions in the financial markets.
However, in reality, a more important strategic calculation was to create an internationally competitive financial conglomerate like a Korean “Goldman Sachs.”

It may be more appropriate and realistic to evaluate these governmental efforts to consolidate the capital markets and relevant laws as being more proactive and aggressive measures to develop capital markets rather than reflective or defensive measures in response to the development of capital markets or demands from financial industries.

In the course of passing the Consolidation Act and the Holding Company Act, political conflicts mounted on the relevancy of emulating the Anglo-American model, which was regarded as being failed or flawed due to the ongoing global financial crisis that originated from the subprime mortgage problem in the U.S. Opponents of consolidating the capital markets and relevant laws claimed that the government’s attempts to consolidate the capital markets and laws were simply copies of the U.S. investment banking model, which had failed and was highly likely to fail in the future while increasing the systemic risks of the entire financial system. Meanwhile, proponents claimed that the problem of the U.S. model was not a problem of the model itself, but a problem of management. It is yet to be seen how the outcome will turn out, but it seems clear—considering the ongoing impacts of the current global financial crisis—that an alternative model that can lessen the systemic risks of the financial system is necessary and that reintroducing some firewalls among different financial sectors is gaining support in the academic and policy communities (The U.S. government 2009).

**Increasing Supervisors’ Power and Independence**

Another major change in financial supervision occurred on February 29, 2008, with the amendment to the Act on the Establishment of Financial Services Commission. Three distinctive changes occurred. First, the newly created FSC came to be more independent from MOFE control, thereby having the statutory authority to draft and amend financial laws and regulations. According to the amendment, the Financial Supervisory Commission was integrated with the Financial Policy Bureau of the former Ministry of Finance and Economy (currently, the Ministry of Strategy and Finance) to become the FSC. The new FSC was charged with performing “duties concerning financial policy, supervision of the soundness of foreign exchange business management institutions, and financial supervision under the jurisdiction of the Prime minister” (Article 3). In particular, the new FSC had the statutory authority to draft and amend financial laws and regulations, which had
previously belonged to the MOFE. The FSC did not have an independent authority to submit finance-related bills to the National Assembly. However, due to the amendment, the new FSC came to have the ultimate authority in making finance-related government bills. Moreover, as a result of the amendment, those government officials under the MOFE who performed tasks related to the supervision of the soundness of the finance and foreign exchange business management institutions, including the public officials of the secretariat to the Public Fund Oversight Committee and the Financial Intelligence Unit and the public officials of the FSC, came to be regarded as belonging to the new FSC. In other words, the amendment attempted to separate the functions and staff of the FSC from MOFE control.

Second, the FSS became more independent of the bureaucratic control in terms of governorship. The governor of the FSS—a position that was usually held concurrently by the chairperson of the FSC—was to be appointed by the president on the recommendation of the chairperson of the FSC. The governor ultimately was given general control over the affairs of the FSS (Articles 29 and 30). The chairperson of the FSC came to hold the governorship of the FSS concurrently under the peculiar situation created after the financial crisis in late 1997. At that time, the FSC was in charge of both financial and corporate restructuring. To expedite the reforms in both sectors, the original law gave tremendous power to the FSC chairperson by appointing him concurrently to the governorship of FSS. However, giving special powers and control of the FSS, which is composed of non-public officials, to the FSC chairperson has been a controversial approach as it has left everything under the control of the FSC’s public officials.

Third, the amendment made the FSC’s bureaucratic control over the activities of the FSC more explicit. For instance, the amended act stipulated that “The Financial Services Commission may, when recognized as necessary, instruct the Financial Supervisory Service to report on matters concerning the operations, properties and accounting of the Financial Supervisory Service, or it may inspect the operations, financial status, account books, documents and other materials of the Financial Supervisory Service as prescribed by the Financial Services Commission” (Article 60). Moreover, the FSC may issue orders necessary for guidance and supervision of the operations of the FSS and when the activities of the FSS are “unlawful or significantly unjust to public interests or the protection of financial consumers, such as depositors, the FSC may revoke all or part of such disposition or suspend the execution thereof” (Article 61). In short, in return for giving independent
governorship to the FSS, the FSC came to have more direct and hierarchical control over the activities of the FSS.

**Remaining Controversies: Independence and Accountability**

Despite its remarkable achievement in maintaining consistency and consolidated financial supervision, the FSC/FSS still has unresolved critical issues. Indeed, securing its independence and accountability remains one of the most critical factors for the success of its supervisory functions.

First, in terms of organizational independence, the FSC/FSS is still vulnerable to bureaucratic interference concerning financial supervision. For example, the relationship between the MOFE and the FSC was not completely separated until recently, and the newly merged Financial Services Commission is an extension of the bureaucratic control of the MOFE (MOSF). In fact, 19 FSC officials were recruited from the MOFE in April 1998, and the number of FSC officials gradually increased, reaching 70 by 2004 (Kim, D.-S. and Suk-Heon Yoon 2005). These FSC officials considered the MOFE to be their home organization and believed that they would ultimately return to the MOFE (Kim 2006: 135-147). Meanwhile, as a result of the amendment enacted in February 2008, the new FSC came to have independent power to submit bills to the National Assembly, but it is still uncertain whether the new FSC can be free from the influence from the MOSF. In fact, although the commissioner has a legally guaranteed term of three years, commissioners have frequently been changed according to presidential will. Therefore, although the FSC and the FSS have tremendous power in the actual supervisory process, the MOSF still has the power to set the agenda for financial policies.

Second, the FSS’s legal status is still ambiguous and organizationally the FSC and the FSS are divided. Unlike the FSC, the FSS is staffed by non-civil servants. Initially, when the integration plan was announced in April 1998, positioning the FSS was a critical issue for former supervisory organizations (e.g., determining whether the new agency would be established as a subordinate organization under the FSC or under the control of the National Assembly). The staff who worked in the four organizations were considered semi-public in the sense that they were not public servants but dealt with public services. Meanwhile, the FSC was an organization composed of public servants. Therefore, to subordinate the FSS to the FSC meant that the bureaucracy would control an essentially private organization. In the end, the FSS came to be under the direct control of the FSC, despite resistance from the prior supervisory organizations. For example, the FSC commissioner
holds the position of the FSS governorship. The formal status of the FSS still remains uncertain, which is one of the critical issues that needs to be resolved to secure both independence and accountability of financial supervision. The legal status of the FSS is a private organization, but the FSC can supervise and intervene in the activities conducted by the FSS. Therefore, in terms of rigorous legal standards, the FSC is neither an independent administrative agency nor a central government organization. A few attempts have been made to unify the FSC and the FSS and create a more independent organization relatively free from bureaucratic control by the government, but they have all failed due to the lobbying efforts of the MOFE. As a result, the vague dual structure of financial supervision, divided by the FSC and the FSS, remains.

Third, many grey areas exist in the legal power of the FSC/FSS. Although the FSC performs a quasi-judicial function, no properly established procedure exists for governing different officers who pursue impeachment and judicial sanctions against a party who violates the law. The sanctions of the FSC are still based on administrative regulations. Such ambivalence raises another critical issue about accountability: Who is going to watch the watcher? A common view is that a regulator should be operationally independent and account for the use of its power. However, determining how to secure the institutional independence of the FSC/FSS as a regulator remains controversial. We can think of an alternative option to make it a neutral agency outside the executive and legislative branches of government. However, such an option seems to be unrealistic in the Korean context given the strong tradition of government dominance.

**Concluding Remarks**

The ultimate goals of any financial supervisory reforms should be to enhance supervisory capacity and the effectiveness of supervision. A unified supervisory reform is no exception. However, the effectiveness or efficiency of financial supervision is difficult to evaluate empirically because it is difficult to define the objectives of financial supervision. Excessively strict regulation and supervision may contribute to maintaining financial stability, but it can discourage financial development or market growth. Furthermore, prudential financial supervision does not necessarily prevent financial crises. In fact, it is still empirically controversial whether a unified financial supervisory model is better than non-unified models. In reality, due to the differences in levels of development in financial service industries and other relevant factors such as institutional, political,
and economic factors, we need to take a comprehensive approach that considers the synergistic and complementary nature of various factors in designing a new financial supervisory framework. The simple emulation of a certain unified model or a mosaic copy that combines the best practices in various countries developed under a different institutional context cannot work properly in a different institutional setting.

Based on the Korean experience, we can identify broader comparative implications that need to be seriously considered for better financial supervision under a unified supervisory framework. First, it will be a serious task to check and balance a consolidated, more powerful supervisor. In the Korean case, the FSC/FSS supervises all types of financial institutions and recently gained statutory authority to draft and amend financial laws and regulations. As the only authority, it can wield tremendous power over the management of financial institutions. However, it is not clear which organizations (or who) will maintain the checks and balances on the tremendous power of the single supervisor (FSC/FSS). Moreover, if the unified supervisor fails to detect systemic risks and prevent them in a timely manner, the system-wide impacts of supervisory failure are likely to increase further in accordance with the consolidation of capital markets, as the current global financial crisis and its contagion pattern have convincingly demonstrated. Alternatively, the unified supervisor (FSC/FSS) needs to be checked and balanced by other financial or political authorities or the supervisory functions can be shared among various financial authorities, although some functions may overlap.

Second, financial deregulations for a speedy consolidation of financial markets should keep abreast of the development of market discipline. One of critical underlying assumptions, shared by the policymakers of the Korean government, in the course of deregulating entry barriers to the capital markets and other relevant regulations for consolidating capital markets is that more competition will bring about more innovation and ultimately more market discipline. However, this assumption presupposes self-discipline and self-compliance from participants in the financial markets. If the involved actors or financial institutions do not behave in a disciplined way, they are likely to engage more with highly speculative and risky businesses, eventually increasing the negative cost to the entire financial system through systemic crises. Therefore, building market infrastructure that can enhance market discipline should accompany financial deregulations. In this respect, the pace and sequence of financial deregulations should be pursued in a prudentially gradual way. The Korean government has taken a far more aggressive and speedy way of financial deregulations to
create bigger, consolidated financial markets. However, it remains uncertain whether those deregulations have enhanced the market discipline among involved actors in the financial markets or whether those measures have been accompanied by other measures to strengthen market infrastructure.

Finally, the current global financial crisis is revealing a new challenging task for designing a new financial supervisory framework at both the global and national levels. In particular, financial deleveraging\textsuperscript{36} has been accelerated at the global level, where financial institutions in advanced economies have cut lending and investment to domestic markets as well as overseas lending or investments to emerging markets.\textsuperscript{37} This unprecedented scale and speed of financial deleveraging and contagion has provoked a series of discussions for designing a new financial regulatory framework at both the global and national levels (IMF February 2009).\textsuperscript{38} However, designing a new financial supervisory framework is a challenging task at the national and global levels. At the national level, if a country’s financial markets are fully unified to the global financial markets while its financial supervision framework is predominantly nation based, it is almost impossible to maintain a stable financial system, completely preventing the cross-border financial contagion. Likewise, without a sound financial supervisory framework at the national level, it is difficult to achieve both a unified and stable financial system at the global level. In the end, through a muddling-through process, a new financial supervisory will emerge and will likely put more emphasis on the cross-border supervisory cooperation among financial authorities to supervise the flow of cross-border capital.

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Regulating and supervising are not the same functions. For instance, a main role of a regulator is to issue regulations and promote compliance with those regulations, whereas a supervisor’s main function is to conduct on-site and off-site monitoring of financial institutions’ financial activities. Within the unified financial supervisory framework, these two functions usually reside in the same agency. In this chapter, we use the term supervision to mean both regulatory and supervisory functions.

Studies on the financial services regulations in Europe emphasize this political aspect in the shift of financial supervisory framework. For more details, see Masciandaro (2006), Quaglia (2007), and Masciandaro and Quintyn (2008).

Masciandaro (2006) shows the path-dependent nature of reforming financial supervision, focusing on the preexisting role of central banks in bank supervision.

For a discussion of the British debate on creating the Financial Supervisory Authority and its effects, see Bruilt and Wharf (1999) and Briault (February 2002).


See Čihák and Podpiera (2006), table 2. For a more recent and comprehensive review of different regulatory practices in the world, see Central Bank Publications (2009).

Some of these countries include Argentina, Brazil, Egypt, France, Greece, India, Indonesia, Italy, New Zealand, Portugal, Spain, Thailand, Turkey, and the United States. See Čihák and Podpiera (2006), table 2.

Some of these countries are Brazil, France, Italy, Indonesia, India, Malaysia, Singapore, Thailand, and the United States. This is based on data from Central Banking Publications (2004) and Čihák and Podpiera (2006), table 2.

Some of these countries are Korea, Japan, the United Kingdom, Sweden, Norway, Australia, and Germany.

In Singapore’s case, regulation has been unified within the central bank, not by creating a separate agency outside of central bank.

In Australia, securities regulation is conducted separately from banking and insurance regulation, so we can say that the regulatory structure had not been fully unified.

For more details on bank regulation and supervision around the world, see World Bank Database on bank supervision and regulation. The most recently updated information (June 2008) is available at http://econ.worldbank.org/WEBSITE/EXTERNAL/EXTDEC/EXTERESEARCH/0,contentMDK:20345037~pagePK:64214825~piPK:64214943~theSitePK:469382,00.html#Survey_III

Scholars started to debate the advantages and disadvantages of unified financial services supervision in the late 1980s, when the British government sought to create a unified financial regulatory agency. See Mwenda (2006). For a detailed literature review on this topic in regard to designing a financial supervisory framework, see Masciandaro and Quintyn (2007) and Martínez and Rose (2003).

According to one study, consolidation in the financial sector is beneficial up to a relatively small size, but there is little evidence that mergers yield economies of scope or gains in managerial efficiency. See Amel (2004).

Amsden (1992) criticizes the influence of American-trained Korean economists (A-TKEs) who “were the champions of a financial liberalization to increase equality and efficiency. In the presence of big business groups, however, financial liberalization led to more, not less, concentration of capital. The A-TKEs were allies of the World Bank in denouncing a government-led investment drive in heavy industry, although heavy industry supplanted light industry as a leading sector when Korean wage rates began to rise.” Amsden (1992: 355).

For instance, an 8 percent ceiling on bank ownership occurred; in particular, the government set a ceiling on chaebols’ ownership of commercial banks—4 percent for commercial banks and 15 percent for local banks. However, chaebols were allowed to establish their own NBFIs, and no ownership restriction was applied except for investment and trust companies—a 5 percent ceiling was applied to the top 30 chaebols.

Most FSC staff members were recruited from the bureaucrats of the Ministry of Finance and Economy.

More than 1,400 persons work in 24 departments and 5 offices, which represents a substantial reduction from the 64 departments of the former supervisory bodies.

This integration followed the British model. For the specific process of establishing the FSS, see Ahn and Choi (May 2001).

Masciandaro (2006) shows the path-dependent nature of reforming financial supervision, focusing on the preexisting role of central banks in bank supervision.
This process is very similar to the case of establishing a unified regulator in Britain. For example, the British government created the Financial Services Authority (FSA) by integrating regulatory roles previously carried out by different sector-oriented regulatory organizations, such as the Securities and Investment Board, the Investment Management Regulatory Authority, and the Supervision and Surveillance Department of the Bank of England.

For more details on the initial agreement between the IMF and the Korean government on December 5, 1997, see the IMF website available at http://www.imf.org/external/np/oth/korea.htm. In addition, for a discussion on the historical origin of the IMF’s conditionality and its historical change (e.g., the increasing number of structural conditions), see Buira (2003).

There were three important differences between the Commission’s recommendations and the IMF’s restructuring program. First, the Commission did not specify the sequencing of the reforms. Second, the Commission did not offer recommendations on the resolution of the NPL problem, partly because it was charged with offering a “big picture” vision of reform, but also because its members—like most outside observers—were not aware of the depth of the problem. Third, although it recommended the establishment of a consolidated supervisor, the Commission did not fully address the issues related to the bureaucratic structure of supervision. See Park, Song and Wang (2004), fn. 4.

This is the definition adopted by the Korea Federation of Banks (KFB). The KFB kept records of the blacklisted credit defaulters for up to two years. However, due to the snowballing number of credit defaulters in 2003 and 2004, the MOFE decided to reduce the obligatory period for preserving credit records of credit defaulters from two years to less than one year in April 2005.

The four teams are the Macro-Prudential Supervision Team, Financial Industry & Market Team, Early Warning Team, and Financial Issue Analysis Team.

One source is the report by the Ministry of Finance and Economy entitled “Capital markets and financial investment services bill 2006” (2006).

Financial functions are classified by (i) financial services, (ii) financial investment products, and (iii) type of investors. “Financial services” are divided into six subcategories: dealing, arranging, asset management, asset custodian management, and discretionary and nondiscretionary investment advisory services. “Financial investment products” are further classified into securities or derivatives products depending on whether there is a risk of loss beyond the principal amount of investment. The act imposes more stringent consumer protection standards for financial investment products with a higher risk.

Major regulations to be scrapped include the prohibition of concurrent engagement in securities, futures, and asset management services; restriction on financial investment products; restriction on types of vehicles for collective investment scheme and classes of indirect investment securities; restriction on management of proprietary assets owned by an asset management company, trust company, and merchant bank; and obligatory registration with the Financial Supervisory Commission by securities issuers.


To create a Korean “Goldman Sachs” was an expression used by those bureaucrats who initiated the consolidation of capital markets.

In the U.S. Senate, some politicians—from both the Republican and Democratic Party—jointly proposed reenacting the Glass-Steagall Act to reimpose the separation of commercial and investment banking, which had been repealed in 1999.

By the end of 2005, there had been five commissioners, and none had completed his three-year term.

In the Japanese case, the staff of the Financial Services Agency are all public servants. This difference highlights that the Korean government was in a rush to reorganize the financial supervisory functions, but the change was still incomplete and problematic.

Three attempts were made to reform the FSC/FSS dual structure in 2000, 2002, and 2004, when financial scandals occurred, but all attempts failed and rather reinforced the bureaucratic control of the MOFE. For details of this process, see Kim and Yoon (2005)

Deleveraging is the process of banks paying off any existing debt on their balance sheets and closing credit lines.

IMF (April 2009).

For instance, the Financial Stability Forum published a report in April 2008 to set out an agenda for regulatory reform in various fields: strengthening prudential oversight on capital flows; enhancing transparency and valuation; changing the role and use of credit ratings; strengthening the authorities’ responsiveness to risks; and making