

The Australian APEC Study Centre

AT RMIT University

# REPORT ON THE SEOUL ROUNDTABLE MEETING

A COLLABORATION OF THE KOREAN INSTITUTE FOR  
INTERNATIONAL ECONOMIC POLICY (KIEP) AND THE  
MELBOURNE APEC FINANCE CENTRE AT RMIT UNIVERSITY  
(MAFC)

HELD AT KIEP, SEOUL, 23<sup>RD</sup> SEPTEMBER 2009

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# **REPORT ON THE SEOUL ROUNDTABLE MEETING – A COLLABORATION OF THE KOREAN INSTITUTE FOR INTERNATIONAL ECONOMIC POLICY (KIEP) AND THE AUSTRALIAN APEC STUDY CENTRE AT RMIT UNIVERSITY (AASC)**

## **Introduction**

The meeting was convened as a component of the visit arrangements to Seoul of the Victorian Treasurer, the Hon. John Lenders MP. The meeting was chaired jointly by Dr. Sangkyom Kim of KIEP and Ken Waller, Director of AASC and the Melbourne APEC Finance Centre (MAFC). The Minister and his party participated in a special session of the meeting, during which lunch was served; that part of the meeting was hosted by the President of KIEP, Dr. Wook Chae. Dr. Evanor Palac-McMiken, Counsellor (Economic), Australian Embassy, Seoul, Hae-Kyong Holdaway, Minister-Counsellor (Economic), Senior Treasury Representative, Tokyo and Ms. Prue Holdstein, Commissioner to Tokyo, Victorian Government attended the meeting. The complete list of participants is shown in the attachment to this report, together with a copy of the agenda.

The objectives of the round table were to deepen relations between Australia and Korea in financial services sectors, to promote understanding of the impact of the global financial crisis on the Korean and Australian and the region's economies, to consider the impact of the crisis on business, to promote Melbourne's expertise in financial services, and to consider issues arising from discussions relating to the proposed Australia Korea Free Trade Agreement.

## **Roundtable Discussions**

### ***Session 1. Macro economic policy perspectives on developments arising from the global financial crisis.***

Global imbalances were seen as the fundamental cause of the crisis, reflecting persistent US current account imbalances and these driven by high consumer demand in the US, massive trade surpluses of East Asian economies, offset by US bonds held by those economies. The depreciation of the US dollar against East Asian currencies and the Euro over the period 2002-07 had not improved the US trade balance. As a small open economy, the impact of external financial and exchange rate shocks on Korea have direct impact on real activity via trade and indirectly via asset price fluctuations. Despite an improving global economic situation, Korea faces continuing external risks. A tri-polar problem is the inter-linkages between global imbalances and financial and economic recovery. This problem had necessitated macroeconomic coordination by the G20 and an enhanced role for the IMF and regional facilities. Important to recovery is a slowdown in US consumption growth, a lower US trade deficit and increased domestic consumption in the Asia Pacific region. Regional currency coordination and a regional currency exchange system could contribute to stability. The prospects for a greater voice by the Asia Pacific in G20 and cooperation in regional financial and economic cooperation were noted as matters to be developed.

The low interest rate environment (in both real and nominal terms) had encouraged risk taking and had contributed to failures in regulatory systems both in the US but more widely. Basel II procedures in banking had not allowed for sufficient recognition of risks inherent in low-grade mortgage origination and distribution and for the spread of risk

through securitization to managed and pension funds. Despite notions of risk diversification, significant risks had been left on banks' balance sheets. Banks were found wanting and exposed to liquidity management problems and this exacerbated by sharply increased funding costs. The impact on the region was reflected in a sharp contraction in capital flows and credit growth and which contributed to a sharp fall in high-value industrial production.

The Australian economy had proven to be resilient to the crisis, with some albeit modest growth in GDP and the likelihood of unemployment peaking at lower levels than forecast. An easing of monetary policy and fiscal stimulus had contributed to the favourable position; banks were in a relatively strong position and lower interest rates had been passed on to borrowers. The uniform consumer credit laws in Australia encouraged careful consumer lending by banks. A question for banks is the extent to which they depend on sourcing funding from offshore wholesale markets. Australian forecasts point to weak global growth in 2009 and few economies would show positive growth. There is usually a quick pace to recovery following a major crisis but recovery from the financial crisis may be slower. Significant issues remain, namely global imbalances, the need for the US to export more and for China to increase its imports and to appreciate the yuan. Action by the US Fed in lending to other central banks and they in turn lending to commercial banks had been a significant and positive initiative.

Concern was expressed that there was little progress on global imbalances. Some academics in Korea argued that foreign reserves needed to be enhanced as a buffer against future shocks. An Australian perspective on ways to minimize external shocks was that of adjusting fundamental structures through a consistent reform program, including by improving education. As regards approaches in Asia, a shift in social policies would be important in giving societies confidence in lowering savings in favour of consumption. A question for China was how to speed up changes which would encourage a higher rate of domestic consumption. It was noted that Asian growth had been very strong and that the call now from G20 was for sustainable balanced growth. However, so long Asian economies continued to maintain strong export growth to China and China in turn continued strong exports to the US; it would be difficult to decouple US/China relationship.

There are new prospects for greater cooperation between China, Japan and Korea in resolving economic and financial imbalances and there are signs that the new Japanese government may be considering how Korea might act as a broker between Japan and China and the promotion of an East Asia community. Whether or not such a community would include the US is unclear at this juncture.

Concern was expressed about the dangers of financial system protectionism, where governments might restrict financial support programs to nationally owned banks rather than extending them to all banks.

## ***Session 2. Regulatory response to changing financial system landscape***

It was noted that the Australian regulatory system based on a functional approach and encompassing a holistic supervisory system was serving Australia well through the crisis. The Council of Financial Regulators chaired by the Treasury and including the Reserve Bank, the Australian Prudential Regulatory Authority and the Australian Securities and Investment Commission met regularly as the crisis unfolded and this

facilitated efficient communications between the authorities. A principles based approach to regulation facilitated dialogue with participants from the private financial sector. The supervisory agencies are well resourced and have broad ranging supervisory and enforcement powers. This provided for a robust framework and for system stability. Lessons had been learned after the collapse of Australia's largest general insurer HIH in 2001 and this had led to a review and to some changes to APRA. Australia has a proactive regulatory approach and the system is subject to review and reform as necessary. The government is actively involved in G20 and is attempting to influence the international debate, including in the Financial Stability Board, on international best practice supervision and regulation.

Bankers are resorting to best banking practices and returning to greater reliance on the deposit base and less on wholesale funds and are looking to improve liquidity management and to build their capital base. Asset Liability Committee meetings are conducted more regularly than they were in the pre crisis period and much greater attention is paid to credit quality and to capital management. While the supervisory system is important, banks are sharply focused also on factors that may impact adversely on reputational risk. The saga of Citibank highlighted vulnerabilities over the scale of investing in complex products and that banks that might suffer reputational risks were likely to do so for protracted periods. It was noted that ASIC is an effective consumer protection agency but that community education about the risk inherent in financial products was particularly important. Some Asian economies have under - developed consumer protection policies and this in part reflects the short-term investment horizon of Asian savers, compared with for example, the long-term savings view prevalent in Australia.

In Korea, the Financial Supervisory Board had developed a consolidated rules approach to financial institutions. It was noted that if markets are efficient, theory suggested that only a light regulatory approach was needed; conversely, inefficient markets required deeper regulatory supervision. The crisis pointed to serious market deficiencies and hence the call by the international community for reviews of regulations and practices.

### ***Special Session.***

The President of KIEP welcomed the Treasurer and his team and endorsed the collaboration between the Institute and the AASC. He noted that over recent decades, Australia and Korea had cooperated on many levels and on many matters, including on regional and multilateral issues. KIEP was established in 1990 as a government think tank and advised government on a range of policy issues, including the WTO, APEC, and OECD and on international economic cooperation and official development assistance. It was involved in developing positions on Korea's Free Trade Agreements and was the only such think tank in Korea specializing in regional studies; it undertakes analytical research on macro financial issues as well as being Korea's national APEC Study Centre.

The Treasurer thanked the President and the Korean team for the warm welcome and for organising the discussions. He thanked the President for the opportunity provided in the agenda for a discussion on Victoria's policies and prospects. He noted that with a population of 5.3 million, Victoria contributed 25% of Australia's gross product but with an ageing workforce, the central challenge was to boost productivity growth. He noted that the government had set a number of targets to enhance productivity, jobs growth

and a balanced budget. As a consequence of its financial probity, the state enjoyed a AAA rating, yet it is undertaking massive investments in workforce skills and in the education system broadly, in a broad band network and in critical water, transport and health sectors. He noted that competition is encouraged by an open trade and investment policy, reductions in taxes and improved financial services. The regulatory burden is being reduced and regulation is on a principles based approach. As the chief financial officer of the state he is required to reduce the regulatory burden by 5%, with performance measured on a world-class scale. The overarching guide is to balance the budget yet invest heavily in skills and infrastructure. He referred to the recent government publication – a prospectus - “A great place to do business: Growing Victoria’s financial services sector”, which had been distributed to participants in advance of the meeting.

Responding to questions over lunch, the Treasurer said he believed that confidence in Australia had been maintained during the global financial crisis and he anticipated that Victoria would record positive growth over the year. He stressed the need to resist protectionism at this time and that rather than go into protectionist mode, economies should seek to expand investment and trade in goods and services. He noted that he had held informative discussions with the Korean Investment Corporation and had discussed the Korean investment scheme.

Before departing from the meeting, the Treasurer thanked President Wook Chae for the hospitality extended to him during the visit, and welcomed the engagement between the Institute and the AASC and the MAFC. He welcomed further cooperation between Korea and Victoria and between the Centres and noted prospects in wealth management and pensions and financial services in both Korea and Victoria.

### ***The session continued with a discussion on the proposed Korea Australia Free Trade Agreement.***

In 2004, the government of Korea announced a road-map setting out strategic objectives for the pursuit of FTAs and for simultaneous negotiations with different groups of countries with the purpose of expanding trade and investment, increasing efficiencies and securing resources. Korea seeks comprehensive and high level FTAs. As regards negotiations with Australia, Korea is sensitive on agriculture and notwithstanding model generated gains, and assessments that show a bilateral FTA would deliver gains for countries, (increasing real GDP and welfare gains in both), Korea still had concerns. It was also noted that a FTA would support an already significant, highly complementary and growing trade and investment relationship between the two countries, but internal processes in Korea in getting political agreement could prove more difficult than the bilateral negotiations. Liberalising services was expected to be a difficult issue and compared with other FTAs in which Australia was a party, the prospects for financial services opening in an agreement with Australia were judged as providing only marginal benefits to Korea. Nonetheless, there is some prospect of the negotiations concluding next year and with entry into force in 2011.

It was noted that selling a FTA in a political economy reform process which had to deal with protectionist interests would likely have more chance of success if proposals were accompanied by adjustment and compensation arrangements. While there had been strong initial resistance in Korea to a FTA, understanding in the Korean public about potential benefits had improved. A question was raised that if Korea is seeking more

from an agreement in terms of access to knowledge in pensions and funds administration and wealth management, should not cooperation on such matters be reflected in an agreement? It was also observed that Korea has world-class expertise in derivatives and perhaps Australia could benefit from cooperation with Korea on derivatives markets. It was noted that Korea's agreements with ASEAN and with EU and the US provided for gradual opening of services markets and so agreements with other countries such as Australia, needed to take into account the impact on Korea's undertakings with those countries and groups.

Discussion focused on whether a multiplicity of FTAs may cause countries to substitute trade and investment patterns away from some countries and toward others without necessarily stimulating domestic structural reforms. In response it was noted that where FTAs develop economic linkages based on best practices, such developments may not necessarily cause an issue of substitution but rather one of encouraging market opening and efficiency gains.

### ***Session 3. Enhancing regional cooperation on trade and investment, governance and structural reform***

It was noted that the global financial crisis had caused a world-wide reduction in trade and combined with a sharp decline in domestic demand in Korea, businesses and investors in Korea had been seriously impacted; illustrated by sharply falling exports, household consumption, private sector construction, plant and equipment investment, services, FDI and GDP growth – starting from around the third quarter 2008. Notwithstanding some signs of recovery, encouraged by fiscal expansion, business expectations remain mixed and there remains a lack of confidence in the business and investor sectors. While business had been encouraged by earlier tax reforms, some revisions in 2009 to taxation, including repeal of a temporary investment tax credit and a rise in the minimum rate of corporate tax, could negatively impact on business investment. There had been some mitigation of regulations in capital city areas to ease factory building and extensions but labour laws continue to be seen as a major impediment to business, although there had been some improvements in the behavior of unions. The Korean government is seeking to revise labour-related laws and is applying the rule of law in labour disputes.

A question was asked as to whether there had been any real improvement in corporate governance following the global financial crisis. Based on a concept of “momentum strategy”, if a stock tracks upwards, the market tends to reinforce that trend; however, if this continues over time, it may well reflect an inefficient market process. Empirical studies to assess whether forms of governance contribute to value creation lead to questions of firms' ownership. Is the legal person a family based group, a state or a corporate entity, and to questions as to whether the CEO and the audit process is independent. The general findings of such studies point to conclusions that board structures are not that important in value creation. Ideas promulgated by the World Bank and the IMF in the early 90's which were focused on the elimination of family firms on the grounds that such firms performed less profitably than corporations with dispersed shareholding and independent boards, were now proving to be of dubious value. Around 35% of stocks of listed firms are owned by families and this is leading to conclusions, contrary to Anglo/Euro concepts, that family ownership is in fact conducive to value creation. Some further conclusions are that foreign ownership may have some influence on a company's behavior but it is often less strong in monitoring firms'

behavior than might be expected. Doubt was expressed that there is some convergence to a world model of corporate governance. Many firms (including family owned firms) exhibit intrinsic values. An unresolved question is the extent of the influence of forms of governance arrangements on firms' performance and value creation.

It was observed that real ownership structures in Korea had not changed significantly. It was also observed that corporate structures involving principal/agent relationships do require regulatory oversight and government intervention. A key question in the performance of family owned firms is the incentive arrangements that are in place.

The growth of wealth management globally and in Korea raised a range of issues that need to be addressed, including risk management, governance, investor education and the development of skills. From a perspective of cooperation between Australia and Korea on such matters, there is already valuable momentum. Areas of common interest could be to undertake research on the efficiency of capital markets, the impact on those markets of the global financial crisis and the relevance of regulatory frameworks. There is available a depth of knowledge in universities to contribute with research and in investor education. The Melbourne Centre for Financial Studies is developing relationships with Harvard University and there is much that continued collaboration between Australia and Korea and KIEP and the AASC can do to promote financial services and education.

In closing the discussions, the Director of AASC thanked Dr. Sangkyom and his team for the excellent arrangements made for the meeting and the hospitality extended. He noted the quality of the discussions and the range of subjects considered and that areas of future cooperation had been identified such as risk management, governance, regulatory systems and financial markets, trade and investment and macroeconomic policy issues. He strongly hoped that this form of dialogue would be continued between the two Centres. Dr. Sangkyom endorsed the value of the dialogue, welcomed the opportunity of collaboration between the two centres and looked forward to continuing cooperation to promote the APEC agenda in the region.

## Attachment A: Roundable Agenda



### Seoul Roundtable – Collaboration of the Korea Institute For International Economic Policy and The Melbourne APEC Finance Centre At RMIT University

Seoul, 23<sup>rd</sup> September 2009

OFFICES OF KIEP, SEOUL – 3---4 Yomgok-Dong, Seocho-Gu  
1370747, Seoul

#### Start of Roundtable discussions

#### WELCOME

09.30-09.40am *Welcome remarks by KIEP and by Ken Waller, Director, Melbourne APEC Finance Centre*

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#### **SESSION 1. *Macroeconomic policy perspectives on developments arising from the global economic and financial crisis***

With a focus on impact on economic growth and financial markets in Korea and Australia and on the Asia Pacific region, including access to bank credit and bank lending, financial system stability and growth and inflation outlook over the medium term

09.40-09.55am Dr. Yonghyup Oh, Director, International Macro Economics and Finance Division, Korean Institute for International Economic Policy

09.55-10.10am Mr. Chris Ryan, Head International Markets, Reserve Bank of Australia

10.10-10.30am Open discussion

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#### **SESSION 2. *Regulatory responses to changing financial system landscape***

With a focus on any recent and prospective changes in key regulatory approaches in Australia and Korea and approaches to enhance regional financial system supervisory cooperation

10.30-10.45am Hae-Kyong (HK) Holdaway, Minister-Counselor (Economic), Senior Treasury Representative, Australian Embassy, Tokyo

- 10.45-11.00am Representative from Korean regulatory agency (TBC)
- 11.00-11.15am Craig Burgess, Head of Private Bank, North Asia , Australia and New Zealand Banking Group Limited (ANZ)
- 11.15-11.30am Open discussion
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**Arrival of the Hon. John Lenders, Treasurer of Victoria, Minister for Financial Services and Minister for Information and Communications Technology and his party.**

**SPECIAL SESSION *Perspectives on Australia's handling of the global financial crisis and prospects for Victoria's financial services sector and opportunities for deeper Korean business engagement in Victoria.***

- 11.30-11.45am Mr. John Lenders, Treasurer
- 11.45-12.00pm Open discussion – on the Treasurer's comments and on issues arising in the morning sessions

(A working lunch box will be served and discussions continued over lunch).

- 12.00- 12.30pm *Exchange of views on proposed Korea Australia Free Trade Agreement.*

With a focus on guiding philosophy; coverage and content and with views on investment openings and prospective two-way opportunities for finance sectors, e.g. Funds and asset management and securities.

- 12.30-12.40pm Dr. Hansung Kim, Head of FTA Team, Trade and Investment Policy Division, Korea Institute for International Economic Policy.
- 12.40 -12.50pm Mr. Syd Bone, Chairman, Melbourne Centre for Financial Studies.
- 12.50-1.00pm Open discussion
- 1.00-1:15pm The Treasurer gives his concluding comments; thanks KIEP for organizing and hosting the round table and for the cooperation between KIEP and the Melbourne APEC Finance Centre and thanks all participants for their contribution to the discussions.

**The Treasurer and his party depart KIEP.**

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### **SESSION 3**

***Enhancing regional cooperation on trade and investment, governance and structural reform***

With a particular focus on measures that can be promoted in regional groupings involving Korea and Australia and whether new initiatives may be relevant

1.15- 1.30pm      Dr. Song Wongun, Research Fellow, Korea Economic Research Institute

1.30 – 1.45pm      Tony Naughton, Professor of Finance and Head School of Economics, Finance and Marketing, RMIT University

1.45- 2.00pm      Open discussion

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## **CONCLUSION**

2.00-2.15pm      Concluding remarks  
Dr. Sangkyom Kim  
Mr. Ken Waller

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## **Attachment B: Participants**

### **The Korean Delegation**

**Mr. Wook Chae**, President, Korea Economic Research Institute

**Mr HangSung Kim**, Head of FTA Research Team, Department of Trade and Investment Policy, Korean Institute for International Economic Policy

**Mr. Sangkyom Kim**, Executive Director of Korean National Centre for APEC Studies, Korean Institute for International Economic Policy

**Mr Yonghyup Oh**, Director Department of International Macro-Finance, Korea Institute for International Economic Policy

**Mr. Young-Joon Park**, Associate Research Fellow Dept of International Macroeconomics and Finance, Korea Institute for International Economic Policy

**Mr. Wongun Song**, Research Fellow, Economic Research Division, Korea Economic Research Institute

**Mr. Jeongmeen Suh**, Research Fellow, WTO Research Team, Dept of Trade and Investment Policy, Korea Economic Research Institute

**Mr Jong Joon Jang**, Research Fellow, FTA Research Team, Dept of Trade and Investment Policy, Korea Economic Research Institute.

### **The Treasurer's Delegation**

**The Hon John Lenders MP**, Treasurer, Victoria Government

**Mr David Bell**, Economics and commercial advisor to the Treasurer, Victoria Government

**Mr. Justin Pascoe**, Acting Chief Executive Officer, Victorian Funds Management Corporation

**Ms. Prue Holstein**, Victorian Government's Commissioner for Tokyo, Victoria Government

### **The Australian Delegation**

**Mr. Ken Waller**, Director, Australian APEC Study Centre at RMIT University

**Mr. Chris Ryan**, Head International markets, Reserve Bank of Australia

**Ms. Hae-Kyong (HK) Holdaway**, Minister-Counsellor (Economics), Senior Treasury Representative, Australian Embassy, Tokyo

**Mr. Craig Burgess**, Head of Private Bank, North Asia, ANZ Banking Group

**Mr. Syd Bone**, Chairman, Melbourne Centre for Financial Studies

**Professor Tony Naughton**, Professor of Finance and Head of School of Economics, Finance and Marketing, RMIT University

**Dr. Evanor Palac-McMiken**, Counsellor, Australian Embassy, Seoul