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Towards a Better Framework for Supply of Funds in Asian Financial Markets: Lessons from Korea

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abstract

Despite great importance of SMEs in Korea (with 99.9% of total number of companies), financing for SMEs has proven difficult for Korean SMEs. More than 95% of their funding comes from banks and policy institutions, with very little raised from capital markets. Banks are also reluctant to provide financing to SMEs due to higher delinquency rate than other loans. Corporate bond spread between large corporations and SMEs have been significantly higher than those of other countries.

In order to reduce funding difficulties of SMEs, the Korean government has adopted three broad policies: (i) availability expansion policy, (ii) access enhancement policy and (iii) corporate restructuring policy. These policies have been generally successful in reducing funding difficulties of SMEs over the years, although certain improvements remain to be done.

Key lesson from the Korean experience is to adopt measures to reduce market failures, i.e., (i) reduce asymmetric information both from the supply and demand side, (ii) establish robust policy support system where market failure is prominent, through well defined institutional framework as well as appropriate policy priorities, (iii) develop capital markets for SMEs and (iv) introduce strong corporate restructuring system to separate 'good' SMEs from the 'bad'.