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Nakornthon Bank

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Nakornthon Bank

Introduction

In the evening of Friday, February 19, 1999, Hyung Lo, Strategic Planning Manager at Nakornthon Bank in Bangkok, Thailand, stared at the stack of papers on his desk. On the following Monday, he was to deliver to the board of directors his opinion of the value of each option Nakornthon faced. Nakornthon needed capital in order to stay in business. The economic crisis of July 1997 had seriously affected the ability of Nakornthon's debtors to repay their loans. As a result, the Bank incurred substantial losses over the last six quarters, deteriorating almost all the existing equity in the business.

Over the last few months, Nakornthon had been in negotiations with a number of foreign banks as potential partners. If Nakornthon partnered with a foreign bank, the Wang Lee family would be able to maintain ownership of some tiny portion of the bank. The Bank has also signed a memorandum of understanding with the Bank Of Thailand to possibly participate in a recapitalization scheme. If Nakornthon applies for a government bail-out with the Bank of Thailand, existing equity shares in the bank would be essentially written down and the Wang Lee family would lose control of the bank. Both of these alternatives would be better than closing the doors of Nakornthon for good.

Discussions with foreign banks had been going on since early 1998. Nakornthon spoke extensively with the Bank of Nova Scotia, but the two sides could not agree on price. Two other banks, United Overseas Bank of Singapore and Standard Charter of the United Kingdom, have also expressed interest in acquiring a majority stake in Nakornthon. The foreign banks are currently conducting due diligence and will essentially submit bids. However, the Bank of Thailand will play a key role in choosing a strategic partner due to the high levels of risk associated with non-performing loans.

Hyung Lo has been asking himself the following questions to remain objective: Would any foreign bank be willing to invest in Thailand yet? Could Nakornthon recover without foreign recapitalization? If so, who would be the best fit? Can the government bail-out provide enough cushion for Nakornthon to get back into the black? Does Nakornthon really have any value? Would Nakornthon's shareholders be better off if all of its assets were liquidated? Hyung Lo needed to be able to provide insight to these questions for his presentation to the board on Monday (See Exhibit 1).

Road to Devaluation

The first sign of pressure on the Thai baht came in July 1996. Concurrently, the Bangkok Bank of Commerce collapsed and a number of international banks began to unwind their carry trades (borrowing in dollars or yen and lending in local currencies). These events forced the Bank of Thailand (BOT) to inject liquidity into the financial system to support the baht (See Exhibit 2).

In the beginning of 1997, Thailand released poor fiscal and export numbers for the end of 1996. In addition, a downturn in the real estate market put many property developers in the red. Pressure on both the manufacturing and real estate sector caused companies to begin to default on interest payments.

In March, as an attempt to avoid a crash in the banking system, the Thai government announced that it would buy \$3.9 billion in property development loans from finance companies. That did not happen. Later in the spring of 1997, interest rates in the U.K., Germany and Japan decreased. In May of 1997, reports leaked that Thai finance companies became large sellers of baht for dollars and that the BOT directly contacted foreign investment banks to sell forward a large amount of dollars. The BOT forward interventions attempted to maintain interest rates and to not rattle an already fragile financial sector. In mid-May, BOT stopped intervening and allowed interest rates to rise and instituted capital controls to segment the on- and offshore markets.

By the end of June, BOT's forward book was \$26 billion and BOT's reserves were \$28 billion. Realistically, BOT had only \$2 billion with which to maintain the baht. With the imposition of capital controls, market participants assumed that devaluation was pending. However the timing of the announcement of the float on July 2, caught most participants by surprise. The baht dropped by 15% in the first day following the announcement. Initial reactions on the Thailand stock exchange pushed the market higher. The optimism deteriorated as it became known that the BOT's massive forward foreign exchange liabilities limited its ability to provide any support for the baht.

When the dust settled, Thailand had spent \$32 billion of \$33 billion official reserves from January 1997 to August 1997 in a failed attempt to defend the baht. The Thailand government identified four major problems: net internal reserves were depleted because of the baht defense, systemic problems exist in the financial sector, the financial sector faced a serious liquidity shortage, and the regional economic turmoil poses a significant constraint in the country's ability to recover.

In order to overcome the currency and financial crisis, Thailand enlisted the support from the IMF, the World Bank, and the Asian Development Bank. Key to the economic recovery is the restructuring of the financial sector. Toward this goal, three main steps are underway: 1) segregation of viable and unviable financial institutions, 2) strengthen the operations of and prudential supervision and regulation of the remaining institutions, and 3) capital market reforms.

By August 1997, 33 of 91 financial institutions were deemed viable and left operating. The Financial Restructuring Authority (FRA) took control of the remaining 58 insolvent financial institutions. The FRA allowed two of the 58 institutions to restart. The FDA liquidated the assets of the other institutions for 37% of their face value. To restore public confidence in the remaining operating institutions, the government created the Financial Institutions Development Fund (FIDF) to provide a guarantee of the deposits and liabilities of the remaining financial institutions. This fund will be phased into becoming self-financed by a limited deposit insurance plan.

The second step toward recovery involves strengthening the remaining institutions. BOT announced new asset classification and provisioning requirements and relaxed the restriction on foreign ownership in Thai financial institutions. BOT wants to bring the loan classification and provisioning rules and accounting standards in line with international best practices. The goal is to increase both the internal supervisory and technical functions of the financial institutions. Relaxing the foreign ownership helps the industry by strengthening the capital base. (After 10 years, foreign shareholders could maintain or lower but not raise their stakes in Thai institutions until the stake is less than 50%). BOT now requires banks to maintain a minimum capital adequacy ratio of 8.5%.

The IMF focused an aid package to help the Thai government through the reform process. Outside experts will help to develop recommendations:

- to improve accounting practices
- to create incentives for proper corporate governance
- to adjust the legal framework for the facilitation of bankruptcies and foreclosures
- to improve corporate external debt management and exchange rate risk management
- to enhance the government's ability to monitor the country's capital flows.

The overall efforts toward change should help Thailand rebound from the crisis and prevent a relapse.

Thailand: General Background

Thailand boasts one of the most diverse economies in South East Asia. Since the 1970's, the economy has transitioned from an import substitution based manufacturing base, to a manufacturing base targeted

at export to high technology manufacturing of computer and automobile parts. The 1997 turmoil underscored the need for further reform, especially in the financial system. The belief that cheap capital could be used to fund current-account deficits, which would be corrected once capital goods imports translated into higher-technology, higher value-added exports, was not grounded.

Thailand: Government Institutions

As a general comment, Thailand's government institutions are firmly established and display a high degree of sophistication and business savvy. Evidence of this can be seen through the extensive web site offerings of each ministry and major government entity.

Government

There is a history of corruption, military dictatorship and influence and weak coalitions in Thailand's government. The government is set up as a Constitutional monarchy with King Bhumibol Adulyadej as the ninth monarch of the 214-year-old Chakri dynasty. In 1973, the last of the military strongmen was removed in a student-led uprising. However, in 1991, there was a military coup. The junta installed the retiring army chief, General Suchinda Kraprayoon. Through the king's intervention, Suchinda was forced to step down and Anand Panyarachun was appointed head of a second interim government.

The New Aspiration Party (NAP), led by Chavalit Yongchaiyudh, who had engineered the revolt against Banharn, gained a narrow two-vote margin over Chuan's Democrats in the election that was held in November 1996. Chavalit was able to assemble a six-party coalition. However, Chavalit was blamed for failing to shore up the banking system and for squandering reserves in a futile defence of the baht. Once Thailand became embroiled in economic crisis after the collapse of the baht on July 3rd 1997, Chavalit's indecision and uncertain commitment to the IMF-led rescue plan destroyed his credibility, both domestically and internationally, and in November 1997 he was forced to step down.

Legislature / Parliament

Thailand is a unitary state, and that situation is unlikely to change greatly despite efforts under the new constitution to modify the pivotal role played by Bangkok. Under legal changes approved in early 1998, about 100 city and municipal councils will in the future get much of their revenue from sales and land taxes, instead of relying solely on central government grants. Until now, only the Bangkok Metropolitan Administration has had an adequate tax base. However, effective power will remain with the centralised bureaucracy.

Parties tend to be based on personalities, not ideology. Traditionally power-brokers have spent large sums to attract popular candidates and secure votes, with a view to recouping this outlay once in government.

Legal System

One of the major barriers to economic recovery and effective integration of the Thai economy is the outdated legal system. Indeed reform of the legal system is one of the mandates of the IMF package. Many of the rules and regulations presently on the books date from the 1930's and 1940's and were not designed to deal with the types of economic and business issues presently facing the country. Two principal examples of this are the Thai laws governing foreclosure and bankruptcy.

In general the foreclosure process is extremely long and cumbersome, and the laws governing bankruptcy discourage lending to fundamentally sound companies experiencing temporary difficulties. Although some measures have been passed to update these laws, additional necessary reform languishes in parliament. The personal interests of politicians are one of the fundamental barriers to passage of legislation and regulations that would strengthen the remedies of creditors. Many politicians have substantial business and real estate investments in Thailand. They have little incentive to pass laws that

aid creditors in foreclosure proceedings. Ultimately most experts predict that overwhelming national interests will force passing of the necessary revisions.

Although foreclosure laws are still outdated, the Thai parliament, in March 1998, did pass a new Bankruptcy Act. The new Act replaces the previously existing laws, which date from 1940. Under the old laws creditors which granted additional monies to a debtor, knowing the debtor was insolvent, were not entitled to file a claim for repayment. Although the reformed regulations are not ideal, they do for the first time allow for reorganization as an alternative to liquidation. The Act incorporates elements of Chapter 11 of the US Bankruptcy Code.

The importance of passing updated laws is highlighted by the negative impact current rules have on realized values at government auctions of bad loans and foreclosed properties. Foreign investors are reluctant to bid aggressively at these auctions given the weak remedies presently available. This hinders Thailand's recovery efforts. A continuing problem is that Thailand's legal system is not large enough to deal with the tremendous volume of bankruptcies and foreclosures precipitated by the crisis.

Central Bank of Thailand

The primary roles of the BOT are to formulate monetary policy to maintain monetary stability, supervise financial institutions, act as banker to the Government, act as banker to financial institutions, manage international reserves and to print and issue bank notes.

Prior to the crisis the Central Bank of Thailand was highly regarded for its prudent monetary policies. Evidence of its prudence can be seen in the restrictions placed on real estate lending as early as 1995. However, weak handling of the debt crisis has tarnished the bank's reputation. **Since then the BOT has sought ...**

Stock Exchange

Thailand boasts two stock exchanges, the Stock Exchange of Thailand (SET) and the Bangkok Stock Dealing Center (BSDC).

Stock Exchange of Thailand:

The Securities Exchange of Thailand, as it was first named was created as part of the SET Act of May 1974. Securities trading commenced on April 30, 1975. The Securities and Exchange Act of 1992 (SEA) replaced the SET Act and established the Securities and Exchange Commission (SEC) as the sole supervisor of securities business. The SEA is a comprehensive legislative framework regulating areas such as disclosure, investor protection, fund management, takeover procedures and the establishing of securities firms.

The SEA defines three prime objectives for the SET:

1. provide a center for trading listed securities and the system and method for securities trading;
2. undertake any related business, such as acting as a clearing house, securities depository center, securities registrar and providing securities data; and
3. undertake any other business given the approval of the SEC.

The SET has experienced tremendous growth since its inception. Some highlights:

- at the end of 1975 there were 21 companies listed, and trading turnover for the year totaled 547 million baht;
- for 1993, annual turnover reached 2,201 billion baht;
- on January 4, 1994, the market opened at an historic high of 1753.73 Index points and the following day recorded its highest-ever trading turnover of 40.01 billion baht; and

- at the end of 1998, 413 companies were listed and, the Index closed at 355.8. Turnover for the year totaled 855.17 billion baht.

Bangkok Stock Dealing Center:

Thailand's second exchange is the BSDC, which is another secondary market for securities trading. Trading on the BSDC started on November 14, 1995, following its formation in October of that year. It has 74 finance and securities companies as founder members. It is a Self-Regulatory Organization (SRO) and non-profit organization under the jurisdiction and supervision of the Securities and Exchange Commission of Thailand (SEC).

Primary goals of the BSDC are:

1. To act as a secondary market in order to increase liquidity and promote private investment as a fundamental for the future development of Thailand's capital market.
2. To create opportunities and boost confidence among small- and medium-size growing business entities which wish to employ the secondary market to mobilize funds for business expansion.
3. To create more saving opportunities for individual investors.

Securities and Exchange Commission:

Prior to 1992, oversight and regulation of the Thai securities markets was uneven and fell under the jurisdiction of various government agencies. Recognizing the importance of an effective stock market to the long-term economic goals of the country, the government in 1992 passed the Securities and Exchange Act. Formation of the Thai Securities and Exchange Commission was one outcome of this legislation.

The Financial Sector Restructuring Authority (FRA):

Established on October 24, 1997 in accordance with the Emergency Decree on Financial Sector Restructuring. The FRA was created as an independent body to oversee the rehabilitation of 58 finance companies whose operations were suspended by the order of the Finance Minister on June 26, 1997 (16 companies) and August 5, 1997 (42 companies) and to safeguard the interest of depositors and investors.

Thailand: Current Situation and Future Prognosis

Banking Industry: The primary challenge facing the Thai government is to restore confidence in the economy and speed resolution of the banking capital crisis. To this end, the Ministry of Finance and the BOT, in August 1998, announced a comprehensive reform package. The centerpiece of this package was a two tiered public support scheme designed to increase capital and liquidity in the Thai banking industry.

Tier 1 Capital Support Scheme:

Under Tier 1 of the scheme, the troubled bank issues preferred shares to the Thai government in return for tradeable, 10-year government bonds. A key requirement of this scheme, is that the bank must fully provision for all non-performing loans immediately. Losses on the loan portfolio will be borne by the existing shareholders, and new public and private capital will have preferred status to ensure this. NPL's, after full provisioning, stay on the books of the bank. Government capital will be injected in an amount equal to the amount provided by a private investor, which will likely be a foreign bank. If the capital adequacy ratio is still below 2.50% the Thai government will inject additional funds up to this level. Private investors can buy the government shares within three years after the injection.

Tier 2 Capital Support Scheme:

Under Tier 2 the bank issues subordinated debentures to the government in exchange for non-tradeable 10-year government bonds with a matching maturity. The BOT retains the right to convert the debentures into Tier 1 stock if the capital adequacy ratio falls below 2.5%. A notable negative feature of the Tier 2 scheme is the negative arbitrage that exists between the subordinated bonds issued to the government, and

the government bonds received by the bank. The net effect is a drain on the precious cash of the troubled bank.

Loan Classification and Provisioning Rules (LCP):

These recently revised rules, promulgated by the Bank of Thailand, detail the calculation of capital adequacy ratios. Certain elements of these regulations have been relaxed to provide breathing room to troubled financial institutions.

- *Tier 1 Capital:* Consists of paid in capital, perpetual preferred shares, warrants, legal reserves and retained earnings.
- *Tier 2 Capital:* Tier 2 is more broadly defined than Tier 1 and consists of revaluation reserves, statutory reserves, preferred shares, perpetual debt, convertible debt and subordinated debt.
- *Risk Weighted Assets:* consists of all assets on the balance sheet together with certain off balance sheet items. The bank must set aside reserves for possible charge-offs and losses. The reserve amount is calculated based on the following table:

Asset Classification	Old Reserve Requirement	New Reserve Requirement
Performing, Pass	None	1% of amount
Performing Special Mention	None	2% of amount
NPL Sub-Standard	15% of Sub-Std. Amount	20% of amount less collateral
NPL Doubtful	100% of Doubtful amount	50% of amount less collateral
NPL Non-collectible	100%	100% of amount less collateral
NPL Loss	100%	100% of amount less collateral

Overall Economy:

According to official Thai government papers filed with the IMF, Real GDP is expected to grow 1.0% in 1999 vs. a 7.0% decline for 1998. The moderate full year increase masks an expected continual strengthening during the year. Indeed growth in the 4th quarter of 1999 is projected at a robust 3-4%. Inflation is anticipated to moderate to 2-3.0%, vs. 1998's 9.2%. The current account balance is expected to stabilize at \$11 billion, while official reserves are expected to increase further to \$32-34 billion vs. \$26 billion at the end of 1998 (See Exhibits 4 and 5).

One of the major challenges facing Thailand is that of privatization of the government's vast business holdings. While many privatization efforts were contemplated and/or planned prior to devaluation, current economic conditions significantly increase the pressure to sell these entities. The five agencies slotted for urgent privatization are: Airports Authority of Thailand (AAT), State Railways of Thailand, Electricity Generating Authority of Thailand, the Telephone Organization of Thailand and the Communications Authority of Thailand.

While the economic incentive to privatize is compelling, powerful political interests have impeded progress. For example, a major factor delaying privatization of AAT is that it is under *de facto* control of the Royal Thai Airforce. The main asset of the AAT is Bangkok's airport, which generates \$150 million a year for the Airforce.

Sovereign ceilings for foreign currency ratings	Bonds and Notes		Bank Deposits	
	Long Term	Short Term	Long Term	Short Term
Thailand	Ba1	NP	B1	NP
Indonesia	B3	NP	Ca	NP
Vietnam	B1	NP	B3	NP
Korea	Baa3	NP	Ba2	NP

Philippines	Ba1	NP	Ba2	NP
Malaysia	Baa3	NP	Ba1	NP

Source: Moodys Investors Services

Nakornthon Bank: Business Lines



NTB offers a full range of commercial banking services, but specializes in trade finance and foreign exchange operations. NTB has a relatively small branch network (70 as of the end of 1998, with the majority located in Bangkok), which restricts its ability to generate funding. The bank's small size has necessitated the formation of partnerships and joint ventures to expand the product offering and improve service levels. NTB entered into a joint venture with Citibank to improve the operation and management system. To diversify its revenues NTB has partnered with Schrodgers to offer mutual funds, and has also initiated debt underwriting and trading activities. NTB was the first bank in Thailand to issue a multi-function global ATM/debit card. Other products offered by NTB include: overdraft facilities, short and long term loans, bank guarantees, acceptances, avals, treasury services and cash management.

Nakornthon Bank Loans by Sector (%)	Fiscal Year 1996	Fiscal Year 1997
Agriculture	1.6	2.2
Mining	0.2	0.2
Manufacturing	40.8	43.2
Commerce	22.0	23.0
Real Estate	11.0	8.9
Construction	2.6	2.8
Public Utilities	2.5	2.6
Services	6.3	6.2
Personal	18.0	15.0
Banks/Finance	3.9	2.9

Nakornthon Bank: Ownership

As with many businesses in Thailand, NTB has a family of Chinese descent as its majority owner. In this case, the Wanglee family. Founded in 1933, NTB is the second oldest commercial bank in Thailand, and was known as the Wang Lee Bank until 1985. Shares of NTB have been traded on the Thai Stock Exchange since 1985. As of January 24, 201,606,000 shares were issued and outstanding. NTB shares are traded on the SET, and members of the Wanglee own a large percentage of the company. Crown Property (an investment vehicle of the Thai government) owns approximately 5% of NTB's common stock. The tradition of family control of companies has created difficulties in reforming Thailand's economy as many of these families are unwilling to sell ownership in these entities. From a practical standpoint many of these families will be financially devastated by the sale of their ownership at current reduced prices (See Exhibit 6).

Top five shareholders of Nakornthon as of April 1998 were as follows:

Shareholder	Number of Shares	% of Total Shares
Nomura Singapore	20,083,950	9.96
Crown Property Bureau	10,274,101	5.10
Wanglee Co., Ltd.	7,000,000	3.47
Muangthai Life Assurance	5,349,076	2.65
Wanglee Holding Co., Ltd.	5,245,459	2.60

Strategic Forward

Nakornthon Bank ("NTB") is facing a tumultuous period while the Wanglee family decides the bank's fate. NTB can either apply for a Tier-1 recapitalization with the Bank of Thailand or it can seek out a strategic partner to provide it with an infusion of capital. Analysts believe that NTB will opt for foreign majority ownership over nationalization saying that it is "the lesser of two evils." The founders and major shareholders of Nakornthon Bank conclude that foreign partnership is the best way to guarantee the bank's future.

Under the Financial Restructuring Program, legislators believed that all Thai banks would eventually seek Tier-1 capital increases from the Bank of Thailand. NTB has contacted the Thai banking regulators over their recapitalization plans since NTB does not have an adequate capital base as required by the central bank. NTB has signed a memorandum of understanding with the Bank of Thailand to participate in the government's Tier-1 capital injection scheme, effectively hedging its current uncertainty. Thailand's banking officials have set June 1999 as the first deadline for banks to satisfy capital adequacy requirements. According to the central bank, "Nakornthon Bank may join the Tier-1 scheme before seeking a foreign partner or it may let the Financial Sector Advisory committee pick the foreign partner on its behalf." As of yet, the Thai central bank has not considered NTB's case since it has potential foreign partners.

The banks that survived the economic crisis in July 1997 have been looking to foreign partners to assist them out of difficult situations. In 1998, ABN-Amro acquired a majority stake in the Bank of Asia and the Development Bank of Singapore holds more than a 50% stake in another local bank, Thai Danu. A deal with Nakornthon has been in the air since early 1998 when the government eased foreign ownership laws (shareholder regulations). Foreign banks wanting to expand global operations at "fire sale" prices began scouring the Thai market for potential takeover targets. Many banks were interested in NTB because the bank has sufficient liquidity and has not borrowed from the central bank, unlike many other banks, since the economic crisis. NTB even completed a rights issue in February 1998 for about 670 million baht (US\$17 million). And even though NTB's non-performing loans (NPLs) increased due to the economic slowdown, the level is still below the industry average of around 30%.

In February 1999, Nakornthon Bank said it expected to select a strategic partner by March 1999 and complete its recapitalization program by June 30. NTB has received three separate letters of intent from prospective strategic partners. The three potential suitors ("Acquirers") are Standard Chartered Bank of the United Kingdom, Bank of Nova Scotia of Canada and United Overseas Bank of Singapore. The banks requested to begin final due diligence from February onwards. Since NTB is burdened with non-performing loans and operates in a difficult environment, the due diligence process for the acquiring banks involved is crucial.

Each of the three acquirers has some level of operations in Thailand. As the recovery process from the Asian economic crisis is taking place, the three banks want to gain a stronger foothold in the Thai market

at bargain basement prices. The Thai market is still considered a buyer's market with the acquirers having substantial bargaining power. The acquirers would gain access to foreign allies and networks which is deemed beneficial, but the banks are expected to impose tough conditions for any deal to go through.

Bank of Nova Scotia (Canada)

Probably the first bank to be interested in Nakornthon Bank was Bank of Nova Scotia ("BNS") or Scotiabank, the most international of Canadian banks. BNS employs approximately 41,000 people and operates more than 1,700 branches in almost 50 countries. The bank provides a complete range of retail, commercial, corporate and investment banking services to customers around the globe. Interestingly, S&P recently downgraded BNS due to the bank's international exposure, but BNS's CEO and President both believe that long-term outlook for emerging markets offer excellent potential. Almost half of the bank's 1998 earnings were generated from international operations and the expansion process continues. Their goal is to grow global revenues and realize higher returns while reducing corresponding risks.

Bank of Nova Scotia received representative office license in Thailand in 1980. In 1993, BNS received its Bangkok International Banking Facilities license in 1993 allowing the bank to lend foreign currency in the Thai market. The bank received its full banking license in 1996 and opened its first branch on July 2, 1998. BNS currently operates 2 branches in Thailand specializing in commercial, trade and investment services.

Bank of Nova Scotia spent over six weeks reviewing Nakornthon's financial statements mid-1998. Eventually, BNS made a low offer that reflected concerns over NTB's high level of bad debt. Although excessive debt and a cash shortage make Asian businesses seek foreign investment; many companies still resist the idea of letting "outsiders" run the show. In June 1998, BNS suspended talks to take over NTB after the two parties failed to agree how much the bank was worth and amidst an unwillingness on the part of the Thai bank managers to step aside after the take over.

However, Bank of Nova Scotia remains interested in NTB. There have been numerous rumors that have been vehemently denied by both parties that the Bank of Nova Scotia has acquired a majority stake in Nakornthon Bank, some as recent as January 18, 1999.

United Overseas Bank (Singapore)

After talks with Bank of Nova Scotia stalled in June 1998, Mr. Vorawee Wanglee, Nakornthon Bank's Chief Executive Officer, visited Singapore to seek a strategic and investment partner. United Overseas Bank emerged as the Singapore candidate.

Voted "Asiamoney's" 1998 Commercial Bank of the Year, the United Overseas Bank ("UOB") provides a wide variety of banking products and services to individuals and organizations. The bank's network is comprised of 137 branches (including 63 overseas offices) of which 3 are in Thailand.

With new opportunities created by the economic crisis, Singapore's equity investments in Thai companies almost doubled to 18.3 billion baht last year, moving Singapore companies to third place among foreign investors. The sharp rise was due to DBS's purchase of a controlling stake in Thai Danu Bank in 1998. Also, the Government of Singapore Investment Corporation bought a 15% stake in Thai Farmers Bank and smaller stakes in Bangkok Bank, National Finance, Securities One and Nation Multimedia. The trend for Singaporean companies to purchase Thai organizations subsists due to the geographical proximity, incentive schemes and advantageous currency situation.

Although Nakornthon Bank fits in to United Overseas Bank expansion plans, UOB has kept a low profile during the courting and due diligence process. Despite NTB being up for sale for months, the main

sticking point for UOB is price. According to bank analysts, the Thai banks have pegged their share price too high and UOB does not want to pay so much.

Standard Chartered PLC (United Kingdom)

Standard Chartered has also been denying reports surrounding the possible take over of NTB. Krungthep Turakit, a Thai language business daily, irresponsibly reported that Standard Chartered was one of three banks schedule to sign a memorandum of understanding on a stake in NTB. The inaccurate report caused the Stock Exchange of Thailand to suspend trading in Nakornthon's shares until the news could be clarified. Dru Narwani, Standard Chartered chief executive for Thailand, said his bank is discussing the possibility of acquisition with more than one Thai bank, but hasn't reached any conclusion yet.

Standard Chartered Bank, founded in 1853, is an international banking group that focuses its activities in Asia, Africa and the Middle East. Employing around 25,000 people, the bank's network consists of over 600 offices in more than 40 countries. Standard Chartered specializes in Personal Banking, Corporate Banking and Capital Markets.

Sir Patrick Gillam, the chairman of Standard Chartered, said "the current turbulence in Asia leads us to be cautious about the short term, recognizing that we face a challenging environment. However, we remain confident about both the fundamentals of Asia and the long term prospects for Standard Chartered."

The bank has been in Thailand for more than 100 years. Standard Chartered's Thai branch focuses on wholesale treasury, custodial services and global corporate business. The current branch also offers local corporate banking and consumer banking, but this would be handled by a newly acquired entity if/when a deal goes through.

Standard Chartered simply wants control to grow its asset base in Thailand. Since the central bank controls approximately 800 bank branches in Thailand, Standard Chartered's repeated requests for a license to open 20 new branches in the country have been ignored.

Standard Chartered's main objective is a branch network. The bank is keen on acquiring a small, strategically located branch network in Thailand with half its branches in Bangkok and the other half scattered around the country. However, most banks in Thailand have high operating costs due to overstaffing and overexpansion (too many branches). Although Standard Chartered does not plan to cut down the number of Nakornthon's 66 branches, the bank will have to rationalize the branch network at some point in time. There is also the issue of NPLs.

Standard Chartered is making many recommendations to the Bank of Thailand regarding the conditions of any deal:

- The old shareholders should take responsibility for their part of the debt. If there is a write-down of capital after the deal, the burden should be for the old shareholders (or potentially the central bank), not the new.
- The bank wants a clear majority shareholding with the amount of capital they inject. Standard Chartered does not want to be in a situation in which they are constantly putting more and more money into the deal.

However, the Bank of Thailand is in new territory given the current banking situation in Thailand. Due to the high level of risks involved, the central bank will not provide such guarantees and Standard Chartered fears "capped guarantees."

Standard Chartered wants a clear majority as the bank plans to bring in-house experts into Thailand to bring down the NPLs to below 10%, for example. If a deal does occur, the Standard Chartered name would definitely be present. The market focus would be on the corporate side, more of the middle market, and significantly more on consumer banking.

Standard Chartered wants a branch network and some type of guarantee from the Bank of Thailand regarding NPLs. The rest of the issues can be dealt with. Standard Chartered has the breadth and depth to bring in its own people and customers, create its own core of depositors and banking products and implement its customer policies and procedures.

Conclusion

Foreign banks are interested in investing in Thailand for the right price, but the banks may need to be enticed by a “sweet deal” from the central government. The structural changes in the political and legal systems are slowly taking place to facilitate Thai integration. Although the current situation is uncertain, the Bank of Thailand is providing recapitalization schemes. Since Nakornthon Bank faces impending deadlines to reach capital adequacy ratios, Hyung Lo’s presentation to the board needs to focus on the issues (value of Nakornthon Bank, management control, intangibles such as branch network and a Thai banking license) in order for Nakornthon Bank to survive.

Exhibit 1

Hyung Lo spoke with a research analyst on Wall Street who covers the Asian banking sector to get a market opinion of his bank's situation.

Hyung Lo: What is your overall outlook for Nakornthon?

Analyst: Nakornthon needs to recapitalize in order to stay in business. As I see it, there are two options other than dissolving the business. Nakornthon can either sell a piece of the company to a foreign institution or enter the Thai government's Tier 1 capitalization plan. The Tier 2 capitalization plan should not be considered an option as it is an accounting gimmick which does not really help the company out at all. Tier 2 also introduces a negative spread situation that causes a cash outflow.

If Nakornthon sells out to a foreign institution, it would enjoy additional liquidity to help it through the recovery period, it would allow existing shareholders to maintain a small position in the company, and it would possibly see an increase in business from increased depositor security, which comes with an association with an international bank. The only issue which could be a stumbling block is the fact that no international bank would want to accept the liabilities of this bank for such low quality assets as backing. Usually there is value in the loan portfolio's collateral. In this case, however, so many loans are based on a severely depressed real estate market, the collateral is essentially worthless.

Nakornthon's Thai banking license may have some value to a foreign bank as well as its branch network. The Thai government has not allowed foreign banks to build a presence on the ground. Since Nakornthon is one of the smallest banks in Thailand, it could be seen as the cheapest way to enter the market.

Hyung Lo: What would have to happen for a foreign institution to be interested in a Thai bank?

Analyst: For a deal to be negotiated, some sort of deal would have to be struck to protect the foreign institution from the potentially huge downside. Take for example the deal that HSBC negotiated with the Korean government when it purchased Seoul Bank. The Korean government took a large percentage of the non-performing loans from the Seoul Bank's portfolio before HSBC took control.

Bank of Asia and Thai Danu sold large portions to foreign investors. Both of those deals were set up in early 1998. Unfortunately for ABN-Amro and the Development Bank of Singapore, the complete picture of the problems in Thailand was not yet clear. Since the close of those deals, the optimistic recovery projections which gave value to Bank of Asia and Thai Danu have been negatively revised. The foreign banks have had to inject much more capital than initially anticipated in order to keep the banks liquid. The deals may not have been done if more and better information was available.

That's something that the IMF money is attempting to fix. They are attempting to bring the country's reporting practices in line with those of the rest of the world. I must though, the IMF has a tough road ahead. Getting a straight answer in Thailand can sometimes be as difficult as herding cats.

Hyung Lo: And what about the Tier 1 recapitalization plan?

Analyst: If Nakornthon enters the government's Tier 1 capitalization program, all existing shares would be essentially worthless. The Wang Lee family would lose all control and ownership of the bank. Nakornthon would be joining the ranks of other Thai banks, such as Siam City Bank and Bangkok Metropolitan Bank, who have already begun the Tier 1 capitalization process. It is not yet clear that the program will work. All it appears to do is put the government in the bank's drivers seat and write-off the value of existing shares. The banks essentially do not receive any real money.

The government will most likely focus its effort to make the larger banks (see exhibit 7) healthy before the government focuses on the smaller players, like Nakornthon. If Nakornthon were to shrivel up and blow away, it would have no substantial impact on the Thai economy.

Hyung Lo: Reports out of Thailand suggest that the economy is on the road to recovery. What are your thoughts?

Analyst: After all my years of covering the Asian markets, I have learned to take everything with a grain of salt. Government and business announcements are often sketchy if they are true at all.

1998 was a terrible year for the banks in Thailand. I expect that a number of banks will have negative interest income. I expect the number of NPL's to continue to increase in 1999. This will continue to slash into earning. I also expect the Thai government to pass new bankruptcy and foreclosure legislation that will better protect the rights of creditors. This, unfortunately, will not likely effect the markets in the near term because implementation will be slow. At the end of the day, Thailand's banks are still in bad shape. They will continue to lose money until a) a large portion of the NPL's are written off, b) they can recapitalize or restructure some of their debt, and c) their debtors recover enough to pay their interest.

Exhibit 2

1997 Asian Contagion Chronology	
May 15, 1997	Thailand announces capital controls, which split the on and offshore markets.
June 27, 1997	BOT suspends operations of 16 finance companies.
July 2, 1997	BOT announces the float of the baht. The baht devalues by 15% onshore markets and 20% offshore markets.
July 11, 1997	Central Bank of the Philippines announces a wider float of the peso and Bank Indonesia widens the rupiah trading band to 12%.
July 14, 1997	Bank Negara Malaysia abandons the defense of the ringgit
August 5, 1997	BOT suspends 42 more finance companies.
August 14, 1997	Bank Indonesia abandons the rupiah trading band.
August 27, 1997	Malaysia imposes stock market trading restrictions, including a ban on short selling.
October 23, 1997	Hong Kong stock market loses 23% over the previous four days. S&P downgrades Korea and Thailand's sovereign ratings.
October 27, 1997	US stock market drops 554 points (DJIA). Brazil, Argentina and Mexico see their biggest single day losses. World equity markets lose ground.
November 1, 1997	Indonesia closes 16 private banks.
November 10, 1997	In Thailand, opposition leader Chuan Leekpai becomes Prime Minister.
November 17, 1997	Korea abandons defense of the won.
December 8, 1997	BOT closes 56 of the suspended finance companies
December 23, 1997	Rating agencies downgrade Korea's sovereign rating.

Note: The actual situation in Thailand was far worse because forward contracts are not included in the accounting for international reserves.

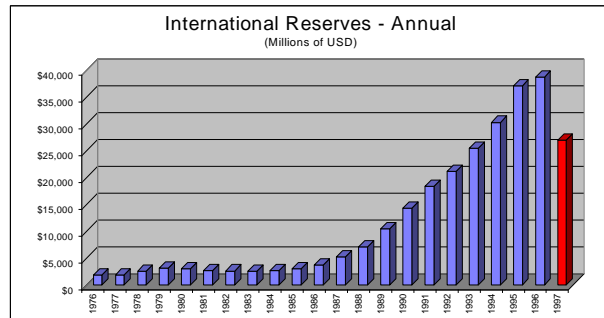
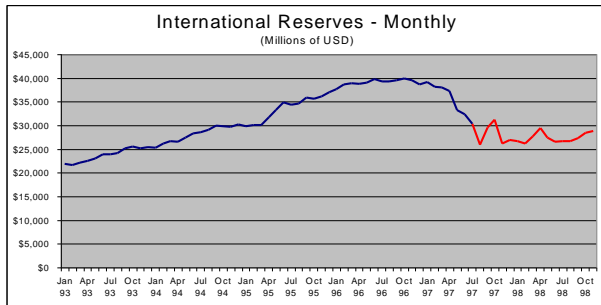
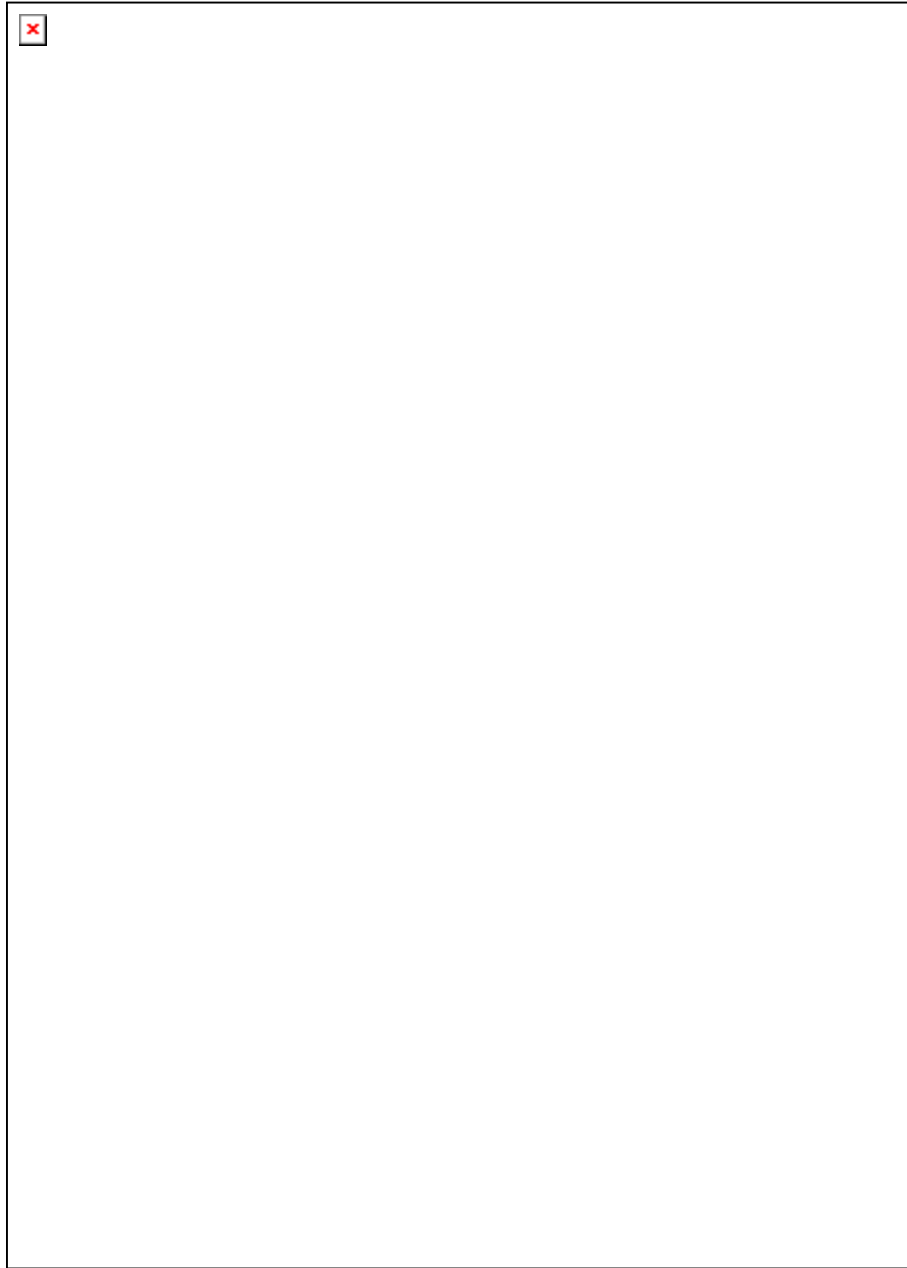


Exhibit 3

Thailand: Top Ten Exports
















 Garments	 Cars and Parts	 Frozen Shrimp	 Jewelry	 Canned Seafood
 Radios, TV's	 Rubber	 Computers	 Plastic Products	 Footwear
 Chips	 Rice	 Tapioca		

Exhibit 4**THAILAND KEY ECONOMIC INDICATORS**

	1997e	1998 f	1999 f
GDP at Current Prices (Billion Baht)	4,775	4,779	4,797
Real GDP Growth (%)	-0.40%	-8.50%	-0.40%
Consumption (%)	-1.50%	-8.30%	0.10%
- Private Sector	-0.90%	-8.60%	-0.80%
- Public Sector	-5.60%	-6.40%	6.30%
Investment (%)	-14.50%	-29.20%	-7.20%
- Private Sector	-21.80%	-26.00%	-4.00%
- Public Sector	8.40%	-36.40%	-15.80%
Inflation (%)			
- Consumer Price Index	5.60%	8.10%	0.80%
- Wholesale Price Index	4.00%	13.80%	-1.50%
Baht : US Dollar (Average)	31.4	41.4	37.0
International Trade (Billion Baht)			
Exports	1,789.7	2,178.1	1,966.8
% Change	-29.8%	-21.7%	-9.7%
USD Millions	56,721	52,818	53,293
% Change	-3.8%	-6.9%	-0.9%
Imports	1,874.5	1,696.5	1,506.5
% Change	-4.3%	-9.5%	-11.2%
USD Millions	61,348.0	40,809.0	40,482.0
% Change	-13.4%	-33.5%	-0.8%
Trade Balance	-84.9	481.6	460.3
As % of GDP	-1.8%	-10.1%	-9.6%
Current Account Balance	-40.3	535.3	505.6
As % of GDP	-0.8%	-11.2%	-10.5%
Balance of Payments	-299.2	50.6	-
Official Reserves (Billion US\$)	27.0	29.5	-

Source: Bangkok Bank Data Department

Exhibit 5

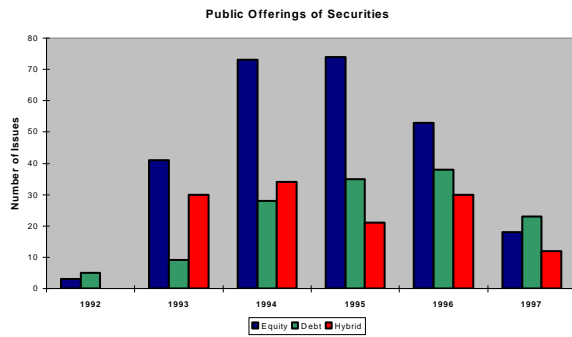
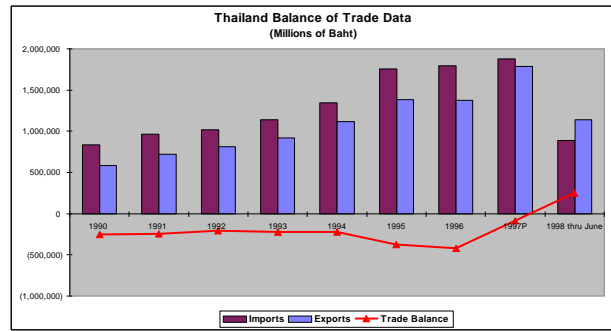
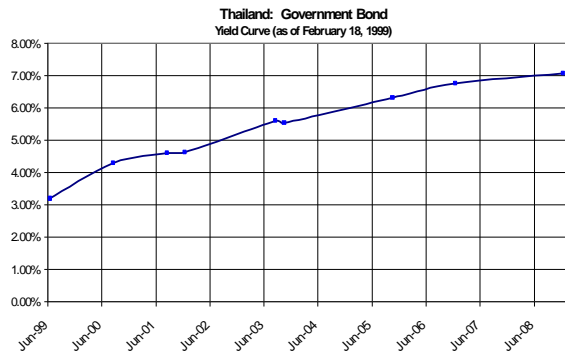
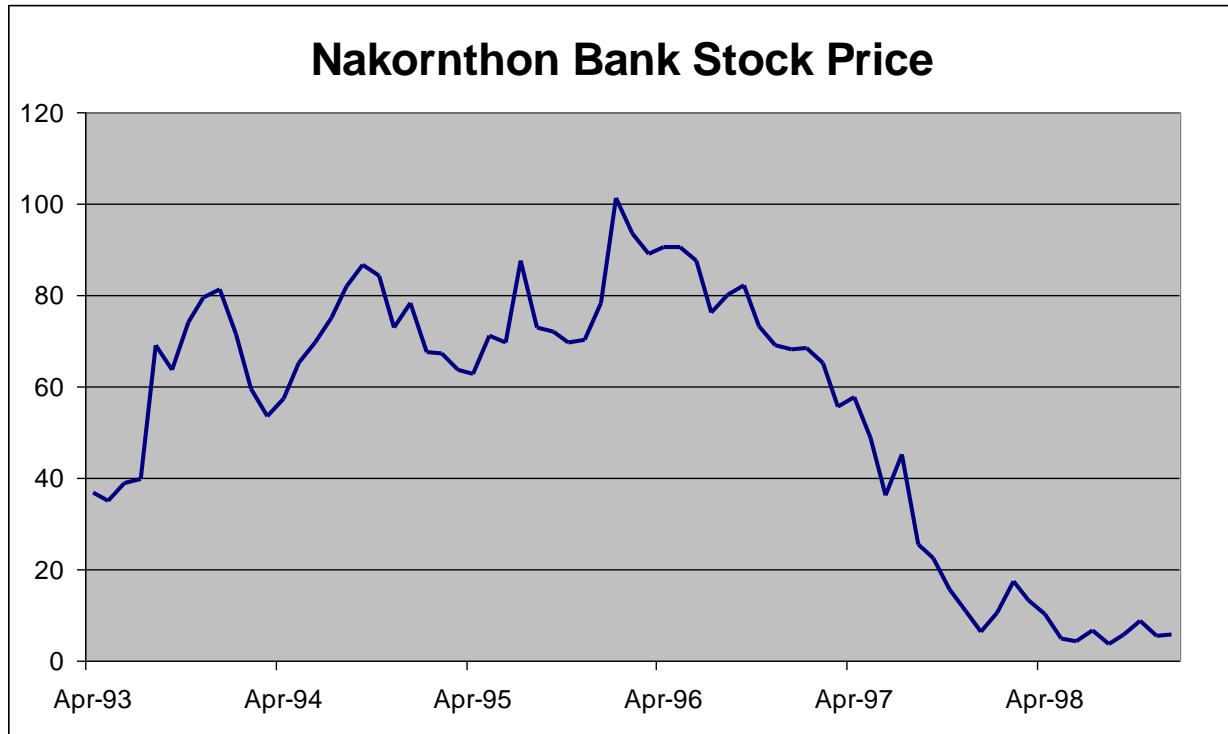


Exhibit 6



Nakornthon Stock Price

	1992	1993	1994	1995	1996	1997	1998
January	29.76	50.18	71.48	67.59	101.14	68.50	10.50
February	28.01	47.65	59.32	67.10	93.36	65.00	17.25
March	27.62	40.07	53.49	63.70	88.99	55.50	13.00
April	27.04	36.57	57.38	62.73	90.44	57.50	10.25
May	25.67	35.01	65.16	70.99	90.44	48.75	4.70
June	25.29	38.71	69.53	69.53	87.53	36.00	4.30
July	24.90	39.63	74.88	87.53	76.00	45.00	6.70
August	28.01	69.05	81.69	72.94	80.00	25.50	3.70
September	35.01	63.70	86.55	71.97	82.00	22.50	5.70
October	41.62	73.91	84.12	69.53	73.00	15.50	8.60
November	41.82	79.26	72.94	70.02	69.00	10.75	5.50
December	43.76	81.21	78.29	78.29	68.00	6.30	5.70

Exhibit 7

	MARKET VALUE BIL BAHT	THAI MARKET BETA*
Bangkok Bank	44.8	1.33
Krung Thai Bank	22.6	1.43
Nakornthon	0.63	1.01
Siam Commercial Bank	6.07	1.40
Thai Danu Bank	4.62	1.42
Thai Farmers Bank	40.0	1.40
Thai Military Bank	4.13	1.29

* Betas based on 103 equities on Thai Stock Exchange as of 2/19/99

Exhibit 8

LOAN PORTFOLIO STATUS	TOTAL LOANS	RISK WEIGHT FACTOR	RISK ADJUSTED ASSET VALUE
Pass	30,864	1%	30,555
Special Mention	4,984	2%	4,884
Substandard	5,941	20%	4,753
Doubtful	10,997	50%	5,499
Doubtful of Loss	9,375	100%	0
Loss	3	100%	0
Total	62,164		45,691