Financial Services Commission
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Financial Supervisory Service
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Press Release

October 29, 2008

Regulations Improvement to Provide Liquidity to Financial Market

Ⅰ Improvement in Won Liquidity Ratio Requirement

1. Background

- The need for improvement in Won liquidity ratio requirement (100% or above), which was introduced in January 1999, has been continuously raised.

  - Current requirement is too stringent compared with that of other advanced countries and is not in line with the global standard.
  - Excessive issuance of bank debenture to comply with the requirement now seems to cause negative impact on the market, raising interest rates including bank debenture rate and CD rate even though banks have few liquidity problems.
  - The Bank of Korea also raises the need for improvement in the requirement.

2. Improvement in Liquidity Ratio Requirement

- The FSC/FSS plan to make regulatory changes, by lowering the maturity requirement of liquidity ratio from the current “ratio of assets with maturity of 3 months or less against liabilities with maturity of 3 months or less” to “ratio of assets with maturity of 1 month or less against liabilities with maturity of 1 month or less.”

- The proposed changes are expected to let the liquidity ratio of large commercial banks rise by 13.5% (as of the end of August 2008, 107.2% → 120.7%).

- The changes will take effect for the liquidity ratio as of the end of October 2008.

3. Expected Results and Future Plans

- The FSC/FSS expect that the regulatory changes will lead to stabilization of bank debenture rate and CD rate by easing the demand for bank debenture. In addition, the FSC/FSS expect that concerns over banks competing for higher interest rate to attract deposits will be mitigated.

- The FSC/FSS will reinforce monitoring of liquidity status of banks and overall financial market and take appropriate measures if necessary. To prevent deterioration of profitability and asset quality, banks will be required to establish plans for improvement in funding and placement structure. And the FSC/FSS will oversee the implementation and management of the plans.

Ⅱ System Establishment for Liquidity Support for Securities Companies and Asset Management Companies

1. Liquidity Support Measures by the Bank of Korea (Oct. 24)

- The Bank of Korea had irregular RP transactions with the Korea Securities Finance Corp.
  - Purchase Amount: 1.9 trillion won (5.00% per annum, which was revised down to 4.25% on Oct. 27.)
  - Maturity: 28 days (the longest period of maturity in record)

- The Korea Securities Finance Corp. plans to provide liquidity to securities companies and asset management companies upon request by utilizing the funds secured.
  - Expected interest rate: approximately 4.48%
  - RP transaction between the Korea Securities Finance Corp. and securities companies as of Oct. 28: 1.43 trillion won

- The Bank of Korea will take additional liquidity support measures if necessary.

2. Liquidity Support Mechanism

- The Korea Securities Finance Corp. seeks funding through RP transaction with the Bank of Korea, mainly through transaction with government bond, monetary stabilization bond and bank debenture, etc.

- For the next step, the Korea Securities Finance Corp. provides liquidity via RP transaction with underlying assets of government bonds and monetary stabilization bond and bank debenture, etc. which fund management companies or securities companies hold.

- In the meantime, the Korea Securities Finance Corp. can conduct RP transaction even when underlying assets are not government bond, monetary stabilization bond, or bank debenture, etc. (government-run corp. bond, corporate bond, and CP)
  → Replace them with government bond or monetary stabilization bond or bank debenture, etc. through transaction with national pension funds

3. Expected Results

- While the Bank of Korea takes almost no risk since the proposed liquidity support is guaranteed by government bond, monetary stabilization bond, and bank debenture, etc., the negative impact on the market will be minimized as individual fund management companies or securities companies receive liquidity via the Korea Securities Finance Corp.

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