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Press Release

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REGULATION ON BANKS' LOAN-TO-DEPOSIT RATIOS

In the 2010 Financial Policy Agenda announced in December 2009, the FSC unveiled its plans to adopt banks' loan-to-deposit (LTD) ratio as one of its bank liquidity guidance ratios, which aims to encourage sound management of banks and alleviating factors driving the asset competition among banks. As a step to follow up with the announcement, the Regulation on Supervision of Banking Business is slated to be amended to employ banks' liquidity or LTD ratio to measure bank management soundness after a notice and adjustment period between March 26 and April 15.

Background

For the past few years, expansion in mortgages and SME loans triggered off an asset competition among banks. As a result, signs of instability in banks' liquidity became apparent during the 2008 financial crisis as bank debentures and other market-based capital served as funding sources while resources that are required to support stepped up lending were not backstopped with deposits.

Although domestic banks' LTD ratio was around 100% at the end of 2004, the ratio had risen sharply between 2005 and 2007 reaching 127.1% at the end of 2007. However, following the persistent guidance from the regulator to reduce the ratio since the second half of 2008, banks' LTD ratio had fallen to 110.4% as of end-January 2010.

Loan-to-Deposit Ratio of Commercial Banks

(in %)

	2003	*2004*	*2005*	*2006*	*2007*	*2008*	*06/09*	*09/09*	*12/09*	*01/10*
Excluding CDs	**95.4**	**101.7**	**103.7**	**111.9**	**127.1**	**121.9**	**115.3**	**113.6**	**112.1**	**110.4**
Including CDs	89.0	94.0	93.3	98.4	106.3	103.0	99.8	98.1	97.6	97.3

Proposed Changes

The planned changes in the regulation will apply to commercial banks in principle having won-denominated loans in excess of KRW2.0 trillion. This will include foreign bank branches, of which only HSBC will apply with KRW3.3 trillion in won-denominated loans as of December 2009, and the National Agricultural Cooperative Federation (NACF), the only one among the special purpose banks given the policy-driven nature of their loans.

The ratio is calculated through the following method, excluding CDs:

$$\text{Loan-to-deposit ratio} = \frac{\text{won-denominated loans}}{\text{won-denominated deposits}^{*}}$$

* Demand deposits, savings deposits, time deposits (figures from bank balance sheets)

The target for banks' LTD ratio is to be set at 100% with a grace period until the end of 2013 whereupon banks will be required to maintain a ratio within 100% from January 1, 2014. To oversee the progressive lowering of the ratio during the grace period, the FSS will review the ratio retrenchment plans of each respective bank on an annual basis.

The proposed LTD ratio regime is expected to operate with a certain amount of flexibility that will take into account the parallel links with BCBS regulations on liquidity, if and when it is introduced.

Future Plans

The FSC's final decision on the proposed regulatory amendment to the Regulation on Supervision of Banking Business is expected to follow a 20-day notice and adjustment period.

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