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Press Release

December 16, 2013

PLAN TO STIMULATE M&AS AMONG SECURITIES COMPANIES

The FSC announced its ‘Plan to Stimulate M&As among Securities Companies’ on December 16 in a bid to revitalize capital markets as part of the so-called ‘10-10 Value-up Plan’ previously announced on November 27, 2013.

BACKGROUND

Korea’s securities industry has 62 securities firms, small in size compared to those of the advanced countries, and their business scope is mostly limited to brokerage businesses in domestic market.¹ Securities firms have been competitively lowering their brokerage fees to compete over the limited size of the domestic market, consequently hurting their profitability.² Against this backdrop, the FSC came up with measures to encourage the securities industry’s consolidation through market-led M&As.

MAJOR CONTENTS

1. Incentives for securities firms pursuing M&A

The FSC will offer securities firms incentives for M&As by easing requirements eligible for investment banking (IB) licenses or allowing enter new businesses such as pension fund trusts or PEFs.

- ① The Minimum equity capital requirements eligible for investment banking licenses will be eased from the current KRW 3 trillion to KRW 2.5 trillion for securities firms making M&As that would increase their equity capital by KRW 500 billion.
- ② Securities firms making M&As that would raise their equity capital by KRW 100 to 300 billion will be allowed to enter new businesses such as personal pension fund trusts.
- ③ Securities firms making M&As that would increase their equity capital by KRW 50 to 150 billion will be preferentially granted approval for operating private equity funds.

2. Strengthened supervision for poorly-performing securities firms

Currently, securities firms are either recommended or required to take necessary measures for management improvement in case their net capital ratios (NCR) fall below certain levels.³ However, the NCR is to evaluate securities firms’ capability in case of liquidity risk. It is not

¹ Large securities firms earn 52% of their revenue from their brokerage services; small and medium-sized firms gained 45% of their revenue from brokerage business.

² ROE of securities firms(%): 7.7(FY’10) → 5.6(FY’11) → 3.0(FY’12) → 0.4(expected, FY’13)

³ Management Improvement Recommendation in case the NCR falls below 150%; Management Improvement Requirement in case the NCR falls below 120%.

enough to encourage securities firms to improve their management in a more timely and proactive manner.

The FSC will revise conditions for prompt corrective actions to include a broader range of criteria such as leverage ratios.

Prompt Corrective Actions	Criteria for PCAs	Corrective measures
Management Improvement Recommendation	<p>Current</p> <ul style="list-style-type: none"> - NCR <150%; or - Composite rating 3 or higher; capital adequacy rating 4 or lower <p>To be added</p> <ul style="list-style-type: none"> - Net losses for two consecutive years & leverage ratio ≥ 900%; or - leverage ratio ≥ 1,100% 	<ul style="list-style-type: none"> - Improvement of manpower and organization management - Curtailment of expenditure - Efficient management of branches - Disposal of non-performing assets - Restriction on any practices causing a decrease in net capital - Increase or reduction of capital stock - Restriction on advancement into a new business - Establishment of special allowance for bad debts
Management Improvement Requirement	<p>Current</p> <ul style="list-style-type: none"> - NCR <120%; or - Composite rating 4 or lower <p>To be added</p> <ul style="list-style-type: none"> - Net losses for two consecutive years & leverage ratio ≥ 1,100%; or - leverage ratio ≥ 1,300% 	<ul style="list-style-type: none"> - Restriction on the holding of high-risk assets and disposal of assets - Closure and consolidation of business offices, or restriction on opening new offices - Curtailment of organization - Disposal of subsidiaries - Demand for the replacement of corporate executives - Suspension of business in part - Merger or acquisitions

3. Improve Net Capital Ratio(NCR) rules

The FSC will improve net capital ratio(NCR) rules, one of barriers to M&As. Currently, NCRs of securities firms are calculated on an individual basis; therefore, if a brokerage firm acquires other brokerage firm as a subsidiary, the acquirer's NCR sharply drop with acquisition investment deducted from its equity capital.

In order to address such a problem, the FSC plans to introduce consolidated accounting standards in calculating NCRs so that brokerage firms' investments for acquisition could be differentially reflected into a total risk depending on the acquired firm's risks.

IMPLEMENTATION SCHEDULE

Measures	Implementation timing (expected)
Incentives for M&As - easing requirements eligible for IB licenses - allowing personal pension fund trusts - allowing private equity fund management	2 nd half of 2014 (A revision bill on the FSCMA will be submitted for parliamentary approval in the first quarter of 2014)
Revised criteria for prompt corrective actions	2 nd half of 2014
Improved NCR rules	2 nd half of 2014

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