Financial Services Commission

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Press Release

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KOREA'S HOUSEHOLD DEBT AND POLICY RESPONSE

1. CURRENT STATUS OF KOREA'S HOUSEHOLD DEBT

As of end-September 2014, outstanding household credit totaled KRW 1,060.3 trillion with household loans totaling KRW 1,002.9 trillion and merchandise credit[1] KRW 57.4 trillion.[2]

The ratio of household debt to income in Korea was 160.7 % (as of 2013), higher than 115.1% in the US(as of 2012) and 135.7% of the OECD average(as of 2012). However, Korea's household financial assets to liabilities ratio maintained stable levels of 46%, while the ratios in Spain and other major OECD countries have been rising.

< Household financial assets to liabilities ratio in major economies (%) >

	2002	2004	2006	2008	2010	2012	2013
Korea	49.2	46.8	46.7	51.0	46.5	46.6	**46.2**
Spain	38.9	42.5	45.6	56.7	54.6	50.2	-
OECD	33.6	35.6	36.3	43.5	40.6	40.3	-

The quality of household mortgage loans has been improved with proportions of fixed-rate and fully-amortized loans steadily increasing. As of end-2014, the percentage of fixed-rate and amortized loans out of banks' household mortgage loans stood at 23.6% and 26.5% respectively, exceeding 20% initially targeted by 2014.

<Proportions of fixed-rate and fully amortizing loans out of banks' mortgage loans (%, %p)>

	end-2010(A)	end-2011	end-2012	end-2013	end-2014(B)	(B-A)	Targets by end-2017
Fixed-rate	0.5	3.1	14.2	15.9	**23.6**	**+23.1**	40
Fully-amortizing	6.4	7.7	13.9	18.7	**26.5**	**+20.1**	40

2. POLICY MEASURES TO MANAGE HOUSEHOLD DEBT GROWTH

It is a natural phenomenon that household debt increases as economy grows. The bottom line is that it is important to boost the economy while maintaining household debt soundness.

Under such awareness, the government has been managing household debt with policy measures focused on two aspects. First, secure soundness of the financial system by maintaining the pace of household debt growth at manageable levels, improving the quality of household loans and bolstering financial institutions loss-absorbing capacity. Second, ensure financial soundness of households with measures to boost household incomes and provide tailored financial services to financially-vulnerable households.

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[1] Sales on credit by credit card companies and other financial companies
[2] Data of「Household Credit in Q4 2014」available on the BOK website

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The government set basic policy directions to manage household debt with 「Comprehensive Measures on Household Debt」 in June 2011.

The policy measures were focused on maintaining the pace of household loan growth at economic growth rates; improving the quality of household loans with a larger share of fixed-rate and amortizing loans; and providing tailored support for low-income households.

Since the measures were taken in 2011, household debt growth rate has been stabilized.[3] The quality of household loans has been also improved significantly.[4]

The stress test by the IMF(January 2014) evaluated that it is highly unlikely for Korea's household debt to default in the event of falls in house prices or rise in interest rates.

With the 「Three-year Plan for Economic Innovation」 in February 2014, the government set out a package of measures to boost household income in addition to measures to maintain soundness of household financial debt.

The government set the ratio of household debt to disposable income as a key indicator in managing household debt and decided to reduce the ratio by 5%p by end-2017 compared to 160.7% as of end-2013.

As part of measures to boost household income, the government eased restrictions on the loan-to-value(LTV) and debt-to-income(DTI) ratios for household mortgage loans in August 2014 to revitalize stagnated housing market.

3. Household debt status after easing LTV & DTI regulations(Aug, 2014)

Household loans have grown faster after August 2014 than previous year due to increased housing market transactions and interest rate cuts.

Despite relatively rapid growth of household loans, Korea's household debt is at manageable levels.

- About 70% of the total household debt is held by high income households who can afford debt repayment.[5]
- Korean households have financial assets twice as large as financial liabilities. Korean households' total assets including real estate are five times bigger than their total liabilities.
- Debt delinquency rates and LTV ratios remained low and stable. Financial institutions are healthy with sufficient capital to absorb loss.[6]
- The financial authorities are conducting various stress tests according to international standards while closely monitoring household debt trend.

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[3] Growth rate of household credit(year-on-year): 9.3% (annual growth rate from 2005 to 2010), 8.7%(2011), 5.2%(2012), 6.0%(2013), 6.7%(September 2014)

[4] Percentage of fixed-rate loans increased from 0.5% in 2010 to 23.6% in 2014, while that of fully-amortizing loans rose from 6.4% in 2010 to 26.5% in 26.5%.

[5] Proportion from total household debt volume by household income quintile(%, National Statistical office): (1st quintile)4.3,(2nd quintile)11.4, (3rd quintile)14.6, **(4th quintile)22.5**, **(5th quintile)47.2**

[6] The banking sector has an average of 0.41% in household mortgage loan delinquency rate, 52.4% in loan-to-value ratio and 13.98 % in BIS ratio.

There has been significant improvement in the structure of household debt. The proportion of fixed-rate and amortized loans is steadily increasing.[7] Borrowers are refinancing their high-interest loans from non-banking sector with lower-interest loans from banks[8].

"These developments are credit positive for Korean banks because they show that the government's push to de-risk banks' mortgage portfolio is working" – Moody's (Jan, 2015)

Increase in refinancing after the central bank lowered benchmark rate significantly reduced household's debt servicing burdens[9].

Considerable proportion of new loans are being consumed in buying houses which contributes in normalizing housing market and encouraging more productive use of housing finance. The IMF evaluated that Korea's household debt "does not pose a near-term threat to the macro-economy" and the structure is getting stronger in its annual meeting held in February, 2015.

"Overall household debt has been rising,…this has been marched by a corresponding increase in household financial assets rather than reflecting an increase in borrowing to finance consumption. Therefore, we do not see debt levels as a near term threat to the macroeconomy…The structure of household debt could also be strengthened."- IMF (Feb, 2015)

4. Future Plan

The government will maintain the current policy stance for household debt management while devising additional measures to further improve the quality of household loans and prevent commercial property loans from surging in the non-banking sector (the so-called "balloon effect").

The government will launch a refinancing program worth KRW 20trillion in March 2015 to help borrowers refinance their floating-rate and non-amortizing loans to fixed-rate and amortized ones.

To prevent the balloon effect in the non-banking sector, the government will set out a guideline for application of loan-to-value ratio in March 2015.

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7 Proportion of loans(2010→2014, %): (fixed-rate)0.5→23.6, (amortized)6.4→26.5

8 Increase in housing mortgage loan volume from non-banking sector(KRW trillion): (Aug-Dec, 2013)2.7→(Aug-Dec,2014)0.8

9 Monthly interest payment per household in the second half of 2014 decreased KRW 2,802 (KRW 33,624 annually). Total household interest payment reduction is estimated at KRW 478.5billion annually.