

POLICY DIRECTION FOR CAPITAL MARKET REFORM:

MEASURES TO VITALIZE THE KONEX, OTC TRADING OF UNLISTED STOCKS AND THE DERIVATIVE MARKET

The FSC outlined its policy direction and key tasks to push forward capital market reform in order to enhance the vitality of capital markets and strengthen its support for real economic activities.

Current situation	Policy direction (5)	Detailed tasks (15)
Stock exchange market is stagnant compared to advanced overseas markets	Reorganize the bourse system	① vitalize the KONEX market ② foster competition among exchanges ③ enhance the vitality of capital markets
Investment in start-ups and venture companies still fall short	Boost venture capital investment	④ remove barriers for venture capital investment ⑤ diversify venture capital investors' options to recoup their investment ⑥ stimulate private bond markets
Needs for asset accumulation grow for aging population, while investment returns fall	Improve efficiency in financial asset management	⑦ revise PEF regulations ⑧ enhance management of pension assets ⑨ foster financial investment advisory businesses
Market infrastructure and investor protection lag behind international standards	Enhance efficiency and trust in transaction	⑩ introduce electronic securities system ⑪ improve public disclosure rules ⑫ establish a 'stewardship code'
Regulations and practice restrict market players' business activities	Strengthen competitiveness of financial investment businesses	⑬ strengthen the role of securities firms in raising capital ⑭ encourage securities firms to offer asset management services ⑮ strengthen competitiveness of asset management businesses

As part of the capital markets reform, the FSC announced today its detailed plan to **vitalize the KONEX, OTC trading of unlisted stocks and the derivative market**. Plans for the remaining tasks will be announced as scheduled.

< Announcement schedule for policy tasks >

announcement schedule	key issues & policy tasks
April 2015 (April 23)	<ul style="list-style-type: none"> - vitalize the KONEX market (task①) - boost the vitality of derivatives market (task③) - stimulate over-the-counter markets (task⑤)
May 2015	<ul style="list-style-type: none"> - electronic securities system (task⑩) - improve public disclosure system (task⑪)
June ~ Sept 2015	<ul style="list-style-type: none"> - foster competition among exchanges (task②) - remove barriers for venture capital investment (task④) - operate securities companies specialized in M&As of SMEs (task⑤) - foster private bond markets (task⑥) - revise PEF regulations (task⑦) - improve management of pension assets (task⑧) - stimulate financial investment advisory businesses (task⑨) - establish a stewardship code (task⑫) - revise securities trading system(task⑬)
2 nd half of 2015	<ul style="list-style-type: none"> - strengthen the role of securities firms in raising capital(task⑬) - encourage securities firms to provide asset management services(task⑭) - strengthen competitiveness of asset management businesses(task⑮)

I. VITALIZE THE KONEX MARKET

CURRENT SITUATION

The KONEX was launched in June 2013 as a third stock market to trade shares of start-ups and small & medium-sized companies. The KONEX market has expanded rapidly in size since its launch. The number of listed companies rose from 21 in July 2013 to 80 in March 2015. Market capitalization grew from KRW 0.46 trillion to KRW 1.94 trillion over the same period. It also provided a direct channel for small and medium-sized companies to raise capital as 27 companies raised a total of KRW 98.7 billion as of March 2015.

The KONEX currently allows only institutions or individuals with deposits of more than KRW300 million to invest. It has relatively eased listing regulations with the appointment of designated advisors to assist filings, reporting and public disclosure of the KONEX-listed companies.

MEASURES TO VITALIZE THE KONEX MARKET

More incentives need to be devised to encourage more start-ups to be listed on the KONEX, while attracting more venture capital investments.

1. Lower barriers while expanding incentives for investors

(Individual investors) The deposit regulation will be eased to KRW 100 million from the current KRW 300 million to lower hurdles to individual investors. The KONEX will also introduce a ‘small investment account’ to allow individual investors to invest up to KRW 30 million per year regardless of deposit levels.

(Institutional investors) High-yield funds holding more than 2% of their portfolio in KONEX stocks will be given priority in allocation of shares in listings of such companies on the KOSDAQ.

< The Role of capital markets for each stage of business life cycle >

	Start-up stage (0-3 yrs)	Growth stage (4-9 yrs)	Mature stage (10-15 yrs)
Investment risk	Very high investment risk - angel investors - venture capital	Relatively high investment risk - professional investors - high-risk takers	Moderate investment risk - general investors
Role & features of capital markets	Over-the-counter market (Feature) - no investor protection measures - one-on-one contract solely dependent on each investor's intention (Role) - Facilitate secondary investment into start-ups and divestment of initial investment for investors	KONEX market (Feature) - relatively eased investor protection measures - Listing based on evaluation about a company's growth potential, not quantitative factors such as financial conditions (Role) - enable divestment of initial investment for investors and directing financing for companies (Listing requirement) - sign an advisory service contract with a brokerage firm - receive TCB technology rating & attract investments by institutional investors	KOSDAQ market (Feature) - a trading platform for shares of financially stable companies - strong investor protection measures in place (Role) - raise a larger amount of funds through public offering (Listing requirement) - companies with equity capital of KRW 1.5 billion & net profit of KRW 1 billion or sales volume of KRW 5 billion - companies with promising technologies are exempt from listing requirements other than equity capital of KRW 1 billion

2. Ease listing requirements for companies

Quantitative standards for KONEX listing will be abolished. The number of designated advisors will be increased from the current 16 to 51. A special listing will be introduced for early-stage startups to allow them to be listed without designated advisors.

3. Support for KOSDAQ listing of KONEX-listed companies

Listing requirements will be eased for KONEX-listed firms seeking to list their shares on the KOSDAQ through merging with KOSDAQ-listed SPAC.

4. Strengthen investor protection

Individual investors should be well informed by brokerage firms about market characteristics of KONEX and relevant investment risks when opening a small investment account. The bourse and designated advisors will be required to offer investors sufficient information about listed companies. A special listing program will require stronger measures to protect investors.

IMPLEMENTATION SCHEDULE

Easing the deposit regulation will be implemented immediately after the revision to the KRX

regulation in May. Small investment accounts will be introduced as soon as brokerage firms complete development of relevant systems. A special listing for early-stage startups and KOSDAQ listing of KONEX-listed companies through a merger with SPAC are scheduled to be implemented in June with relevant revisions to the KRX regulations.

II. ESTABLISH K-OTC BB*

* K-OTC BB: Korea Over-The-Counter Bulletin Board

The Korea Financial Investment Association (KOFIA) established the Free Board market in March 2000 to trade unlisted stocks of small and medium-sized companies. As the over-the-counter market failed to boost trading of unlisted stocks, the FSC and KOFIA announced the plan to overhaul the Free Board market in January 2014. Under the plan, the Free Board was reorganized into two-tier markets: ① K-OTC (launched on August 25, 2014) as a primary market for trading unlisted stocks of blue-chip companies; and ② K-OTC BB (to be launched on April 27, 2015) as a secondary market for all non-listed stocks of SMEs or venture companies.

	Free Board	Primary (K-OTC)	Secondary (K-OTC BB)
Entry	<ul style="list-style-type: none"> - minimum screening: review of minimum criteria - review of basic financial conditions 	<ul style="list-style-type: none"> - tighter screening: review of financial conditions including sales amount - listing authorized by KOFIA 	<ul style="list-style-type: none"> - minimum screening: review of minimum criteria
Disclosure	<ul style="list-style-type: none"> - non-regular disclosure & disclosure upon inquiry - half-yearly disclosure (recommended) 	<ul style="list-style-type: none"> - half-yearly disclosure (mandatory) - non-regular disclosure, disclosure upon inquiry, detailed information 	<ul style="list-style-type: none"> - no disclosure requirements
Trading method	<ul style="list-style-type: none"> - trade settled when selling and buying prices match 	<ul style="list-style-type: none"> - trade settled when selling and buying prices match 	<ul style="list-style-type: none"> - KOFIA offers selling & buying prices only - actual trading is settled by brokerage companies

III. EXPAND THE DERIVATIVES MARKET

CURRENT SITUATION

The overall trading volume is falling with trading of KOSPI 200 Futures and Options decreasing, while underlying assets are diversified into individual equity, currency and interest rate products. Speculative trading diminished particularly by retail investors, enhancing market stability with investor protection measures¹ in place.

NEW PRODUCTS TO BOOST THE DERIVATIVES MARKET

(‘Mini KOSPI 200’ Futures & Options) Trading units for KOSPI 200 derivative products will be downsized in order to attract more retail investors and satisfy sophisticated investment demands. The trading units of Mini products will be cut to one-fifth compared to KOSPI 200

¹ Raised minimum deposit for retail investors, strengthened education requirement(mandatory) for new investors

Futures and Options.²

(KOSDAQ Individual Equity Futures) New futures products will be developed with individual stocks listed on KOSDAQ as underlying assets to offer investors risk hedging tools for KOSDAQ investments.

(Dividend Index Futures) New futures products will be developed and introduced with dividend index as underlying assets in response to growing demand for dividend investments.

(RMB Currency Futures) Chinese Renminbi(RMB) futures will be introduced to provide risk hedging tools so that RMB trading market could function in a stable manner.

LISTING SCHEDULE (TENTATIVE)

- Mini KOSPI 200 products & KOSDAQ Futures (July 2015)
- Dividend Index Futures (August 2015)
- RMB Futures (September 2015)

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² e.g. KOSPI 200 Futures (KRW 130 million per unit) → Mini KOSPI 200 Futures (KRW 26 million per unit)/
KOSPI 200 Options (KRW 30 million) → Mini Options (KRW 6,000,000)