Financial Services Commission

Press Release

July 22, 2015

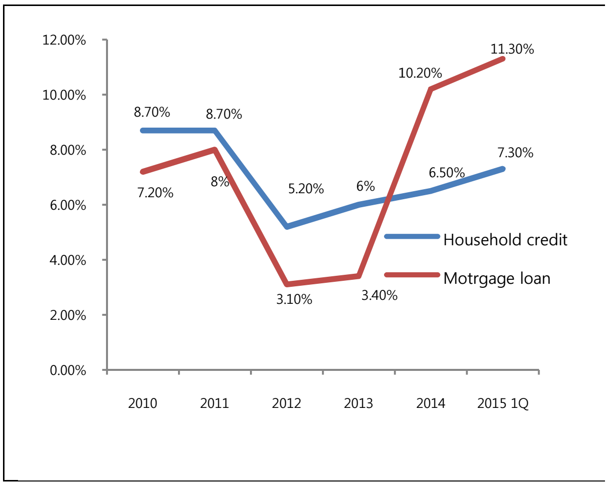
HOUSEHOLD DEBT MANAGEMENT MEASURES

The government announced today a package of measures to manage household debt. A consultative body was formed among relevant government agencies[1] in March this year to discuss and come up with comprehensive and preemptive measures to manage household debt in response to potential internal and external risks. The measures are focused on accelerating the improvement of household loan quality, strengthening the assessment of a borrower's repayment ability, tightening household debt management in the non-banking sector, and strengthening banks' ability to respond to internal or external shocks.

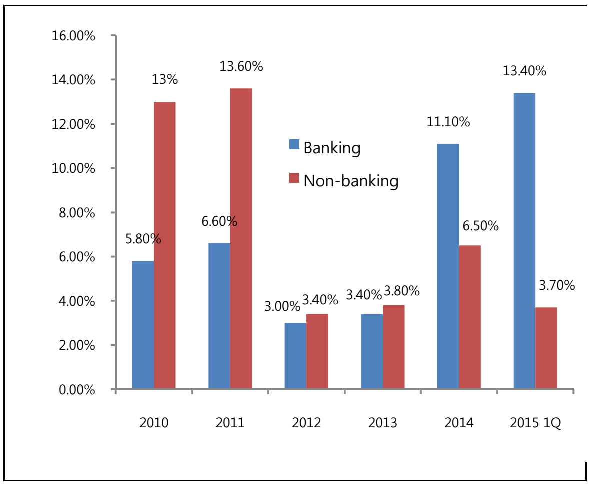
CURRENT STATUS OF KOREA'S HOUSEHOLD DEBT

The household debt has grown fast recently after years of stabilized growth around 6%.[2] Particularly, mortgage lending from banks has been rising fast since the second half of last year[3], which is attributed to multiple factors such as eased mortgage restrictions and growing demand for loans with interest rate cuts.

Household Debt Growth Rate / source: BoK



Mortgage Lending Growth Rate (Banking & Non-Banking Sectors) / source: BoK



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1 Ministry of Strategy & Finance, Financial Services Commission, Ministry of Land, Infrastructure & Transport, Financial Supervisory Service, Bank of Korea

2 Household credit growth (%, year-on-year)/source: BOK
9.3% (average from 2005 to 2010), 8.7% (2011), 5.2% (2012), 6.0% (2013), **6.5% (2014), 7.3%(1Q of 2015)**

3 Household lending growth (trillion won)/source: FSS
KRW 35.7 trillion (August 2013~June 2014) -> KRW 79.8 trillion (August 2014~June 2015)
Banks' mortgage lending (trillion won)/source: FSS
KRW 16.6 trillion (August 2013~June 2014) -> KRW 59.5 trillion (August 2014~June 2015)

Mortgage lending by banks which amounted to KRW 375 trillion at the end of March 2015 maintains its financial soundness with a delinquency rate of 0.39% at the end of March 2015. Banks have sufficient capability to absorb potential losses with a BIS capital adequacy ratio of 13.9% at the end of March 2015. Since the government-led KRW 32 trillion program was launched in March this year to help mortgage borrowers switch to fixed-rate and amortized loans, the shares of such mortgages continue to increase and hit 30%, initially targeted by the end of 2016, in the first half of this year.[4] In addition, 70% of household debt is held by households in the highest income brackets – fourth and fifth quintiles. Household financial assets are more than twice household financial liabilities.[5] Given the soundness of household debt, the possibility is limited that household debt risks would cause a systemic risk.

As household debt continues to grow faster than income with a slow economic recovery, however, the government needs to take preemptive and comprehensive measures in response to internal and external risks such as a U.S. interest rate increase and subsequent impact.

HOUSEHOLD DEBT MANAGEMENT MEASURES

1. Accelerate the switch of mortgage debt structure to fixed-rate & amortized loans

In order to reduce households' repayment burden in the event of interest rate hikes, we need to accelerate the switch of mortgage debt structure to fixed-rate and amortized mortgages. To this end, the government will further raise annual targets for fixed-rate and amortized mortgages and strengthen incentives for banks to handle more fixed-rate and amortized loans.

SHARES OF FIXED-RATE, AMORTIZED LOANS OUT OF TOTAL MORTGAGES BY BANKS

	end-2014	end-June 2015 (estimated)	annual targets & adjustment		
			end-2015	end-2016	end-2017
amortized	26.5%	33%	25% ► **35%**	30% ► **40%**	40% ► **45%**
fixed-rate	23.6%	33%	25% ► **35%**	30% ► **37.5%**	**40%**

For long-term, fixed-rate and amortized mortgages, banks will be applied lower contribution rates, as low as 0.05%, compared to the maximum 0.30% applied to short-term, floating-rate and "bullet" loans, in their contributions to the Housing Finance Credit Guarantee Fund managed by the Korea Housing Finance Corporation. Banks will be granted extra cuts in contribution rates, up to 0.06%p per year, depending on their achievements in targeted goals of fixed-rate, amortized mortgages. Differential contribution rates will be applied from December 2015.

Guidelines will be established for banks to be implemented from January 2016 to provide detailed explanation about types and methods of extending amortized mortgages. A mobile application will be developed to be available for the public in October this year to boost consumer awareness about benefits of amortized mortgages. The application will provide

[4] Shares of fixed-rate, amortized mortgages (from banks)

	end-2010	end-2011	end-2012	end-2013	end-2014	end-March 2015	end-June 2016(estimated)
amortized	6.4%	7.7%	13.9%	18.7%	26.5%	**29.8%**	**33%**
fixed-rate	0.5%	3.1%	14.2%	15.9%	23.6%	**27.6%**	**33%**

[5] Ratios of household financial assets to financial liabilities/source: BOK
2.13 (2011), 2.17 (2012), 2.19 (2013), 2.23 (2014), 2.27 (1Q of 2015)

services that compare interest rates across banks and products, calculate saved interest rate payments, and propose appropriate loan products for users.

2. Strengthen the assessment of a borrower's repayment ability

Bank's screening of loan applications will be more focused on assessment of a borrower's debt repayment ability rather than the value of the collateral. Starting from January 2016, banks will be encouraged to use income verifications[6] that show the borrower's actual income in order to more accurately assess the borrower's ability to repay. In the case of referring to a borrower's reported income data[7], less credible than income verifications, banks will be required to apply tighter standards in the screening process.

For new mortgage loans from January 2016, a certain amount of the mortgages that exceeds a borrower's income level or home value should be given out in amortized mortgages. Detailed guidelines will be out later. In the case of switching outstanding mortgages to amortized ones, the loan-to-value and debt-to-income ratios previously applied will be applied same without recalculating LTV and DTI ratios.

In regard with floating-rate mortgages, banks will be required to decide the loan amount after considering potential increase in the borrower's debt servicing burden in the event of interest rate hikes. Stress rate will be added to the interest rate at the timing of mortgage lending when calculating the maximum amount of the floating-rate mortgage. Banks will be also required to evaluate a borrower's repayment ability for all other debts as well as a mortgage loan.

ASSESSMENT STANDARDS FOR A BORROWER'S REPAYMENT ABILITY

current	to be amended
principal & interest repayment of a mortgage loan + interest repayment of other debts	principal & interest repayment of a mortgage loan + **principal** & interest repayment of other debts
annual income	annual income

3. Tighten control over household debt growth in the non-banking sector

The FSC will restrict excessive increase in non-residential mortgages in the non-banking sector by strengthening evaluation of collateral and tightening the loan-to-value ratios for non-residential mortgages from September 2015. The LTV ratios will be set based on an average successful bid rate by region and collateral, while additional ratios by borrower will be adjusted reflecting risk factors. The minimum LTV ratio for non-residential mortgages will be lowered from the current 60% to 50% and cut further gradually in the future.

The FSC is considering incentives for non-bank financial institutions to increase amortized mortgages by temporarily reducing or exempting provisions for amortized mortgages. We will also strengthen monitoring of credit lending from the non-banking sector.[8]

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[6] e.g., income certificate, receipt of withholding tax, national pension contributions, health insurance premium

[7] e.g., credit card expenditure, sales, etc.

[8] credit lending (unit: trillion won)

	end-2012	end-2013	end-2014	end-March 2015
banks	90.4	94.3	94.7	**93.1**
non-banks	31.1	32.6	34.0	**34.4**

4. Strengthen a systemic resilience against potential risks of economic shocks

To strengthen a systemic resilience in the event of a crisis, household debt will be reflected as one of factors to be considered for banks to secure additional capital against possible risks.[9]

Monitoring of household debt will be strengthened with the relevant government agencies, financial companies, research institutions and credit bureaus. From next year, financial institutions' micro data on household loans will be compiled by the FSS to be used in monitoring.

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For any inquiry, please contact Foreign Press & Relations Team at fsc_media@korea.kr

[9] e.g., household lending will be factored into selecting "domestic systemically important banks (D-SIBs), deciding imposition of countercyclical capital buffer and assessing risks to impose additional capital under Pillar 2.