

FSC HOLDS MEETING TO REVIEW CORPORATE BOND AND MONEY MARKET SITUATION AND REAL ESTATE PF RISKS

The FSC held a meeting with relevant authorities to review the corporate bond and short-term money market situation and risks in the real estate project finance (PF) market on March 6.¹ At the meeting, authorities discussed (a) the current corporate bond and money market trends, (b) direction for addressing risks in the real estate PF market, (c) direction to revise the inter-creditor agreement in real estate PF, and (d) measures to support private sector-led real estate PF restructuring.

INSPECTION RESULTS ON CORPORATE BOND AND MONEY MARKET

At today's meeting, participants assessed that the corporate bond and money markets are showing clear signs of recovering from the contraction seen in the second half of last year. Corporate bond spreads have narrowed since the end of November last year,² and demands for issuing corporate bonds are being smoothly absorbed in the market as the volume of non-financial corporate bonds issued in last January and February surpassed the amount of bonds reaching maturity.³ In the money market, interest rates on commercial papers (CPs) have continued to decline⁴ due to the turnaround in liquidity conditions, and those on PF-ABCPs (project finance asset backed commercial papers) also appear to be on decline, compared to the end of last year. However, it is necessary to watch over market situations with vigilance because interest rates on PF-ABCPs with rating of A2 or lower still remain high, and as the issuance of corporate debts with shorter term maturities is taking place more frequently.

Meanwhile, there still remain high uncertainties around financial markets this year, as it is forecast that the U.S. will continue to maintain its current tightening stance for longer with the help of its strong economic indicators and the higher-than-expected price indices and the war between Russian and Ukraine and the friction between the U.S and China continue. Therefore, participants agreed to continuously monitor the volatility of corporate bond and money markets with a sense of alertness and respond to it when needed. In addition, utilizing the market stabilization programs, which currently have more than KRW40 trillion in their remaining capacity, participants agreed to continue to provide and expand the availability of policy support in order to maintain stability in the corporate bond and money markets.

¹ The meeting was chaired by FSC Standing Commissioner Kwon Dae-young and participated by officials from the Financial Services Commission, the Ministry of Economy and Finance, the Financial Supervisory Service, the Bank of Korea, policy financial institutions, financial companies and industry associations.

² Corporate bond spreads (compared with 3-yr KTBs, AA-, 3-yr, bp): 177 (year-high, Nov 30, 2022), 99 (Jan 31, 2023), 67 (Mar 2)

³ Net issuance of non-financial corporate bonds (in trillion won): 4.0 (Jan 2023), 4.3 (Feb)

Bond bookbuilding participation rate: 7.2 times (Jan 2023), 5.5 times (Feb)

⁴ CP interest rates (A1, 3-month, %): 5.54 (year-high, Dec 9, 2022), 4.52 (Jan 31, 2023), 4.02 (Mar 2)

RESPONSE MEASURES ON REAL ESTATE PF

At the meeting, participants evaluated, compared to the past crisis, the current real estate PF market situation cannot be seen as a system-wide risk, but that there still remain segment-specific risks and difficulties for certain sectors and regions.

Anxieties in the real estate market have been subsiding on the back of the government's measures to stabilize short-term money market, induce normal supply of funds to real estate projects that are under sound management conditions and implement early rollback of real estate regulations. However, as a weakening of real estate PFs would have a large ripple effect on other areas such as the whole economy and financial markets and thus a recovery from the weakening inevitably takes a significant period of time, participants came to an agreement that it is necessary to draw up preemptive response measures. Since market players not only worry about the stability of real estate markets but also express concern over a potential moral hazard in the sector, authorities should also consider this separately when preparing measures, some participants pointed out.

The government has preemptively prepared the following policy measures to effectively deal with potential instability in the real estate PF market in the future.

- a) Authorities will comprehensively examine each site of real estate PF to look into its loan situation, implementation progress of the project, etc., and set up a quick reporting system for signs of abnormality intended to ensure prompt and timely response.
- b) Authorities will flexibly implement policies tailored to the specific situation and characteristics of each real estate PF site.
 - For the real estate project sites that are under normal management conditions, business loan guarantees will be promptly provided by either Korea Housing Finance Corporation or Korea Housing & Urban Guarantee Corporation to ensure that their projects can be financed seamlessly until the end of projects. As a part of this effort, Korea Housing Finance Corporation will launch a new guarantee program worth KRW1.5 trillion in March for PF-ABCPs switching to long-term loans to help alleviate refinancing risk.
 - For the real estate project sites that are considered to be at risk of facing default risk, a revision to the real estate PF inter-creditor agreement will operate (in April 2023), and the Korea Asset Management Corporation, etc. will actively support financial restructuring driven by the private sector (H1 2023).

<Real Estate PF Inter-Creditor Agreement to be Revised as Shown Below>

- **(Expanded list of entities joining inter-creditor agreement)** Mutual finance unions and cooperatives and the Korea Federation of Community Cooperatives to be included.
- **(Resolution requirement for autonomous council)** Different resolution criteria to be applied for each resolution item to facilitate prompt decision making.

- For the poorly managed real estate project sites, authorities will work to induce takeover by a new project management entity through a selloff and liquidation

process based on market principles.

- c) Authorities will increase the amount of policy funds supplied to construction companies, etc. to KRW28.4 trillion (an increase of KRW5 trillion from the end-2022 balance) and strengthen risk management over real estate trust companies in order to prevent contagion of real estate PF risks into construction companies or real estate trust companies.

FURTHER PLAN

In order to ensure stabilization of the real estate PF and financial markets, the government will flexibly and seamlessly implement the existing programs while actively pursuing the measures announced at today's meeting. In addition, after considering market situations, etc., authorities will promptly review and decide whether to extend the grace period for the easing of certain financial regulations.

As market stability is fostered by market participants themselves, if they all play their respective roles faithfully while having trust in the government-prepared measures, it will be possible to stably manage risks in the market. In this regard, highly valuing the importance of communication with field players, authorities will regularly hold meetings with experts in the real estate PF sector to closely communicate with market participants and share recognition of the situation. In addition, along with the self-rescue efforts of various entities in the real estate PF market, authorities will prepare measures to prevent moral hazard in the industry.

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