

Press Release

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Comprehensive Policy Measures to Overcome the Ongoing Economic Difficulties

I . Background

The ongoing global financial turmoil originating from the U.S. sub-prime mortgage credit crunch has caused concerns. Uncertainties in the financial market have been aroused and these worries are having an impact on the real economy, resulting in slowing domestic demand and investment. The financial turmoil is appearing to morph into the worldwide economic crisis and prospects of a turnaround in the short term appear dim. In response, the Korean government proposes the following policy measures to cope with these unprecedented challenges and has announced preemptive, decisive and appropriate counter-measures.

II . Policy Measures

1. Measures to Stabilize the Foreign Exchange and Financial Market

1) Stabilization of the Foreign Exchange Market

The government will continue its efforts to mitigate adverse

external shocks and secure liquidity in the market by increasing bilateral currency swaps with other nations and expanding the FX reserves.

- ① In addition to the currency swap agreement between Korea and the U.S. amounting to \$30 billion, the Korean government and the Bank of Korea (BOK) will work to expand bilateral swap arrangements with China and Japan. The authorities will also make efforts to expedite the process of the Chiang-Mai Initiative;
- ② The government will increase the ceiling of the Foreign Exchange Stabilization Fund from the current 15 trillion won to 20.6 trillion won, equivalent to twice the volume of daily trading;
- ③ As part of an effort to improve the current account balance, the government will strengthen policies to promote exports. Investments in the Export Insurance Fund will increase and the upper limit of export insurance contracts will be raised from 130 trillion won to 170 trillion won. An additional 20 billion won will be provided to small and medium sized enterprise (SME) exporters to facilitate overseas marketing. The government will also promote export industries by expanding FTA partners. Efforts will be made to expedite FTA negotiations with the EU and to initiate the Korea-India FTA.

The government and the BOK will continue their efforts to maintain stability in order to avoid extreme volatility in the foreign exchange markets. Meanwhile, the Korean government will pursue policy efforts to help financial institutions secure sufficient FX liquidity. As the National Assembly has agreed to provide guarantees

on the external debt of banks, the Korean government will soon finalize the follow-up measures to provide guarantees on foreign currency deposits on the same level as those with local currency deposits.

In addition, Korea plans to participate in international cooperations to calm the global financial turbulence. The government will actively participate in sharing information and taking collective action through international financial institutions such as the IMF. It will also make efforts to collaborate with other countries on international finance policies within the ambit of G-20, of which Korea is likely to take chairmanship from 2010.

2) Stabilization of the Financial Market

The BOK will provide liquidity to securities firms and asset management companies by purchasing repurchase agreements, whilst the government will encourage the active role of institutional investors in the stock market.

The authorities will also continue to implement measures to cope with soaring market interest rates as follows: the BOK has preemptively cut benchmark interest rates by 75bp to 4.25% on October 27; and the government will encourage banks to lower lending rates of non-deposit funds (e.g. CDs, bonds).

In addition, the government will pursue the following measures to supply additional liquidity to financial institutions: the BOK will purchase repurchase agreements, government bonds and monetary-stabilization bonds; as well as to diversify its financial assets qualified for open market operations, including bank bonds

and bonds from certain public corporations such as Korea Land Corporation, Korea Housing Corporation, Small Business Corporation and Korea Housing Finance Corporation.

2. Measures to Stimulate the Real Economy

1) Strengthening of Fiscal Policies to Boost Domestic Demand

In response to the economic crisis, the government will adopt expansionary fiscal policies. The total fiscal stimulus package amounts to almost 14 trillion won, which includes 11 trillion won of public expenditures and 3 trillion won of tax reductions.

The Korean government will expand public expenditures by 11 trillion won to support low income class and local economies, out of which 4.6 trillion won will be invested in SOC projects. About 90% of additional expenditure will be spent on building local infrastructure to stimulate local economies: 3.4 trillion won will be paid out to ease financial distress of SMEs, small business owners, farmers and fishermen; 0.3 trillion won will be spent to tackle unemployment problems and support small business startups; 1 trillion won will be provided to support low income households; and 1.1 trillion won will be available for municipal government expenditure. Besides government expenditure, public corporations will also expand their investments by 1 trillion won.

The government also plans to provide additional tax support to facilitate investments. Temporary Investment Tax Credit will be extended for one more year until the end of 2009, and new investments inside the Population Control Zone will benefit from further tax deductions.

The currently uniform deduction rate (7%) will be differentiated

between regions. A 5% deduction will be applied to investments within Population Control Zones, while 10% will be applied to investments in other areas.

In order to strengthen the cyclical counter-measures, the Korean government plans to front-load its spending as much as possible, with a target spending of approximately 60%.

2) Revitalization of the Real Estate Market and Construction Activities

A potential sharp drop in asset prices may undermine the financial health of Korean financial institutions. Against this backdrop, the government will pursue efforts to revitalize the real estate market.

- ① The government will reduce the stringent requirements imposed upon the reconstruction of apartment buildings, such as the Small Size Apartment Ratios or the Rental Housing Apartment Ratios;
- ② The government is going to drastically reduce the total number of Overheated (Real Estate) Speculation Zones and Speculation-Prone Zones where strict monitoring and leveraging conditions are imposed. Overheated (Real Estate) Speculation Zones will be limited to Kangnam, Songpa, and Seochoe in Metropolitan Seoul as well as for the Speculation-Prone Zones.
- ③ The lock-up period for trading exclusive apartment purchase rights in the metropolitan area will be eased retrospectively and will also be applicable to apartments already sold¹⁾.

1) On Aug. 21st, the Korean government eased the lock up period to 5~7 years for the Population Control Zone and 3~5 years for other metropolitan areas. These measures have been applied only to apartments sold thereafter.

- ④ The Korean government will provide tax benefits for the acquisition of unsold houses in non-metropolitan areas. For homeowners purchasing additional houses in non-metropolitan areas, normal tax rates will be applied and Long-Term Special Deductions (up to 80%) will be permitted for the next two years.
- ⑤ Tax relief on equity sales tax will also be expanded. The acquisition of multiple homes due to unavoidable circumstances such as for work or to receive medical treatment will be treated as owning a single house and thus avoiding heavy taxation;
- ⑥ Residential requirements for single homeowners to be eligible for sales tax deductions will remain the same²⁾;
- ⑦ The Korea Credit Guarantee Fund (KCGF) will provide additional liquidity to construction companies by guaranteeing the government construction contract credit of up to 30 billion won per company; and
- ⑧ The government plans to cut the overdue interest for housing construction companies in arrears with building lot payments to the Korea Land Corporation.

3) Promotion of Investments through Reformed Regulations

With an intent to promote corporate investments, the Korean government will streamline and reduce excessive regulations

2) Current residential requirements are 2 years for Seoul, Gwacheon and 5 new cities. Initially, the plan was to tighten these requirements to 3 years for metropolitan areas and 2 years for non-metropolitan areas, from July 1st, 2009.

regarding the environment, land use, and labor issues.

- ① Regulations on plant establishment, facility expansion or relocation in the Industrial Complex within Growth Management Zones and Population Control Zones will be repealed. Restrictions on plant facility expansion outside the Industrial Complex will be drastically lifted;
- ② The ban on large scale building construction inside Wilderness Areas will be lifted on the condition that such buildings meet pollution mass control limits;
- ③ The supply of industrial sites will increase inside Growth Management Zones, while the entire Incheon Free Economic Zone (IFEZ) will be designated as a Growth Management Zone;
- ④ Environmental regulations deemed excessive compared to those of competing countries will be reviewed and streamlined. Regulations within Environment Protection Zones will be converted from location restrictions to emission control;
- ⑤ The government will make efforts to enhance the flexibility of the labor market. The employment system for temporary workers and dispatched workers will be improved and complementary measures to ease the burden of enterprises will be considered; and
- ⑥ The government will encourage new investments and facilitate the generation of new jobs through regulatory reform of the service sector. It will also continue efforts to increase the competitiveness of high value-added services such as

broadcasting, advertising, designing as well as to lower entry barriers for entry into services such as education and medical services.

3. Measures to Support SMEs and Low Income Families

The government will strive to ease the financial distress of SMEs so as to protect viable enterprises from falling into liquidity traps. Efforts will also be made to alleviate burden on households, by lowering interest rates and strengthening financial support.

- ① The government will provide 1.3 trillion won to state owned banks, such as the Korea Development Bank, the Industrial Bank of Korea, and the Korea Exim Bank in order to provide financial assistance to SMEs;
- ② The government will expand credit guarantees of 6 trillion won to SMEs by contributing 500 billion won to the KCGF and the Korea Technology Guarantee Fund (KTGF). An additional 1.5 trillion of credit guarantees will be provided by the Regional Credit Guarantee Fund;
- ③ To ease the financial distress of exporting SMEs, the government will increase financial aid through the Korea Exim Bank (from 7.5 trillion won in 2008 to 8.5 trillion won in 2009) and expand FX insurance loans and export insurances by 3.5 trillion won;
- ④ The government will pursue efforts to support small businessmen, farmers and fishermen. It will provide financial aid, education and consulting support as well as business start-up services;

- ⑤ As a follow up measure to the government guarantee on the external debt of banks, the government will encourage banks to roll-over loans for viable SMEs by signing MOUs;
- ⑥ By subscribing an additional 100 billion won to the Korea Housing Finance Corporation (KHFC), the government will assist in lowering mortgage loan rates. It will encourage the KHFC to convert floating-rate loans to fixed-rate loans, and increase the supply of long-term fixed-rate mortgage loans;
- ⑦ The government will also strengthen its efforts to tackle youth unemployment problems by expanding internship programs and enhancing job training programs;
- ⑧ The government will reinforce its welfare support for low income families. Financial aid for the unemployed and scholarship programs for low income students will expand; and,
- ⑨ The government will encourage card companies to lower credit card fees for small retailers.

III. Action Plan

- 1. Market stabilization measures not requiring legislative measures will be put into action as soon as possible.
- 2. Steps for fiscal expansion will be made during the National Assembly season this year.
- ① The Korean government will propose a revised budget after

further discussions following Government-Party consultations.

② Revisions to ease real-estate regulations will be handled by the ruling party after Government-Party consultations.

- Extending the Temporary Investment Tax Credit expiration to the end of 2009 will be made by the end of this year, with the revision of the 'Special Tax Treatment Control Enforcement Decree'.

3. Revision bills on labor market flexibility will be submitted to the National Assembly soon after exchanging opinions with diverse stakeholders.