Financial Services Commission

Press Release

June 18, 2020

VICE CHAIRMAN HOLDS MEETING TO REVIEW RISKS IN FINANCIAL SECTORS

Vice Chairman Sohn Byungdoo held a meeting to review market conditions and risk factors in the financial industry on June 18 with experts from the public and private sectors.

The following is a summary of Vice Chairman Sohn's remarks.

(END-OF-QUARTER-EFFECT IN JUNE) In March, the global spread of the COVID-19 infection, rising instability in financial markets and the end-of-quarter shortage in capital supply led to difficulties in the corporate bond and short-term money markets. In response, the government launched various financial support and liquidity injection measures, including a bond market stabilization fund and an SPV to purchase lower-rated corporate bonds and CP. As a result, the markets have begun to show signs of recovery with yield spreads growing at a slower rate.

However, blue chip companies and non-blue chip companies face different conditions for issuing bonds. In June, a total of KRW68 trillion worth of corporate debt will be up for maturity (KRW12.2 trillion in corporate bonds and KRW55.5 trillion in CP and short-term debt). About 90 percent of them are high rated debt and will face not much obstacle in meeting debt obligation. The securities firms with margin call obligations related to equity-linked securities are maintaining foreign currency liquidity in case of global stock price fall. Thus, the liquidity problem is not a major concern.

The government will temporarily ease the liquidity requirements of repo sellers to prevent a surge in cash demand at the end of June. The government will also provide support through policy banks' corporate bond and CP purchase programs.

(INVESTOR PROTECTION WITH DERIVATIVES PRODUCTS) With investors' interest in derivatives products growing, the volumes of FX margin trading and CFD transaction by retail investors have increased significantly this year. For FX margin trading, the proportion of retail investors is very high at about 92 percent, despite the implementation of various measures, such as stricter rules for deposit requirements and risk disclosure. In addition, some of the securities firms have expanded their CFD trading businesses since the government lowered entry barriers for retail investors last November. These derivatives products have high potential to cause damages to investors due to high volatility. The government will continue to closely monitor trading activities. Meanwhile, retail investors should make investment based on rational decisions with thorough understanding of profit structures. Also, the financial authorities are closely looking into the ways in which some of the high-yield, high risk ELS products are being advertised or sold to investors in order to ensure that there are no unfair sales practices involved.

(SOUNDNESS OF FINANCIAL COMPANIES) Amid the continuing trend of low interest rates, the size of investment in overseas real estate has grown significantly.[1] However, when investment losses occur, overseas real estate investment can pose risks to the financial soundness of securities companies. Also, with a large proportion of sell downs to retail or corporate investors, possible damages to investors are concerning. As such, the government will strengthen risk management and enhance monitoring of securities firms' overseas real estate investment while requiring internal reviews from securities companies.

As for venture capital firms, their dependence on the corporate bond market requires a close scrutiny with regard to liquidity problems. The capital raising by venture capital firms contracted amid the pandemic-induced credit crunch in the market, but with the bond market stabilization fund and P-CBOs, the conditions improved beginning in May. The industry has maintained a low default rate and its equity capital ratio remains above the threshold. In the case of a prolonging pandemic situation, venture capital firms may face the risk of falling asset values and difficulties raising capital as individual businesses struggle. Thus, the government will continue to support the issuance of low-rated corporate debt issued by credit lending institutions, while strengthening risk management by drawing up best practice guidelines on liquidity risk management.

With the financial industry's preemptive and proactive response to the COVID-19 crisis, the OECD projects that Korea's growth forecast is least affected by the pandemic. To support the real economy sectors, the government will continue to closely monitor risk factors in the financial industry.

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[1] KRW1.1 trillion (pre-2016) → KRW3.1 trillion (2017) → KRW5.6 trillion (2018) → KRW11.7 trillion (2019)