

JCR Affirmed A+/AA- (FC/LC) Ratings on Korea

Japan Credit Rating Agency, Ltd. (JCR) announces the following credit rating.

Rationale

The ratings reflect the government's sound fiscal position, the country's highly advanced and diversified export industries and its economic development driven by those industries. On the other hand, JCR will keep watch on the future development of the country's household debt problems, the North Korea issue and the European sovereign debt crisis along with their possible impacts on the Korean economy.

The rating outlook is stable. The already decelerating Korean economy is likely to continue a moderate downtrend in 2012 as exports, the engine of the past growth, are expected to slow down on a global economic downturn. The Korean economy has consistently strengthened its exposure to the world economy through its trade expansion in the recent years. The country's foreign currency liquidity position has improved as compared to that before the Lehman shock due to the effect of the measures taken by the government to curb short-term external debts as well as the expansion of the currency swap agreements with the monetary authorities of Japan and China. However, as the future course of the European debt crisis remains unpredictable, its future development and possible impact on the world and Korean economies need to be monitored.

(1) Macroeconomic trends

The Korean economy grew a comparatively high 6.2% in 2010 albeit on the lowered base of the previous year but turned moderately slowing down in 2011 due to a rise of inflationary pressure and subsequent interest rate hikes. The economic growth rate declined to 3.6% in the year. For 2012, the growth of exports may decelerate on a slowdown of the world economy resulting from the European debt crisis. As this will affect employment, private consumption and corporate investments, the Korean economy may continue slowing down moderately to a 3.0-3.5% growth rate. Although the rising inflationary pressure has been a cause for concern since early 2011, the CPI growth rate has basically been on the downtrend after peaking out in August. A major deterioration of the world economy cannot be ruled out depending on the future course of the European debt crisis. JCR will watch how the crisis will be dealt with and how it may impact the Korean economy. JCR also sees it necessary to monitor how household debt burdens in Korea will evolve in the medium run and how higher interest rates may affect its economy.

(2) Public Finance and Financial System

Despite the public fund injection during the financial reforms after the Asian currency crisis, the country's public debt has since stayed at manageable levels thanks to the government's conservative fiscal management. The general government public debt/GDP ratio rose to 33.4% at the end of 2010 from 30.1% at the end of 2008 due to the expanded fiscal spending necessitated by the global financial woes. However, the ratio is still remarkably low by international standard. The government has implemented fiscal consolidation since 2010, keeping its fiscal balance basically in surplus. Therefore, the public debt/GDP ratio is expected to go down from here on barring contingencies such as a steep deterioration of the world economy.

The country's financial system has restored soundness thanks to the structural reforms implemented after the Asian currency crisis. However, the banking sector's loan/deposit ratio had soared till 2007 amid intensified competition, which was one of the factors that brought serious foreign currency liquidity problems to Korean banks from the end of 2008 to early 2009. But the ratio was on the decrease afterward following the tightened regulations introduced by the monetary regulatory authorities. Meanwhile, the nonperforming loan ratio (on below substandard loan basis) of commercial banks was still kept low at 1.7% as of the end of September 2011. The capital adequacy ratio on a BIS basis stood at 14.1% (Tier I ratio: 11.4%) at the end of September 2011, which indicates that there is little immediate concern over the banking sector's risk bearing capacity.

(3) External Balance

Korea has retained a current account surplus in recent years thanks primarily to an increased trade surplus on increasing goods exports. The foreign exchange reserves fell drastically from late 2008 to early 2009 due mainly to an accelerated capital outflow caused by the impact of the global financial crisis. However, the reserves turned increasing again later as the impact of the crisis eased, the

policies taken by the Korean government and the Bank of Korea produced their effects, and the current account balance stayed in surplus. In 2011, there were times when the reserves turned decreasing due to a capital outflow caused by the European debt crisis. However, they recovered to reach USD308.6 billion at the end of November 2011, much bigger than their peak before the Lehman shock. The exchange reserves/short-term external debt ratio fell to 1.3 times in 2008 from 3.5 times at its peak in 2004 when the debt swelled in volume. The ratio improved to 2.2 times at the end of September 2011 after the government introduced new regulations on FX transactions by banks. In addition, due also to the expansion of the currency swap agreements with the monetary authorities of Japan and China, Korea's usable foreign currency facility has expanded to about USD150 billion on top of the exchange reserves. This indicates that the country's resilience to external shocks has largely improved as compared to that before the Lehman shock. The stability of the country's external balance will be maintained unless a global financial crisis deeper than the Lehman shock should occur due to aggravation of the European debt crisis.

(4) North Korea issue

Following deterioration of the relations between North and South Korea after the sinking of a South Korean patrol ship in March 2010, military tensions mounted in the wake of North Korea's bombardment of Yeonpyeong Island in November that year. Tensions somewhat eased later on. However, the geopolitical risks on the Korean Peninsula remain unpredictable following the North's power transfer in December 2011. JCR will keep a close watch on future developments of the bilateral relations.

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Rating

Issuer: Republic of Korea

<Affirmation>

Issues	Rating	Outlook
FC (Foreign Currency Long-Term Senior Debts)	A+	Stable
LC (Local Currency Long-Term Senior Debts)	AA-	Stable

Outline of the method for the determination of Credit Ratings is posted as "Rating Methodology (Sovereign & Supranationals)" on JCR's home page (<http://www.jcr.co.jp>). The rating methodology is subject to additions and changes. In such cases, however, these additions and changes are shown in chronological order. Please check the release date of this press release against that of the rating methodology (i.e., the date when such methodology became effective) and then refer to the rating methodology above.

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