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Week 3: Private Finance for Development

**Korean Capital Market Development**

*With Mr. Jaehoon Yoo*

Billions to trillions to action. Mobilizing finance for development 2016-2030.  
Korean capital market development, with Jaehoon Yoo.

The role of capital market in developing countries has three functions, which might differ from advanced capital markets.

Number one, basically the capital market development is regarded as a policy tool for economic growth. Secondly, the government of developing countries should make best use of capital markets for institutional-building and capacity-building to run the capital market. Therefore, it is quite natural that they are mandated to play a role of regulator, as well as promoter. Finally, the capital market is also mandated to carry out the legal reform to develop the corporate sector, in particular in the traditional economies. But it is much harder to create a capital market in the developing countries.

The history of Korea's capital market can be divided into five stages. First, in the years of '60s and '70s, the capital market development policies have been focused on basic system building and the primary market development for industrial development.

The second stage is 1980s. The key word was market principle-based reform, and also democratization of stock market. In other words, the population for the first time came to know that stocks, bonds are a good way of saving their moneys. 1990s, it is market opening era. The market opening was the most important factor to develop the capital marketing career.

At the same time, the innovation financing was for the first time the important agenda in the capital market development. 1997, Asian crisis has hit Korea. The capital market was not an exception. It was a disguised blessing. The same applies to the capital market. It has had a unique opportunity to carry out a comprehensive reform in the capital market.

We gained valuable lessons and experiences and the system that has long been debated without result was actually implemented. The most important achievement can



be said, at least on the supervisory sector, we have a new supervisory system, and secondly, we have the government bond market which is running at a global standard.

Finally, in 2008 when the global crisis took place, we entered the era of low growth, low inflation, population aging. Therefore, the capital market of Korea has to deal with the other reform agendas, such as investor protection, and pension industry development, and once again, innovation financing to resolve the stagnant growth potential.

I would like to say three different categories of agencies. Number one, capital market policy maker and second, enforcement body, and thirdly, market infrastructure companies. Number one, the capital market policy maker, which is currently called Financial Services Commission. What I like to point out, in case of Korea, two things. The capital market policy is always combined with two functions of promotion and regulation of the markets.

As to enforcement body, there is a Securities and Futures Commission which is under the Financial Services Commission. The commission, the FSC, is very much focused on enforcement functions against criminals' activities at the securities market. We also have a very specialized function in the prosecutor's office. These two organizations closely cooperate. Market infrastructure companies - the most important company is KRX, the Korea's Stock Exchange. The company is a consolidated exchange which covers the main board market, the venture board market, derivatives market, and CCP functions in some markets, and it also carries out treasury repository functions, as well.

The second most important institution is KSD, Korea Securities Depository, which I belong to. KSD as like other CSDs, we carry out basic functions of CSD which is deposit, settlement and clearing, but our business portfolios has evolved to more value-added, more advanced services such as collateral management, repo market service, and securities lending and borrowing service.

We also have three other important infrastructure agencies. Korea Securities Finance Corporation, which basically carries out securities financing and KOSKOM, which is an important IT company, which is running the backbone of Korea's capital market. And finally, we have Korea Finance Investment Association which carries out not only the industry interest-advocating function, but also some self-regulatory function.

It also runs over-the-counter market, which is called KOTC market.



These three categories of institutions have demonstrated a good model of teamwork under the leadership of decision maker since the 1960s, when we first began our industrial development.

Let me explain about advantages in equity and bond markets first, then I'll elaborate on other sectors.

On equity side, I think Korea is running a well-structured multi-tiered stock market system, which covers large firms down to small venture firms. Even a startup can use a crowdfunding system.

It is related to my second point in the equity market, the KOSDAQ, Korea's innovative venture board is considered a very successful venture market, which can finance the much-needed risk capitals for venture companies. Let me turn to the bond market. Korea's bond market, its total balance is \$1.4 trillion US dollars, which is basically as big as the total GDP of Korea, the thirteenth largest in the globe. It has not only well-functioning government bond market, but also having well diversified corporate bond market, as well as derivatives market. Other advantages that Korea's capital market has is the big appetite of institutional investors for domestic and overseas assets. We already have fourth largest pension in the world, which requires more diversified asset portfolios.

Their appetite is ever-increasing. Also, we have good experiences of public-private partnership program and also, we also have private equity fund, and real estate investment trust market, which can help private financing methods in the capital market.

The market capitalization is 1.2 trillion, the thirteenth largest market in the world. It has a relatively well-balanced, well-structured equity market system.

So we have KOSPI, KOSDAQ, KONEX, KOTC markets which will cover from startup companies up to large companies, when they finance equity capital. Second advantage of equity market is our venture capital market. The KOSDAQ is always considered a successful model of venture board in the developing countries. I believe there are some valuable experiences that other countries can learn from.

On the bond side, Korea's bond market is 1.4 trillion, which is largely equivalent to its total GDP of Korean economy. It has not only a sizable government bond market but also has a well-diversified corporate bond market, financial bond market. It also has a well-developed derivatives market, too.



There is an increasing appetite of institutional investors in Korea. For example, there is the fourth largest pension in the world.

If there are good development projects, I think there are good appetites for institutional investors to put their money in. We also have plenty of experiences in PPP, as well as private equity funds and real estate investment vehicles. Therefore, project financings are all possible through various ways of funding.

The disadvantage of Korea's capital market is we are still lacking the junk bond market. There is no high risk, high yield bond market, and also, there is a certain conservatism amongst institutional investors that is still remaining as obstacles for active project financing.

Korea is recently designated as RMB center by the Chinese government. The potential of RMB financial market in Korea is huge, because it has huge trade transactions with China. Therefore, if there are RMB-based financing needs happened, Korea is a good place to find out the RMB-based funding.