

IMPORTANT NOTICE

THIS DOCUMENT IS AVAILABLE ONLY TO INVESTORS WHO ARE NON-U.S. PERSONS WITH ADDRESSES OUTSIDE OF THE U.S.

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NOTHING IN THIS ELECTRONIC TRANSMISSION CONSTITUTES AN OFFER OF SECURITIES FOR SALE IN ANY JURISDICTION WHERE IT IS UNLAWFUL TO DO SO. THE SECURITIES DESCRIBED HEREIN HAVE NOT BEEN, AND WILL NOT BE, REGISTERED UNDER THE U.S. SECURITIES ACT OF 1933, AS AMENDED (THE "SECURITIES ACT"), OR THE SECURITIES LAWS OF ANY STATE OF THE UNITED STATES OR OTHER JURISDICTION AND THE SECURITIES MAY NOT BE OFFERED OR SOLD WITHIN THE UNITED STATES, EXCEPT PURSUANT TO AN EXEMPTION FROM, OR IN A TRANSACTION NOT SUBJECT TO, THE REGISTRATION REQUIREMENTS OF THE SECURITIES ACT AND APPLICABLE STATE OR LOCAL SECURITIES LAWS.

THE FOLLOWING OFFERING CIRCULAR MAY NOT BE FORWARDED OR DISTRIBUTED TO ANY OTHER PERSON AND MAY NOT BE REPRODUCED IN ANY MANNER WHATSOEVER, AND IN PARTICULAR, MAY NOT BE FORWARDED TO ANY U.S. PERSON OR TO ANY U.S. ADDRESS. ANY FORWARDING, DISTRIBUTION OR REPRODUCTION OF THIS DOCUMENT IN WHOLE OR IN PART IS UNAUTHORIZED. FAILURE TO COMPLY WITH THIS DIRECTIVE MAY RESULT IN A VIOLATION OF THE SECURITIES ACT OR THE APPLICABLE LAWS OF OTHER JURISDICTIONS. ANY INVESTMENT DECISION SHOULD BE MADE ON THE BASIS OF THE FINAL TERMS AND CONDITIONS OF THE RELEVANT SECURITIES. IF YOU HAVE GAINED ACCESS TO THIS TRANSMISSION CONTRARY TO ANY OF THE FOREGOING RESTRICTIONS, YOU ARE NOT AUTHORIZED AND WILL NOT BE ABLE TO PURCHASE ANY OF THE SECURITIES DESCRIBED THEREIN.

Confirmation of your Representation: In order to be eligible to view the following offering circular or make an investment decision with respect to the securities, investors must not be a U.S. person (within the meaning of Regulation S under the Securities Act). By accepting the e-mail and accessing the following offering circular, you shall be deemed to have represented to us that (1) you are not a U.S. person nor are you acting on behalf of a U.S. person, the electronic mail address that you gave us and to which this e-mail has been delivered is not located in the United States, its territories or possessions and, to the extent you purchase the securities described in the following offering circular, you will be doing so pursuant to Regulation S under the Securities Act and (2) you consent to the delivery of such offering circular and any amendments and supplements thereto by electronic transmission.

You are reminded that the following offering circular has been delivered to you on the basis that you are a person into whose possession the following offering circular may be lawfully delivered in accordance with the laws of jurisdiction in which you are located and you may not, nor are you authorized to, deliver or disclose the contents of the following offering circular to any other person. If this is not the case, you must return this Offering Circular to us immediately.

The materials relating to the offering do not constitute, and may not be used in connection with, an offer or solicitation in any place where offers or solicitations are not permitted by law. If a jurisdiction requires that the offering be made by a licensed broker or dealer and the underwriter or any affiliate of the underwriter is a licensed broker or dealer in that jurisdiction, the offering shall be deemed to be made by the underwriter or such affiliate on behalf of the issuer in such jurisdiction.

The following offering circular has been sent to you in an electronic form. You are reminded that documents transmitted via this medium may be altered or changed during the process of electronic transmission and consequently, none of the issuer nor BNP Paribas, Citigroup Global Markets Limited, Credit Suisse Securities (Europe) Limited and Nomura International plc (the "Managers"), nor any person who controls any of them nor any director, officer, employee nor agent of any of them or affiliate of any such person accepts any liability or responsibility whatsoever in respect of any difference between the offering circular distributed to you in electronic format and the hard copy version available to you on request from the Managers.

You should not reply by e-mail to this announcement, and you may not purchase any securities by doing so. Any reply e-mail communications, including those you generate by using the "Reply" function on your e-mail software, will be ignored or rejected. You are responsible for protecting against viruses and other destructive items. Your use of this e-mail is at your own risk and it is your responsibility to take precautions to ensure that it is free from viruses and other items of a destructive nature.



Small and medium Business Corporation

(A statutory juridical entity established under the Small- and Medium-sized Enterprises Promotion Act, as amended, in the Republic of Korea)

US\$500,000,000 2.125% Notes due 2026

Issue Price: 99.011%

The US\$500,000,000 2.125% Notes due 2026 (the “Notes”) of Small and medium Business Corporation (“SBC”) will mature on August 30, 2026 (the “Maturity Date”). The Notes will bear interest at the rate of 2.125% per annum from, and including, August 30, 2016 (the “Issue Date”) to, but excluding, the Maturity Date. Interest will be payable semi-annually in arrears on February 28 (or February 29 in a leap year) and August 30 in each year, commencing February 28, 2017.

Approval in-principle has been received from the Singapore Exchange Securities Trading Limited (the “Singapore Stock Exchange”) for the listing and quotation of the Notes on the Singapore Stock Exchange. The Singapore Stock Exchange assumes no responsibility for the correctness of any statements made, opinions expressed or reports contained herein. Approval in-principle from, admission to the Official List of, and listing and quotation of the Notes on, the Singapore Stock Exchange are not to be taken as an indication of the merits of SBC or the Notes.

The Notes have been rated “Aa2” by Moody’s Investors Service (“Moody’s”) and “AA-” by Fitch Ratings Inc. (“Fitch”). The credit ratings accorded to the Notes are not a recommendation to purchase, hold or sell the Notes in as much as such ratings do not comment as to market price or suitability for a particular investor. There can be no assurance that the ratings will remain in effect for a given period or that the ratings will not be revised by the rating agencies in the future.

See “Investment Considerations” beginning on page 5 for a discussion of certain factors to be considered in connection with an investment in the Notes.

The Notes have not been and will not be registered under the United States Securities Act of 1933, as amended (the “Securities Act”), and subject to certain exceptions, may not be offered or sold within the United States or to, or for the account or benefit of, U.S. persons (as defined in Regulation S under the Securities Act (“Regulation S”).

For a description of these and certain further restrictions on offers and sales of the Notes and the distribution of this Offering Circular, see “Subscription and Sale.”

The Notes will be evidenced by a global certificate (the “Global Certificate”), in registered form, which will be registered in the name of a nominee of, and deposited with a common depository for, Euroclear Bank S.A./N.V., as operator of the Euroclear System (“Euroclear”), and Clearstream Banking, S.A., (“Clearstream, Luxembourg”) on or about the Issue Date. Beneficial interests in the Global Certificate will be shown on, and transfers thereof will be effected only through, records maintained by Euroclear and Clearstream, Luxembourg and their respective accountholders. Except in limited circumstances set out herein, individual certificates for Notes will not be issued in exchange for beneficial interests in the Global Certificate. See “The Global Certificate.”

Joint Bookrunner and Joint Lead Managers

**BNP PARIBAS
Credit Suisse**

**Citigroup
Nomura**

The date of this Offering Circular is August 22, 2016.

TABLE OF CONTENTS

	<u>Page</u>
SUMMARY	1
INVESTMENT CONSIDERATIONS	5
USE OF PROCEEDS	9
SMALL AND MEDIUM BUSINESS CORPORATION	10
THE REPUBLIC OF KOREA	27
TERMS AND CONDITIONS OF THE NOTES	67
THE GLOBAL CERTIFICATE	77
TAXATION	79
SUBSCRIPTION AND SALE	81
LEGAL MATTERS	85
INDEPENDENT AUDITORS	85
INDEX TO FINANCIAL STATEMENTS OF THE SME FUND	F-1

THE NOTES MAY NOT BE OFFERED OR SOLD, DIRECTLY OR INDIRECTLY, IN KOREA OR TO ANY RESIDENT OF KOREA, EXCEPT AS PERMITTED BY APPLICABLE KOREAN LAWS AND REGULATIONS.

You should only rely on the information contained or incorporated by reference in this Offering Circular. SBC has not, and the Managers (as defined in “Subscription and Sale”) have not, authorized anyone to provide you with different information. If anyone provides you with different or inconsistent information, you should not rely on it. SBC is not, and the Managers are not, making an offer to sell these securities in any jurisdiction where the offer or sale is not permitted. You should assume that the information appearing in the Offering Circular is accurate only as of the date on the front cover of this Offering Circular. SBC’s business, financial condition, results of operations and prospects may have changed since that date.

IN CONNECTION WITH THIS OFFERING, CITIGROUP GLOBAL MARKETS LIMITED (THE “STABILIZING MANAGER”) OR ANY PERSON ACTING FOR IT, ON BEHALF OF THE MANAGERS, MAY OVERALLOT OR EFFECT TRANSACTIONS, TO THE EXTENT PERMITTED UNDER APPLICABLE LAWS AND REGULATIONS, WITH A VIEW TO SUPPORTING THE MARKET PRICE OF THE NOTES AT A LEVEL HIGHER THAN THAT WHICH MIGHT OTHERWISE PREVAIL FOR A LIMITED PERIOD OF TIME AFTER THE ISSUE DATE. HOWEVER, THERE MAY BE NO OBLIGATION ON THE STABILIZING MANAGER OR ITS AGENT TO DO THIS. SUCH STABILIZATION, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME, AND MUST BE BROUGHT TO AN END AFTER A LIMITED PERIOD. SUCH STABILIZATION SHALL BE IN COMPLIANCE WITH ALL APPLICABLE LAWS, REGULATIONS AND RULES.

This Offering Circular contains information with regard to SBC and the Notes. SBC accepts responsibility for the information contained in this Offering Circular. To the best of knowledge and belief of SBC (having taken all reasonable care to ensure that such is the case), the information contained in this Offering Circular is in accordance with the facts and does not omit anything likely to affect the import of such information. SBC, having made all reasonable enquiries, confirms that this Offering Circular contains all information which is material in the context of the issue, offering and sale of the Notes, that the information contained in this Offering Circular is true and accurate in all material respects and is not misleading, that the opinions and intentions expressed in this Offering Circular are honestly held and have been reached after considering all relevant circumstances and are based on reasonable assumptions, and that there are no other facts the omission of which would make this Offering Circular or any of such information or the expression of any such opinions or intentions misleading. SBC accepts responsibility accordingly. Information provided in this Offering Circular with respect to Korea, its political status and economy, has been derived from information published by the Government and other public sources, and SBC accepts responsibility only for the accurate extraction of information from such sources.

Neither the delivery of this Offering Circular nor any offering, sale or delivery made hereunder shall, under any circumstances, constitute a representation or create any implication that there has been no change, or any event reasonably likely to involve any change, in SBC’s affairs since the date hereof. This Offering Circular does not constitute an offer of, or an invitation by, or on behalf of, SBC or the Managers to subscribe for, or purchase, any of the Notes. This Offering Circular does not constitute an offer, and may not be used for the purpose of an offer to, or a solicitation by, anyone in any jurisdiction or in any circumstances in which such an offer or solicitation is not authorized or is unlawful.

The Managers have not separately verified the information contained herein. Accordingly, no representation, warranty or undertaking, express or implied, is made and no responsibility or liability is accepted by the Managers or any of them as to the accuracy or completeness of the information contained in this Offering Circular or any other information provided by SBC in connection with the Notes or their distribution.

This Offering Circular is not intended to provide the basis of any credit or other evaluation and should not be considered as a recommendation by SBC or the Managers that any recipient of this Offering Circular should purchase any of the Notes. Each investor contemplating purchasing Notes should make its own independent investigation of the financial condition and affairs, and its own appraisal of the creditworthiness, of SBC.

The distribution of this Offering Circular and the offering, sale and delivery of Notes in certain jurisdictions may be restricted by law. Persons into whose possession this Offering Circular comes are required by SBC and the Managers to inform themselves about and to observe any such restrictions. For a description of certain restrictions on offers, sales and deliveries of Notes and on distribution of this Offering Circular, see “Subscription and Sale.”

Any purchase or acquisition of the Notes is in all respects conditional on the satisfaction of certain conditions set out in the Subscription Agreement (as defined herein) and the issue of the Notes by SBC to the Managers pursuant to the Subscription Agreement. Any offer, invitation to offer or agreement made in connection with the purchase or acquisition of the Notes or pursuant to this Offering Circular shall (without any liability or responsibility on SBC’s part or on the part of the Managers) lapse and cease to have any effect if (for any other reason whatsoever) the Notes are not issued by SBC to the Managers pursuant to the Subscription Agreement.

If you are in any doubt about this Offering Circular, you should consult with your stockbroker, bank manager, solicitor, professional accountant or other professional adviser.

CERTAIN DEFINED TERMS AND CONVENTIONS

All references to “Korea” or the “Republic” herein are references to the Republic of Korea. All references to the “Government” herein are references to the government of the Republic of Korea. All references to “SBC,” the “Issuer,” “we,” “us” or “our” herein are references to Small and medium Business Corporation. References to “SMEs” herein are references to small- and medium-sized enterprises. References to the “SME Fund” are references to the Fund for the Establishment and Promotion of Small and Medium Enterprises.

In this Offering Circular, references to “Korean Won,” “Won,” “₩” or “KRW” are to the currency of the Republic and all references to “U.S. dollars,” “Dollars,” “\$” or “US\$” are to the currency of the United States of America (the “U.S.” or the “United States”). This Offering Circular contains a translation of certain Won amounts into Dollars at specified rates solely for the convenience of the reader. Unless otherwise indicated, translations of Won amounts into Dollars in this Offering Circular were made at the base rate under the market average exchange rate system, announced by Seoul Money Brokerage Services, Ltd., in Seoul, between the Won and the Dollar (the “Market Average Exchange Rate”). The translations of Won into Dollars for the annual accounts included in this Offering Circular were made at the Market Average Exchange Rate in effect on December 31, 2015, which was ₩1,172.0 to US\$1.00. No representation is made that the Won or Dollar amounts referred to in this Offering Circular could have been or could be converted into Dollars or Won, as the case may be, at any particular rate or at all.

Any discrepancies in the tables included in this Offering Circular between totals and the sums of the amounts listed are due to rounding.

ENFORCEMENT OF CIVIL LIABILITIES

SBC is established in Korea and all its directors and executive officers and certain other persons named in this Offering Circular are residents of Korea, and all or substantially all of SBC’s assets and assets of such persons are located in Korea. As a result, it may be difficult for you to effect service of process on these persons

within the United States, or to enforce against them or SBC in the United States judgments obtained in United States courts based on the civil liability provisions of the federal securities laws of the United States. There is doubt as to the enforceability in the Republic, either in original actions or in actions for enforcement of judgments of United States courts, of civil liabilities based on the federal securities laws of the United States.

PRESENTATION OF FINANCIAL INFORMATION

This Offering Circular includes the audited annual financial statements of the SME Fund as of and for the years ended December 31, 2014 and 2015 prepared in conformity with Accounting Standards for Non-Public Entities in the Republic of Korea (“K-GAAP for Non-Public Entities”). K-GAAP for Non-Public Entities differs in certain respects from International Financial Reporting Standards (“IFRS”) or other generally accepted accounting principles. The SME Fund is not required to prepare interim financial statements and has no plans to prepare interim financial statements in the future.

In making an investment decision, investors must rely upon their own independent examination of SBC, the terms of this offering and the most recent financial information, including the risks involved. Potential investors should consult their own professional advisers for an understanding of the differences between K-GAAP for Non-Public Entities and IFRS or other generally accepted accounting principles, and how these differences affect the financial information contained in this Offering Circular.

FORWARD-LOOKING STATEMENTS

This Offering Circular includes “forward-looking statements,” as defined in Section 27A of the Securities Act and Section 21E of the United States Securities Exchange Act of 1934, as amended, including statements regarding SBC’s expectations and projections for future operating performance and business prospects. The words “believe,” “expect,” “anticipate,” “estimate,” “plan,” “project,” “predict” and similar words identify forward-looking statements. In addition, all statements other than statements of historical facts included in this Offering Circular are forward-looking statements. Although SBC believes that the expectations reflected in the forward-looking statements are reasonable, it can give no assurance that such expectations will prove to be correct. These forward-looking statements speak only as of the date of this Offering Circular. SBC expressly disclaims any undertaking or obligation to release publicly any updates or revisions for any forward-looking statement contained herein to reflect any changes in SBC’s expectations with regard thereto or any change in events, conditions or circumstances. This Offering Circular discloses important factors that could cause actual results to differ materially from SBC’s expectations (“Cautionary Statements”). All subsequent written and oral forward-looking statements attributable to SBC or persons acting on behalf of SBC are expressly qualified in their entirety by the Cautionary Statements.

SUMMARY

This summary highlights information contained elsewhere in this Offering Circular. This summary is qualified by, and must be read in conjunction with, the more detailed information and financial statements appearing elsewhere in this Offering Circular. Prospective investors are urged to read this entire Offering Circular carefully, including the SME Fund's financial statements and related notes and "Investment Considerations."

SBC and the SME Fund

We are a statutory juridical entity established in 1979 pursuant to the Small- and Medium-sized Enterprises Promotion Act, as amended (the "SME Promotion Act"), to contribute to the development of the national economy by supporting and assisting small- and medium-sized enterprises in Korea. We are one of the few special statutory entities in Korea established with no paid-in capital and operate under the aegis of the Small and Medium Business Administration (the "SMBA") of the Ministry of Trade, Industry and Energy (the "MoTIE").

We are capitalized by the SME Fund established under the SME Promotion Act, and we play a central role in implementing the Government's policy to assist and support SMEs by administering the SME Fund and providing policy financing to SMEs as well as non-financial and other assistance to SMEs. We do not have or operate any separate accounts besides the SME Fund, and proceeds from any debt securities issued by us, including the Notes covered by this Offering Circular, will be credited to the SME Fund, and payments under such debt securities will be made from the SME Fund. The Government's capital contributions and loans are the primary sources of capital for the SME Fund.

Our registered address is 430, Dongjin-ro, Jinju-si, Gyeongsangnam-do 52851, Korea.

Government Supervision and Support

The policy financing that we provide to SMEs is meant to supplement commercial loans and is provided at below-market interest rates. Under Article 66-2 of the SME Promotion Act, any annual net profit from the administration of the SME Fund will be returned to the SME Fund, and the Government is obligated to replenish the SME Fund when there is a deficit. As a result of Article 66-2 of the SME Promotion Act, the Government is generally responsible for our operations and is legally obligated to replenish any deficit that arises if the SME Fund is insufficient to cover any of our annual net losses. In light of the above, if we have insufficient funds to make any payment under any of our obligations, including the Notes covered by this Offering Circular, the Government would take appropriate steps, such as by making a capital contribution, by allocating funds or by taking other action, to enable us to make such payment when due. The provisions of Article 66-2 do not, however, constitute a direct guarantee by the Government of our obligations, and the provisions of the SME Promotion Act, including Article 66-2, may be amended at any time by action of the National Assembly.

The Government closely supervises our operations and appoints members of our Board of Directors (except our standing Directors, who are appointed by our President) and steering committee, which handle our day-to-day operations, from various Government ministries. The SMBA, the Ministry of Strategy and Finance (the "MoSF") and the National Assembly approve our budget and operation plan for the SME Fund.

The Offering

The following is only a summary description of the Notes. This summary is derived from and should be read in conjunction with the full text of the terms and conditions of the Notes (the “Conditions”), see “Terms and Conditions of the Notes.” The Conditions prevail to the extent of any inconsistency with the terms set out in this section. Terms used in this summary and not otherwise defined shall have the meanings given to them in the Conditions and the Agency Agreement (as defined in the Conditions).

Issuer	Small and medium Business Corporation
Offering	US\$500,000,000 aggregate principal amount of 2.125% Notes due 2026 are being offered outside the United States to non-U.S. persons in reliance on Regulation S. See “Subscription and Sale.”
Issue Price	99.011% of their principal amount of the Notes, plus accrued interest, if any, from August 30, 2016.
Maturity Date	August 30, 2026.
Interest	The Notes bear interest at the rate of 2.125% per annum from, and including, August 30, 2016 to, but excluding, the due date for redemption of the Notes. Interest will be paid semi-annually in arrears on February 28 (or February 29 in a leap year) and August 30 in each year (each an “Interest Payment Date”). The first Interest Payment Date will be February 28, 2017 in respect of the period from, and including, August 30, 2016 to, but excluding, February 28, 2017.
Status of the Notes	The Notes are direct, unconditional, unsubordinated and (subject to Condition 4) unsecured obligations of SBC and (subject as stated above) rank and will rank pari passu, without any preference among themselves, and at least pari passu with all other present and future outstanding unsecured and unsubordinated obligations of SBC (other than obligations preferred by mandatory provisions of applicable law).
Negative Pledge	SBC will not create any Security Interest for the benefit of any holder of International Investment Securities or for any guarantee or indemnity in respect thereof without granting equivalent security for the Notes. See “Terms and Conditions of the Notes—Negative Pledge.”
Optional Tax Redemption	SBC may redeem all but not some of the Notes in the event of certain changes in Korean tax law. See “Terms and Conditions of the Notes—Redemption and Purchase—Redemption for Taxation Reasons.”
Withholding Tax	The principal of and interest on the Notes are payable without withholding or deduction for Korean withholding taxes to the extent set forth herein. See “Taxation—Korean Taxation.”

Further Issues	SBC may from time to time, without the consent of the holders of the Notes, create and issue further securities having the same terms and conditions as the Notes in all respects so that such further issue shall be consolidated and form a single series with the outstanding Notes to the extent permitted under the applicable laws.
Use of Proceeds	The net proceeds from the sale of the Notes will be used for general corporate purposes, including repayment of existing obligations under the account of the SME Fund. See “Use of Proceeds.”
Listings and Trading	Approval in-principle has been received from the Singapore Stock Exchange for the listing and quotation of the Notes on the Singapore Stock Exchange. The Notes will be traded in a minimum board lot size of S\$200,000 (or its equivalent in other currencies) for so long as the Notes are listed on the Singapore Stock Exchange and the rules of the Singapore Stock Exchange so require. Accordingly, the Notes will be traded in a minimum board lot size of US\$200,000.
Form and Denomination of the Notes . . .	The Notes are issued in minimum denominations of US\$200,000 and integral multiples of US\$1,000 in excess thereof. Except in the limited circumstances set forth under “The Global Certificate—Registration of Title,” the Notes will only be delivered in book-entry form. The Notes will be represented by a permanent Global Certificate in registered form without interest coupons which will be registered in the name of a nominee and deposited with a common depository for Euroclear and Clearstream, Luxembourg. The Notes are not issuable in bearer form. Beneficial interests in the Global Certificate will be shown on, and transfers thereof will be effected, only through the records maintained by Euroclear and Clearstream, Luxembourg and their respective account holders. See “The Global Certificate.”
Ratings	The Notes are rated “Aa2” by Moody’s and “AA-” by Fitch. Security ratings are not recommendations to buy, sell or hold the Notes. Ratings are subject to revision or withdrawal at any time by the rating agencies issuing such ratings.
Delivery of the Notes	Delivery of the Notes, against payment in same-day funds, is expected on or about August 30, 2016.
Fiscal, Principal Paying, Transfer Agent and Registrar	Deutsche Bank AG, Hong Kong Branch
Governing Law	The Notes and the Agency Agreement are governed by, and construed in accordance with, the laws of the State of New York.
ISIN	XS1477561606
Common Code	147756160

Summary Financial Information

The following tables set forth summary financial information. The summary financial information in the tables has been derived from the SME Fund's audited financial statements and related notes for each of the years ended December 31, 2014 and 2015 included elsewhere in this Offering Circular, which have been audited by Grant Thornton Daejoo, our independent auditors.

The summary financial information should be read in conjunction with the SME Fund's financial statements and notes thereto as of and for the years ended December 31, 2014 and 2015, which are included elsewhere in this Offering Circular. The SME Fund's financial statements have been prepared in accordance with K-GAAP for Non-Public Entities, which differs in certain significant respects from IFRS or other generally accepted accounting principles.

Balance Sheet Data

	<u>As of December 31,</u>	
	<u>2014</u>	<u>2015</u>
	(in billions of Won)	
Total loans ⁽¹⁾	₩14,340	₩13,579
Total borrowings (net of present value discounts) ⁽²⁾	14,800	14,125
Total assets	16,386	15,981
Total liabilities	14,946	14,317
Total equity	1,440	1,663

Notes:

- (1) Gross amount, which includes short-term loans and long-term loans without deducting allowance for doubtful accounts of ₩518 billion and ₩647 billion as of December 31, 2014 and 2015, respectively.
- (2) Net amount, which includes current portion of debt, long-term borrowings and debentures, deducting present value discounts of ₩2.3 billion and ₩1.9 billion as of December 31, 2014 and 2015, respectively.

Income Statement Data

	<u>For the year ended December 31,</u>	
	<u>2014</u>	<u>2015</u>
	(in billions of Won)	
Operating revenues	₩962	₩907
Operating expenses	973	969
Other income	24	68
Income before income taxes	12	6
Income tax benefit	11	6
Net Income	23	12

INVESTMENT CONSIDERATIONS

SBC's business and operations are subject to various risks, many of which are beyond its control. If any of the risks described below actually occurs, SBC's business, financial condition or results of operations could be adversely affected. These risks could materially affect SBC's ability to meet its obligations under the Notes. In such case, investors may lose all or part of their original investment in, and the expected return on, the Notes. Prospective investors of the Notes should carefully consider all of the information contained in this Offering Circular in addition to the following risk factors before making an investment decision.

Risks Relating to Korea and the Global Economy

Unfavorable financial and economic developments in Korea may have an adverse effect on us.

We are established in Korea, and substantially all of our operations are located in Korea. We serve as an execution arm for the Government policies and businesses relating to small- and medium-sized enterprises in Korea, supported by significant capital contributions and other support by the Government. As a result, we are subject to political, economic, legal and regulatory risks specific to Korea. The economic indicators in Korea in recent years have shown mixed signs of growth and uncertainty, and future growth of the economy is subject to many factors beyond our control.

In recent years, adverse conditions and volatility in the worldwide financial markets, fluctuations in oil and commodity prices and the general weakness of the U.S. and global economy have contributed to the uncertainty of global economic prospects in general and have adversely affected, and may continue to adversely affect, the Korean economy. The value of the Won relative to major foreign currencies in general and the U.S. dollar in particular has also fluctuated widely. Furthermore, as a result of adverse global and Korean economic conditions, there has been significant volatility in the stock prices of Korean companies in recent years. Future declines in the Korea Composite Stock Price Index (known as the "KOSPI") and large amounts of sales of Korean securities by foreign investors and subsequent repatriation of the proceeds of such sales may adversely affect the value of the Won, the foreign currency reserves held by financial institutions in Korea, and the ability of Korean companies to raise capital. Any future deterioration of the Korean or global economy could adversely affect our business, financial condition and results of operations.

Developments that could hurt Korea's economy in the future include:

- increased sovereign default risks in selected countries and the resulting adverse effects on the global financial markets;
- adverse conditions and volatility in the United States and worldwide credit and financial markets and the general weakness of the global economy;
- continuing adverse conditions in the economies of countries and regions that are important export markets for Korea, such as the United States, Europe, Japan and China, or in emerging market economies in Asia or elsewhere, as well as increased uncertainty in the wake of a referendum in the United Kingdom in June 2016, in which the majority of voters voted in favor of an exit from the European Union ("Brexit");
- adverse changes or volatility in foreign currency reserve levels, commodity prices (including oil prices), exchange rates (including fluctuation of the U.S. dollar or Japanese Yen exchange rates or revaluation of the Chinese Renminbi or the overall impact of Brexit on the value of the Korean Won), interest rates and stock markets;
- substantial decreases in the market prices of Korean real estate;
- a continuing rise in the level of household debt and increasing delinquencies and credit defaults by consumer and SME borrowers;

- declines in consumer confidence and a slowdown in consumer spending;
- adverse developments in the economies of countries that are important export markets for the Republic, such as the United States, Europe, Japan and China, or in emerging market economies in Asia or elsewhere;
- difficulties in the financial sector in Korea, including the savings bank sector;
- the continued growth of the Chinese economy, to the extent its benefits (such as increased exports to China) are outweighed by its costs (such as competition in export markets or for foreign investment and the relocation of the manufacturing base from the Republic to China);
- social and labor unrest;
- a decrease in tax revenues and a substantial increase in the Government's expenditures for fiscal stimulus measures, unemployment compensation and other economic and social programs that, together, would lead to an increased government budget deficit;
- financial problems or lack of progress in the restructuring of Korean conglomerates, other large troubled companies, their suppliers or the financial sector;
- loss of investor confidence arising from corporate accounting irregularities and corporate governance issues at certain Korean conglomerates;
- increases in social expenditures to support an aging population in Korea or decreases in economic productivity due to the declining population size in Korea;
- the economic impact of any pending or future free trade agreements;
- geo-political uncertainty and risk of further attacks by terrorist groups around the world;
- the occurrence of severe health epidemics in Korea and other parts of the world including an outbreak of severe acute, respiratory syndrome, or SARS, swine or avian flu, or Middle East Respiratory Syndrome, or MERS;
- deterioration in economic or diplomatic relations between the Republic and its trading partners or allies, including deterioration resulting from trade disputes or disagreements in foreign policy;
- political uncertainty or increasing strife among or within political parties in the Republic;
- hostilities or unrest involving oil producing countries in the Middle East and Northern Africa and any material disruption in the supply of oil or increase in the price of oil;
- the occurrence of severe earthquakes, tsunamis or other natural or man-made disasters in Korea and other parts of the world, particularly in trading partners; and
- an increase in the level of tension or an outbreak of hostilities between North Korea and the Republic or the United States.

Escalations in tensions with North Korea could have an adverse effect on us and the market value of the Notes.

Relations between Korea and North Korea have been tense throughout Korea's modern history. The level of tension between Korea and North Korea has fluctuated and may increase abruptly as a result of current and future events. In particular, there have been heightened security concerns in recent years stemming from North Korea's nuclear weapons and long-range missile programs as well as its hostile military and other actions against Korea. Some of the significant incidents in recent years include the following:

- North Korea renounced its obligations under the Nuclear Non-Proliferation Treaty in January 2003 and conducted three rounds of nuclear tests between October 2006 to February 2013, which increased tensions in the region and elicited strong objections worldwide. In January 2016, North Korea

announced that it had successfully tested a hydrogen bomb, its fourth nuclear test and allegedly first test using hydrogen, which is more explosive than plutonium. In February 2016, North Korea tested its intercontinental ballistic missile technology and launched a long-range missile, which it claimed to have launched a satellite into orbit. In response, the Government condemned the provocations and flagrant violations of relevant United Nations Security Council resolutions and withdrew Korean personnel from the inter-Korea Gaesong Industrial Complex and announced its closing. In March 2016, the United Nations Security Council unanimously passed a resolution condemning North Korea's actions and significantly expanding the scope of sanctions applicable to North Korea.

- In June 2016, North Korea test fired an intermediate-range ballistic missile and declared that it had the capability to strike U.S. interests in the Pacific and would continue to increase its “pre-emptive nuclear attack capability.” In response, the Government, along with the United Nations Security Council, strongly condemned the provocation and flagrant violations of relevant United Nations Security Council resolutions.
- In August 2015, two Korean soldiers were seriously wounded in landmine explosions while on routine patrol of the southern side of the demilitarized zone. The Government and the United Nations Command announced that the landmines were emplaced by North Korea, and in response, the Korean army restarted its loudspeaker propaganda broadcasts directed at the northern side of the demilitarized zone. The North Korean army retaliated by firing artillery rounds at the loudspeakers resulting in both sides being placed on the highest level of military readiness. High-ranking officials from the Government and North Korea subsequently met for discussions intending to diffuse military tensions and released a joint statement whereby, among other things, North Korea expressed regret over the landmine explosions that wounded the Korean soldiers.
- In March 2010, a Korean naval vessel was destroyed by an underwater explosion, killing many of the crewmen on board. The Government formally accused North Korea of causing the sinking, while North Korea denied responsibility. Moreover, in November 2010, North Korea fired more than one hundred artillery shells that hit Korea's Yeonpyeong Island near the Northern Limit Line, which acts as the de facto maritime boundary between Korea and North Korea on the west coast of the Korean peninsula, causing casualties and significant property damage. The Government condemned North Korea for the attack and vowed stern retaliation should there be further provocation.

North Korea's economy also faces severe challenges, which may aggravate social and political pressures within North Korea. There can be no assurance that the level of tensions affecting the Korean peninsula will not escalate in the future. Any further increase in tensions, which may occur, for example, if North Korea experiences a leadership crisis, high-level contacts between Korea and North Korea break down or military hostilities occur, could have a material adverse effect on the Korean economy and on our business, financial condition and results of operations and the market value of the Notes.

Risks Relating to SBC

An adverse change in the Government's credit rating would have an adverse effect on our credit rating.

We operate under the aegis of the SMBA of the MoTIE. Under Article 66-2 of the SME Promotion Act, the Government is obligated to replenish the SME Funds, which we are mandated to manage and from which we draw our operating capital, whenever there is a deficit. Accordingly, Moody's and Fitch have each rated us with the same credit rating given to the Republic as our credit is linked to the Government's sovereign credit. Consequently, an adverse change in Government's sovereign credit ratings would have an adverse effect on our ratings and trading price of the Notes.

Risks Relating to the Notes

The Government is not an obligor under the Notes; the Notes are not guaranteed by the Government.

Payment of our outstanding indebtedness is not backed by the full faith and credit of the Government. The Government is not an obligor under the Notes. In addition, payment of interest and principal of the Notes is not supported by a guarantee by the Government. While, under Article 66-2 of the SME Promotion Act, the Government is obligated to replenish the SME Fund when there is a deficit, there is no guarantee that the National Assembly may not repeal or amend this article in a manner which would prejudice the rights of the Noteholders in the future.

There is no existing trading market for the Notes and, therefore, the Notes offer limited liquidity.

The Notes constitute a new issue of securities for which there is no existing trading market. Although the Managers have advised us that they currently intend to make a market in the Notes, they are not obligated to do so, and any market-making activity with respect to the Notes, if commenced, may be discontinued at any time without notice.

There can be no assurance that a market for the Notes will develop in the future. If such a market were to develop, the Notes could trade at prices that may be higher or lower than the offering price depending on many factors, including, among others:

- prevailing interest rates;
- our financial condition, performance and prospects;
- the rate of exchange between the Won and the Dollar;
- political and economic developments in Korea; and
- the market conditions for similar securities.

USE OF PROCEEDS

We expect to use the net proceeds from the sale of the Notes of approximately US\$493,555,000, after deduction of commissions to the Managers but before expenses incurred in connection with the issue of the Notes, for general corporate purposes, including repayment of existing obligations under the account of the SME Fund.

SMALL AND MEDIUM BUSINESS CORPORATION

Overview

We are a statutory juridical entity established in 1979 pursuant to the SME Promotion Act, to contribute to the development of the national economy by supporting and assisting small- and medium-sized enterprises in Korea. We are one of the few special statutory entities in Korea established with no paid-in capital and operate under the aegis of the SMBA of the MoTIE.

We are capitalized by the SME Fund, which was established under the SME Promotion Act to secure financial resources necessary for promoting SMEs and building Korea's industrial infrastructure. We play a central role in implementing the Government's policy to assist and support SMEs by administering the SME Fund and providing policy financing to SMEs as well as non-financial and other assistance to SMEs. Proceeds from any debt securities issued by us, including the Notes covered by this Offering Circular, will be credited to the SME Fund, and payments on such debt securities will be made from the SME Fund. The Government's capital contributions and loans are the primary sources of capital for the SME Fund.

The policy financing that we provide to SMEs is meant to supplement commercial loans and is provided at below-market interest rates. Under Article 66-2 of the SME Promotion Act, any annual net profit from the administration of the SME Fund is to be returned to the SME Fund, and the Government is obligated to replenish the SME Fund when there is a deficit. As a result of Article 66-2 of the SME Promotion Act, the Government is generally responsible for our operations and is legally obligated to replenish any deficit that arises if the SME Fund is insufficient to cover any of our annual net losses. In light of the above, if we have insufficient funds to make any payment under any of our obligations, including the Notes covered by this Offering Circular, the Government would take appropriate steps, such as by making a capital contribution, by allocating funds or by taking other action, to enable us to make such payment when due. The provisions of Article 66-2 do not, however, constitute a direct guarantee by the Government of our obligations, and the provisions of the SME Promotion Act, including Article 66-2, may be amended at any time by action of the National Assembly.

The Government closely supervises our operations and appoints members of our Board of Directors (except for our standing Directors, who are appointed by our President), our Statutory Auditor and Steering Committee, which handle our day-to-day operations, from various Government ministries. The SMBA, the Ministry of Strategy and Finance (the "MoSF") and the National Assembly approve our budget and operation plan for the SME Fund.

Capitalization

As of December 31, 2015, the capitalization of the SME Fund was as follows:

	<u>As of December 31, 2015⁽¹⁾</u> <u>(in billions of Won)</u>
Long-term debt:	
Long-term borrowings	₩ 4
Debentures (net of present value discounts)	10,362
Total long-term liabilities	<u>10,366</u>
Equity:	
Capital contributions	2,726
Capital surplus	5
Accumulated other comprehensive income	80
Accumulated deficit	<u>(1,149)</u>
Total equity	<u>1,663</u>
Total capitalization	<u>₩12,029</u>

Note:

(1) Except as disclosed in this Offering Circular, there has been no material change in our capitalization since December 31, 2015.

Purpose and Authority

We were established in 1979 as a statutory juridical entity pursuant to the SME Promotion Act. The Government empowered us to perform a central role in fostering the growth of SMEs and implementing the Government's SME-related policies. The SME Promotion Act, the related enforcement decree and our Articles of Incorporation define and regulate our powers and authority. As stated in the SME Promotion Act and our Articles of Incorporation, our purpose is to promote SMEs in order to contribute to the development of the national economy. As an instrument in serving the Government's public policy objectives with respect to SMEs, we do not seek to maximize our profits.

The SME Promotion Act contemplates that we will engage in the following activities:

- support SMEs through financial and other assistance programs;
- support SME startups;
- manage the SME Fund;
- conduct business incidental to the foregoing; and
- engage in any other activities entrusted to us for the purpose of promotion of the SMEs by the SMBA.

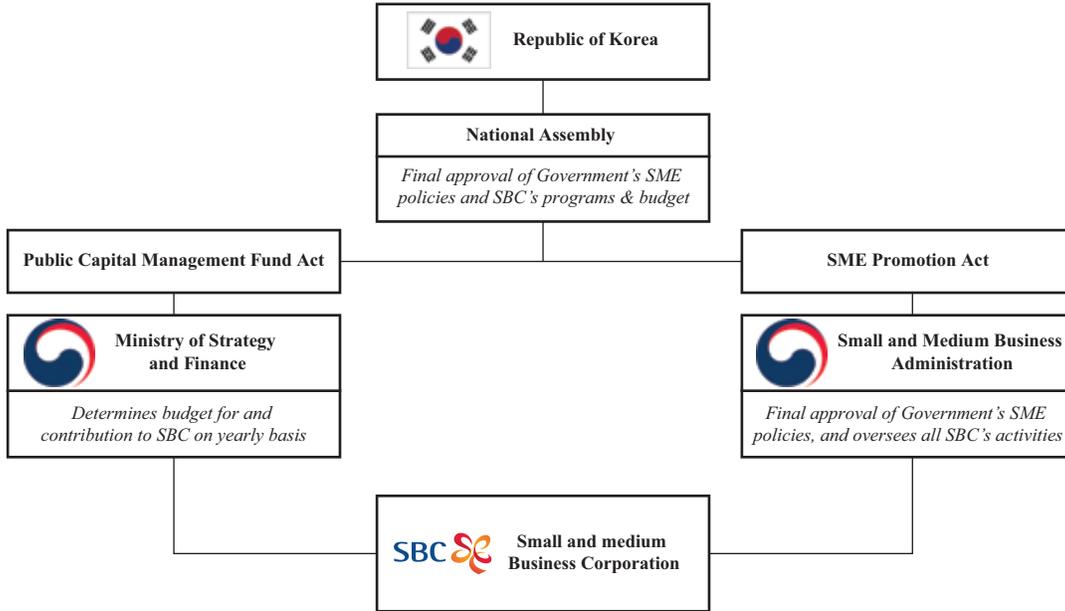
Government Supervision and Support

We are under the direct supervision of the SMBA and our policies and operations are subject to review and supervision by the Government. The Government closely supervises our operations and has power to appoint or dismiss our President and Chief Executive Officer, members of our Board of Directors (except for our standing Directors, who are appointed by our President), our Statutory Auditor and Steering Committee, which handle our day-to-day operations, from various Government ministries and instrumentalities.

The Government's capital contributions and loans are the primary sources of capital for the SME Fund. Under the Public Capital Management Fund Act and the SME Promotion Act, the amount of capital contributions and loans to be made to the SME Fund by the Government is required to be appropriated within the Government's national budget on an annual basis. Such capital contributions and loans are determined based on the SME Fund's budget plan prepared by us, and subsequently approved by the SMBA and the MoSF. Once approved by the SMBA and the MoSF, the budget plan for the SME Fund is then incorporated into the Government's annual national budget together with other Government funds and submitted to the National Assembly for final approval. Upon the National Assembly's final approval of the Government's annual budget, the approved amount of loans from the Government's special account is drawn down to the SME Fund. In addition, the Government may provide capital contributions to the SME Fund pursuant to the Government's national budget (approved by the National Assembly) as needed for us to carry out our policy functions and to repay our obligations as they become due.

Under Article 66-2 of the SME Promotion Act, any annual net profit from the administration of the SME Fund is to be returned to the SME Fund, and the Government is obligated to replenish the SME Fund when there is a deficit. As a result of Article 66-2 of the SME Promotion Act, the Government is generally responsible for our operations and is legally obligated to replenish any deficit that arises if the SME Fund is insufficient to cover any of our annual net losses. In light of the above, if we have insufficient funds to make any payment under any of our obligations, including the Notes covered by this Offering Circular, the Government would take appropriate steps, such as by making a capital contribution, by allocating funds or by taking other action, to enable us to make such payment when due. The provisions of Article 66-2 do not, however, constitute a direct guarantee by the Government of our obligations, and the provisions of the SME Promotion Act, including Article 66-2, may be amended at any time by action of the National Assembly.

The following diagram illustrates the relationship and cooperation between us and related Government ministries and instrumentalities:



Selected Financial Data

The following tables set forth selected financial information of the SME Fund, which have been derived from its audited financial statements and related notes for each of the years ended December 31, 2014 and 2015 included elsewhere in this Offering Circular.

Balance Sheet Data

	As of December 31,	
	2014	2015
	(in billions of Won)	
Total loans ⁽¹⁾⁽²⁾	₩14,858	₩14,226
Total borrowings (net of present value discounts) ⁽³⁾	14,797	14,123
Total assets	16,386	15,981
Total liabilities	14,946	14,317
Total equity	1,440	1,663

Notes:

- (1) Gross amount, which includes short-term loans and long-term loans without deducting allowance for doubtful accounts of ₩518 billion and ₩647 billion as of December 31, 2014 and 2015, respectively.
- (2) Excludes long-term loans to employees.
- (3) Includes current portion of debt, long-term borrowings and debentures.

As of December 31, 2015, the SME Fund's total assets decreased to ₩15,981 billion from ₩16,386 billion as of December 31, 2014, primarily due to a decrease in long-term loans to ₩11,200 billion as of December 31, 2015 from ₩12,032 billion as of December 31, 2014, which was partially offset by an increase in short-term loans to ₩3,026 billion as of December 31, 2015 from ₩2,826 billion as of December 31, 2014 and an increase in cash and cash equivalents to ₩234 billion as of December 31, 2015 from ₩118 billion as of December 31, 2014.

As of December 31, 2015, the SME Fund's total liabilities decreased to ₩14,317 billion from ₩14,946 billion as of December 31, 2014, primarily due to a decrease in current portion of debt (net of present value discounts) to ₩3,757 billion as of December 31, 2015 from ₩3,255 billion as of December 31, 2014.

As of December 31, 2015, the SME Fund's total equity increased to ₩1,663 billion from ₩1,440 billion as of December 31, 2014, primarily due to an increase in capital contribution by the Government to ₩2,726 billion as of December 31, 2015 from ₩2,538 billion as of December 31, 2014.

Income Statement Data

	For the year ended December 31,	
	2014	2015
	(in billions of Won)	
Operating revenues	₩962	₩907
Operating expenses	973	969
Other income	24	68
Income before income taxes	12	6
Income tax benefit	11	6
Net Income	23	12

The SME Fund had net income of ₩12 billion in 2015 compared to net income of ₩23 billion in 2014. The principal factor for the decrease in net income in 2015 compared to 2014 was a decrease in net business income from the Venture Business Startup Loan Program to ₩35 billion in 2015 from ₩95 billion in 2014, primarily due to a decrease in interest income resulting from a decrease in the amount of outstanding loans extended to newly created SMEs. This factor was partially offset by an increase in net gain on disposal of property and equipment to ₩47 billion in 2015 from ₩2 billion in 2014, primarily due to the disposal of our land and building in 2015.

Business and Operations

We offer financial and non-financial support and assistance to SMEs in Korea. In order to qualify as an SME, the average sales of the last three years, the average sales of the last two years, or annual sales, as applicable, for each primary area of business conducted by the relevant enterprise must not exceed the designated threshold (from ₩40 billion to ₩150 billion) and the total assets of the enterprise on its balance sheet at the end of the immediately preceding fiscal year must be less than ₩500 billion. The following table summarizes the criteria used in defining SMEs under the Framework Act on Small and Medium Enterprises:

<u>Type of Business</u>	<u>Average or Annual Revenue</u>
Manufacture of Electrical Devices	₩150 billion or less
Agriculture, Forestry and Fishing	₩100 billion or less
Construction	₩100 billion or less
Retail and Wholesale	₩100 billion or less
Transportation	₩80 billion or less
Professional, Science and Technical Services	₩60 billion or less
Lodging and Food Services	₩40 billion or less
Others	varies

In addition, in order to qualify as an SME, the ownership and management of an enterprise must satisfy the "substantial independence" requirement. For example, a company that falls under the following criteria, among others, is deemed not to satisfy the "substantial independence" requirement: (i) a company (the "first company") in which another company, whose total assets on its balance sheet at the end of the immediately preceding fiscal

year amount to ₩500 billion or more, owns 30% or more of total voting shares issued by the first company or (ii) a company that belongs to a business group that is restricted from cross-holding of shares of companies within the group under the Monopoly Regulation and Fair Trade Act.

Financial Assistance

Our primary function is providing financial assistance to SMEs. Through our management of the SME Fund, we provide long-term loans to SMEs either directly or indirectly through banks or other financial institutions in Korea under various loan programs. These loans are required to be used by the SME borrowers for the purpose of enhancing their productivity and facilitating business innovation.

Loan Programs

We provide financial assistance to SMEs through several loan programs operated with funds from the SME Fund. The following table sets forth the aggregate amount of loans granted to SMEs for loan programs for the years ended December 31, 2014 and 2015.

	For the year ended December 31,	
	2014	2015
	(in billions of Won)	
Venture Business Startup Loan	₩1,290	₩1,500
New Growth Industry Loan	865	1,127
Emergency Stabilization Loan	155	613
Technology Commercialization Loan	350	350
Structural Adjustment Loan	170	212
Small Business Loan ⁽¹⁾	290	—
Investment and Loan Hybrid Financing Loan	150	100
Total	<u>₩3,270</u>	<u>₩3,902</u>

Note:

(1) This loan program was transferred to the Small Enterprise and Market Service in 2015 and is no longer offered by us.

The following table sets forth the aggregate amount of loans outstanding for each of the loan programs as of December 31, 2015:

	Amount outstanding	Percentage of total loans outstanding
	(in billions of Won, except percentages)	
Venture Business Startup Loan	₩ 5,112	36%
New Growth Industry Loan	3,960	28
Emergency Stabilization Loan	708	5
Technology Commercialization Loan	1,197	8
Structural Adjustment Loan	764	5
Small Business Loan ⁽¹⁾	2,014	14
Investment and Loan Hybrid Financing Loan	471	3
Total	<u>₩14,226</u>	<u>100%</u>

Note:

(1) This loan program was transferred to the Small Enterprise and Market Service in 2015 and is no longer offered by us.

Venture Business Startup Loan Program provides financing to newly created SMEs in need of new equipment, machinery, real estate or operating capital during their startup and initial growth stages. In 2015, loans issued under this program had interest rates of between 0% and 6.18% and maturities of eight years or less. Loans granted through this program amounted to ₩1,290 billion in 2015, an increase from ₩1,340 billion in 2014.

New Growth Industry Loan Program provides financing to SMEs with valuable technology and significant growth potential requiring machinery, equipment or real estate for business expansion or modernization. In 2015, loans issued under this program had interest rates of between 1.00% and 5.90% and maturities of 15 years or less. Loans granted through this program amounted to ₩1,127 billion in 2015, an increase from ₩865 billion in 2014.

Emergency Stabilization Loan Program provides financing to SMEs facing temporary or unforeseen difficulties. The loans are meant to provide operating capital to stabilize management and, for SME manufacturers, production. In 2015, loans issued under this program had interest rates of between 1.00% and 8.18% and maturities of five years or less. Loans granted through this program amounted to ₩613 billion in 2015, an increase from ₩155 billion in 2014.

Technology Commercialization Loan Program provides financing to SMEs preparing to commercialize their intellectual property, such as patents, resulting from research and development projects sponsored by the Government or other academic or industrial institutes. In 2015, loans issued under this program had interest rates of between 1.00% and 6.28% and maturities of eight years or less. Loans granted through this program amounted to ₩350 billion in 2015, which was the same amount granted in 2014.

Structural Adjustment Loan Program provides financing for machinery, equipment, real estate and operating capital to SMEs preparing to restructure or change their business. In 2015, loans issued under this program had interest rates of between 1.00% and 6.33% and maturities of eight years or less. Loans granted through this program amounted to ₩212 billion in 2015, an increase from ₩170 billion in 2014.

Small Business Loan Program provides financing for various operational expenses, such as construction costs, lease deposits and purchases of raw materials, to SMEs with less than 10 employees. In 2015, loans issued under this program had interest rates of between 0.0% and 3.79% and maturities of eight years or less. This loan program, however, was transferred to the Small Enterprise and Market Service in 2015 and is no longer offered by us. We are currently engaged in this loan program only to the extent of collection of previously granted loans. Accordingly, there were no loans granted by us through this program in 2015, compared to ₩290 billion granted by us in 2014.

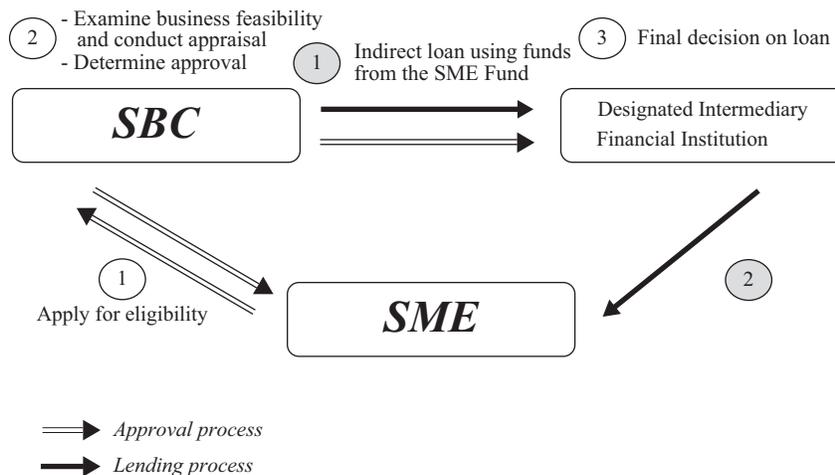
Investment and Loan Hybrid Financing Loan Program offers two types of loans to SMEs with valuable technology and significant growth potential: (i) Income Sharing Loan and (ii) Growth Sharing Loan. Under the Income Sharing Loan, the interest rate is the sum of a fixed interest rate and a rate based on the SME's sale performance. Under the Growth Sharing Loan, we purchase convertible bonds from the SME and provide loans to the SME at a low interest rate. In 2015, loans issued under this program had interest rates of between 0.64% and 4.00% and maturities of seven years or less. Loans granted through this program amounted to ₩100 billion in 2015, a decrease from ₩150 billion in 2014.

Loan Types and Loan Approval

Indirect loans are extended to SMEs through designated intermediary financial institutions. We explicitly set detailed guidelines (including scope of borrowers, maturity and interest rates) for designated intermediary financial institutions to be followed when on-lending to the ultimate borrowers. We monitor our exposure to, and the credit standing of, each financial institution to which we lend. While a loan application is subject to business feasibility and credit review by both us, as manager of the SME Fund, and the designated intermediary financial

institution, the final decision to approve the “indirect” loan is made by the designated intermediary financial institution. In the case of “indirect” loans, it is the designated intermediary financial institution that assumes the full credit risk of the loan. We expressly set interest rates for the designated intermediary financial institution to be followed when on-lending to ultimate borrowers. As of December 31, 2014 and 2015, indirect loans accounted for 51% and 41% of the SME Fund’s total assets, respectively.

The following diagram summarizes the indirect loan process:



Direct loans are extended to SMEs directly by us from the SME Fund, which retains the credit risk. Direct loans carry interest rates that are lower than the average market interest rate for loans to SMEs. As of December 31, 2014 and 2015, direct loans accounted for 39% and 48% of the SME Fund’s total assets, respectively.

The following table sets forth the amount of indirect and direct loans to SMEs as of December 31, 2014 and 2015.

	As of December 31,			
	2014		2015	
	(in billions of Won, except percentages)			
Indirect Loans	₩ 8,397	57%	₩ 6,628	47%
Direct Loans ⁽¹⁾	6,461	43	7,597	53
Total Loans ⁽¹⁾⁽²⁾	₩14,858	100	₩14,226	100

Notes:

- (1) Gross amount without deducting allowance for doubtful accounts.
- (2) Excludes long-term loans to employees.

We developed our own loan approval policies for the SME Fund based on our lending experience and expertise with SMEs. These loan approval policies are established following approval by our Board of Directors. This loan evaluation model takes into account a wide range of financial and non-financial data of SMEs in Korea, with periodic updates to its rating criteria and rating samples. This loan evaluation model comprises four sub-models for five different business segments. We maintain a diversified loan portfolio in order to limit our exposure to particular borrowers and industries. Under our current internal policies and procedures, we are not permitted to extend credit in excess of ₩5 billion to any single borrower, subject to certain exceptions.

All SMEs applying for a “direct” or “indirect” loan are subject to preliminary screening based on their debt-to-equity ratio and history of past delinquencies as well as tax return history. For example, any SME

applicant with a debt-to-equity ratio higher than the basic standard set by us is automatically disqualified. An applicant that passes the preliminary screening is then subject to assessment, which includes evaluation of the applicant's technological capabilities, competitive position in its industry, operating and funding capabilities and the quality of its management, financial prospects and credit rating. In light of our public function of providing assistance and support to SMEs, our loan evaluation model is designed to evaluate the applicant's long-term potential rather than short-term performance and profitability, with emphasis placed on the applicant's business viability.

Non-financial Assistance

We offer various forms of non-financial assistance and services to SMEs, which can be classified into the following three areas.

Marketing and Global Cooperation Services

We offer various resources to help SMEs with marketing and aid their entry into the global market, including: (i) operating "GobizKorea," an online trade portal site (kr.gobizkorea.com), to connect SMEs with potential foreign buyers; (ii) selecting SMEs with high export growth potential and providing them with preferential government support in research and development, marketing and export financing; (iii) operating a number of Business Incubators, which are business centers located in major export market countries providing office space as well as marketing, law, tax and accounting consulting services to SMEs, and offering a network of private consultants providing additional consulting, marketing and technical services to help SMEs establish themselves in such export markets; (iv) promoting information exchange and technology cooperation and organizing international conferences and workshops; and (v) providing marketing assistance to new SME startups.

Human Resources Development

We operate the Small Business Training Institute, which offers management, policy, administrative, training and technology related courses to SME employees through a number of regional institutes. We also offer specialized training programs for young entrepreneurs through our Youth Startup Academy.

Corporate Diagnosis and Technical Assistance

We provide comprehensive consulting services to SMEs in areas such as finance, marketing, employee training, production, technology, information and international cooperation. Under our SME Corporate Diagnosis program, our consultants make on-site visits to SMEs to diagnose problems and consult with the management to devise an action plan to enhance their competitiveness.

Description of Assets and Liabilities

Loan Concentration by Industry

The following table shows, as of the dates indicated, the aggregate balances of the SME Fund's direct loans in Won by industry concentration:

<u>Industry</u>	As of December 31,			
	2014		2015	
	Aggregate loan balance	Percentage of loan balance	Aggregate loan balance	Percentage of loan balance
	(in billions of Won, except percentages)			
Metal	₩1,124	17%	₩1,318	17%
Machinery	1,304	20	1,430	19

Industry	As of December 31,			
	2014		2015	
	Aggregate loan balance	Percentage of loan balance	Aggregate loan balance	Percentage of loan balance
	(in billions of Won, except percentages)			
Textile	270	4	296	4
Food	470	7	551	7
Distribution	749	12	1,088	14
Miscellaneous Goods	547	8	638	8
Electric	307	5	341	4
Electronic	330	5	347	5
Information Technology	248	4	259	3
Chemical Engineering	738	11	818	11
Others	374	6	511	7
Total	<u>₩6,461</u>	<u>100%</u>	<u>₩7,597</u>	<u>100%</u>

Loan Concentration by Size of Loans

The following table shows, as of December 31, 2015, the aggregate balances of the SME Fund's direct loans in Won by outstanding loan amount:

	As of December 31, 2015	
	Aggregate loan balance	Percentage of sub-total loan balance
	(in billions of Won except percentages)	
Up to ₩500 million	₩5,951	78%
Over ₩500 million to ₩1 billion	713	9
Over ₩1 billion to ₩5 billion	928	12
Over ₩5 billion	5	0
Total	<u>₩7,597</u>	<u>100%</u>

Loan Concentration by Borrower

The following table shows the SME Fund's 20 largest borrowers, including financial institutions in connection with the indirect loan process, in terms of outstanding loans as of December 31, 2015.

	As of December 31, 2015 (in billions of Won)
Industrial Bank of Korea	₩2,853
Kookmin Bank	584
Woori Bank	502
Shinhan Bank	417
Kyongnam Bank	410
National Agricultural Cooperative Federation	402
Daegu Bank	389
Busan Bank	331
KEB Hana Bank	219
Kwangju Bank	186
Korea Development Bank	177
Jeonbuk Bank	71
Korean Federation of Community Credit Cooperatives	35
Standard Chartered Korea	15

	<u>As of</u> <u>December 31, 2015</u> <u>(in billions of Won)</u>
National Federation of Fisheries Cooperatives	11
Jeju Bank	11
National Credit Union Federation of Korea	7
Kangil Pharm (medicine distributor)	6
Citi Bank	6
Inteko (chemical engineering company)	5
Total	<u>₩6,637</u>

Asset Quality

The Supervisory Regulation of Banking Business legislated by the Financial Services Commission (the “FSC”) requires banks to analyze and classify their credits into one of five categories—normal, precautionary, substandard, doubtful or estimated loss—by taking into account borrowers’ repayment capacity as well as a number of other factors including the financial position, profitability and transaction history of the relevant borrower, as well as the value of any collateral or guarantee taken as security for the extension of credit. While the SME Fund is not subject to this requirement, we apply these standards on a voluntary basis to our direct loans from the SME Fund, with certain modifications as we deem necessary and appropriate in each of the loan quality categories. The following is a summary of the loan classification criteria we apply based on the asset classification guidelines of the FSC, although such FSC guidelines are not required to be applied to loans from the SME Fund.

- Normal** Credits extended to customers which, in consideration of their business and operations, financial conditions and future cash flows, do not raise concerns regarding their ability to repay the credits.
- Precautionary** . . . Credits extended to customers, which are (1) in consideration of their business and operations, financial condition and future cash flows, judged to have potential risks with respect to their ability to repay the credits in the future, although there have not occurred any immediate risks of default in repayment; or (2) in arrears for one month or more but less than three months.
- Substandard** (1) Credits extended to customers, which in consideration of their business and operations, financial conditions and future cash flows, are judged to have incurred considerable risks for default in repayment as the customers’ ability to repay has deteriorated; or (2) that portion which is expected to be collected of total credits (a) extended to customers which have been in arrears for three months or more, (b) extended to customers which are judged to have incurred serious risks due to the occurrence of final refusal to pay their promissory notes, liquidation or bankruptcy proceedings, or closure of their businesses or (c) of “Doubtful Customers” or “Estimated-loss Customers” (each as defined below).
- Doubtful** That portion of credits in excess of the amount expected to be collected of total credits extended to (1) customers (“Doubtful Customers”) which, in consideration of their business and operations, financial conditions and future cash flows, are judged to have incurred serious risks of default in repayment due to noticeable deterioration in their ability to repay; or (2) customers which have been in arrears for three months or more but less than twelve months.
- Estimated Loss** . . . That portion of credits in excess of the amount expected to be collected of total credits extended to (1) customers (“Estimated-loss Customers”), which, in consideration of their business and operations, financial condition and future cash flows, are judged to have to be accounted as a loss as the inability to repay became certain due to serious deterioration in

their ability to repay; (2) customers which have been in arrears for twelve months or more; or (3) customers which are judged to have incurred serious risks of default in repayment due to the occurrence of final refusal to pay their promissory notes, liquidation or bankruptcy proceedings, or closure of their businesses.

Asset Classification

The following table shows, as of the dates indicated, information on the SME Fund's allowance for direct loan losses:

	As of December 31, 2014		As of December 31, 2015	
	Direct Loan Amount ⁽¹⁾	Direct Loan Loss Reserve	Direct Loan Amount ⁽¹⁾	Direct Loan Loss Reserve
	(in billions of Won)			
Normal	₩5,659	₩ 49	₩6,489	₩ 56
Precautionary	220	15	290	20
Substandard	76	15	157	31
Doubtful	73	33	243	121
Estimated Loss	433	405	418	418
Total	<u>₩6,461</u>	<u>₩518</u>	<u>₩7,597</u>	<u>₩647</u>

Note:

(1) Includes present value discounts.

Non-Performing Loans

Non-performing loans are defined as those loans that are classified as substandard or below based on the FSC's asset classification criteria. The following table shows, as of the dates indicated, certain details regarding the asset quality of the SME Fund's direct loans (net of present value discounts):

	As of December 31,	
	2014	2015
	(in billions of Won, except percentages)	
Direct loans	6,461	7,597
Total non-performing direct loans	582	818
Non-performing direct loans as a percentage of total direct loans	9%	11%
Precautionary and non-performing direct loans	802	1,108
Precautionary and non-performing direct loans as a percentage of total direct loans	12%	15%
Allowance for direct loan losses	518	647
Allowance for direct loan losses as a percentage of non-performing direct loans	89%	79%
Allowance for direct loan losses as a percentage of total direct loans	8%	9%

Loan Loss Provisioning Policy

The SME Fund has established an allowance for loan losses, which is available to absorb losses that it incurs in its direct loan portfolio. This allowance is based on the SME Fund's classification of the loans in its portfolio as of the balance sheet date, under the asset classification criteria of the FSC. If additions or changes to the allowance for loan losses are required, then the SME Fund records provisions for loan losses, which are treated as charges against current income. Loan exposures of the SME Fund that we deem to be uncollectible, including actual loan losses, net of recoveries of previously charged-off amounts, are charged directly against the allowance for loan losses. We do not establish allowances for loan losses on indirect loans from the SME Fund as neither we nor the SME Fund we manage assumes credit risks on such loans.

Loans are classified as of the balance sheet dates as normal, precautionary, substandard, doubtful or estimated loss. The allowance for loan losses is established based on the classification of the loans, using the following percentages prescribed by the FSC.

Loan classifications

Normal	0.9% or above
Precautionary	7% or above
Substandard	20% or above
Doubtful	50% or above
Estimated loss	100%

Non-Performing Loan Strategy

When a direct loan from the SME Fund becomes non-performing, we begin a due diligence review of the borrower’s assets, send a notice demanding payment or stating that we will take legal action, and prepare for legal action. At the same time, we initiate our non-performing loan management process, which begins with:

- identifying loans subject to charge-off based on the estimated recovery value of collateral, if any, for such non-performing loans and the estimated rate of recovery of unsecured loans; and
- identifying loans subject to normalization efforts based on the cash-flow situation of the borrower, which includes deferral of interest and principal repayments.

Once we have confirmed the details of a non-performing loan in the SME Fund, we make efforts to recover amounts owed to us for the account of the SME Fund. Methods for resolving non-performing loans include the following:

- commencing collection proceedings;
- commencing legal actions to seize collateral; and
- writing off these amounts and recovering what we can with respect to these amounts.

Under current laws and regulations, we are not allowed to sell loans from the SME Fund to a third party until after such loans have been charged off.

Loan Charge-offs. Our credit approval process includes assessing credit risk before extending loans and monitoring outstanding loans, in order to minimize loans that must be charged off. To the extent charge-offs are required, the SME Fund follows charge-off policies aimed at maximizing accounting transparency, minimizing any waste of resources in managing loans which have a low probability of being collected and reducing our non-performing loan ratio.

Loans To Be Charged Off. Loans from the SME Fund are charged off when they are deemed to be uncollectible by virtue of their falling under any of the following categories:

- loans for which collection is not foreseeable due to insolvency, bankruptcy, compulsory execution, disorganization, dissolution or the shutting down of the business of the debtor;
- loans for which collection is not foreseeable due to the death or disappearance of the debtor;
- loans for which expenses of collection exceed the collectible amount;
- loans on which collection is not possible through legal or any other means; or
- the portion of loans classified as “estimated loss,” net of any recovery from collateral, which is deemed to be uncollectible.

Procedure for Charge-off Approval. Loans from the SME Fund are typically charged off when classified as estimated loss on a semi-annual basis. In order to charge off a loan, our Risk Management Committee determines the amounts of loans to be charged off, which amounts are also reviewed by our Statutory Auditor. The list of loan charge-off amounts is then submitted to our President for final internal approval.

Treatment of Charge-offs. Once loans are charged off, they are classified as charged-off loans, and the collection of these loans is outsourced to loan collection agencies, such as the Korea Asset Management Corporation.

Liquidity and Capital Resources

The following table sets forth the sources and uses of the SME Fund for the years ended December 31, 2014 and 2015:

	For the year ended December 31,	
	2014	2015
	(in billions of Won)	
Sources:		
Bonds	₩2,990	₩2,600
Collection on loans	4,133	4,317
Government contribution	999	641
Income	459	515
Others	132	22
Total sources	<u>₩8,713</u>	<u>₩8,094</u>
Uses:		
Payments on bonds and borrowings	₩3,364	₩3,258
Extension of loans	4,036	3,889
Expenses	696	632
Others	617	315
Total uses	<u>₩8,713</u>	<u>₩8,094</u>

Sources of Liquidity of the SME Fund

We raise capital for the SME Fund primarily through the issuances of bonds and capital contributions from the Government. The primary sources of the SME Fund have been loan repayments from SMEs, which accounted for 47% and 53% of the total funds raised for the years ended December 31, 2014 and 2015, respectively, and the issuance of bonds, which accounted for 34% and 32% of the total funds raised for the years ended December 31, 2014 and 2015, respectively.

Bonds. In 2014, we raised approximately ₩3 trillion through a total of 36 issuances of bonds. In 2015, we raised approximately ₩3 trillion through a total of 30 issuances of bonds. The amount of bonds issued is determined annually by the Government. The bonds have maturities of two to 15 years from the issue date, and most have a maturity of three years or longer.

The following tables show the breakdown of the bonds issued in 2014 and 2015 by interest type and maturity.

	Fixed rate	Floating rate	Total
	(in billions of Won)		
Bonds by Interest Type ⁽¹⁾:			
2014	₩2,940	₩ 50	₩2,990
2015	2,460	140	2,600
Total	<u>₩5,400</u>	<u>₩190</u>	<u>₩5,590</u>

	<u>2 years</u>	<u>3 years</u>	<u>5 years</u>	<u>8 years</u>	<u>10 years</u>	<u>15 years</u>	<u>Total</u>
	(in billions of Won)						
Bonds by Maturity ⁽¹⁾:							
2014	₩170	₩ 910	₩1,590	₩ 0	₩270	₩ 50	₩2,990
2015	60	790	1,120	260	50	320	2,600
Total	<u>₩230</u>	<u>₩1,700</u>	<u>₩2,710</u>	<u>₩260</u>	<u>₩320</u>	<u>₩370</u>	<u>₩5,590</u>

Note:

(1) Excludes discounts on bonds and losses on interest rate swaps.

Government Contribution. The Government makes capital contributions to the SME Fund. In addition, we may borrow from the Government's special account without pledging collateral or any payment guarantee. The loans have floating interest rates which are adjusted every three months. Both the capital contributions and loans are determined by the SMBA and the MoSF in the Government's annual budget, which is finalized upon the approval of the National Assembly.

The following table presents the Government's capital contributions and loans for the periods and as of the dates indicated. No borrowings from the Government have been made since 2008.

	<u>For the year ended December 31, 2014</u>	<u>As of December 31, 2014</u>	<u>For the year ended December 31, 2015</u>	<u>As of December 31, 2015</u>
	(in billions of Won)			
Capital Contribution	₩107	₩2,538	₩189	₩2,726
Loans	0	16	0	8
Total	<u>₩107</u>	<u>₩2,554</u>	<u>₩189</u>	<u>₩2,734</u>

Uses of the SME Fund

We use capital available in the SME Fund to administer various programs providing support to SMEs. The following tables show the amount of loans provided from the SME Fund to each industrial sector and the number of SMEs to which we provided financial assistance in each industrial sector for the year ended December 31, 2015.

<u>Industry</u>	<u>For the year ended December 31, 2015</u>	
	<u>Amount</u>	<u>Number of SMEs</u>
	(in billions of Won, except number of SMEs)	
Metal	₩ 681	2,841
Machinery	733	2,740
Textile	133	616
Food	234	1,050
Distribution	675	3,692
Miscellaneous Goods	300	1,399
Electric	169	770
Electronic	138	704
Information Technology	101	764
Chemical Engineering	425	1,568
Others	313	1,652
Total	<u>₩3,902</u>	<u>17,796</u>

Organization and Structure

We are managed by our Steering Committee, which reviews and advises on our policies, and the Board of Directors, our highest executive and decision-making body.

Steering Committee

The Steering Committee is our principal governing body, and it reviews and advises on our policies. Under the SME Promotion Act, the Steering Committee consists of our President, who acts as Chairman of the Steering Committee, and up to 20 members who include a person designated by each of the MoSF, the MoTIE and the SMBA from among its respective high ranking officers. Currently, it comprises the following 12 members:

- President of SBC, who serves as the Chairman of the Steering Committee;
- a Director General of the MoSF;
- a Director General of the MoTIE;
- a Director General of the SMBA;
- Vice Chairman of the Korea Federation of Small and Medium Business; and
- seven members commissioned by the Administrator of the SMBA.

Under the SME Promotion Act and our Articles of Incorporation, the Steering Committee is empowered to review (i) items relating to our budget and (ii) other items as determined by the Chairman of the Steering Committee.

The following table provides certain information about the 12 members of the Steering Committee as of the date of this Offering Circular.

<u>Name</u>	<u>Age</u>	<u>Position held</u>
Chae-Un Lim	60	President of SBC
Gyu-Hong Cho	50	Director General for the MoSF
Sung-Cheon Kang	53	Director General for the MoTIE
Un-Man Baek	49	Director General for the SMBA
Jae-Hee Song	61	Vice Chairman of the Korean Federation of Small and Medium Business
Dae-Ho Song	53	Advisory Committee Member of the MoTIE
Hyeon-Bong Yang	57	Lead Research Analyst, Korea Institute for Industrial Economics & Trade
Young Lee	48	Chairman, Korea Venture Business Women's Association
Won-Hee Lee	61	Professor, Hanyang University
Yun-Jae Lee	61	Professor, Soongsil University
Byung-Hong Hwang	58	Senior Managing Director, Korea Credit Guarantee Fund
Won-Hae Lee	61	Chief Executive Officer, Daemo Engineering Corporation

Board of Directors and Statutory Auditor

The Board of Directors is our highest executive body. It comprises the President, Vice-President and the Directors of SBC. The President of Korea appoints or dismisses our President upon the nomination by the Administrator of the SMBA. Our President appoints or dismisses our Vice-President and standing Directors. The Administrator of the SMBA appoints or dismisses our non-standing Directors. The President of Korea appoints or dismisses our Statutory Auditor upon the nomination by the Minister of the MoSF. The Statutory Auditor can attend board meetings as an observer to give opinions without the right to vote. According to our Articles of Incorporation, the term of office for our President is three years and the term of office for our Directors and Statutory Auditor is two years.

The Board of Directors makes decisions on the following issues:

- items to be reviewed and decided by the Steering Committee;
- issuance of bonds by the SME Fund;
- operational regulations; and
- other important issues.

The following table provides certain information about the current members of the Board of Directors as of the date of this Offering Circular.

<u>Name</u>	<u>Age</u>	<u>Year appointed</u>	<u>Position held</u>
Chae-Un Lim	60	2015	President
Young-Ae Lee	66	2014	Chief Audit Executive
Deuk-Moon Lim	58	2014	Senior Vice President and Head of Planning Division
Jin-Su Jeong	58	2015	Vice President of Administrative Support Division
Bung-Geol Ryu	58	2015	Vice President of Business Financing Division
Yong-Seung Lee	59	2016	Vice President of Global Marketing Division
Nae-Kwon Cho	57	2016	Vice President of Human Resources and Technology Support Division
Han-Cheol Lee	58	2015	Vice President of Regional Head Office
Suk-Song Oh	63	2014	Non-Standing Director
Dong-Man Kim	53	2014	Non-Standing Director
Moo-Kyung Han	59	2014	Non-Standing Director
Mi-Yeon Heo	55	2014	Non-Standing Director
Chun-Wu Lee	51	2014	Non-Standing Director
In-Tae Jeong	56	2015	Non-Standing Director
Young-Sam Cho	55	2016	Non-Standing Director
Woo-Young Choi	73	2016	Non-Standing Director

Operating Divisions

We have six operating divisions: planning, administrative support, business financing, global marketing, human resources and technology support, and enterprise resources. These six divisions are further broken down into departments and offices. The key functions of the six divisions are as follows:

- Planning—management of budget and organizational structure, corporate governance, business planning, new business development, personnel management and litigation.
- Administrative Support—issuance of bonds and other financing activities, tax, customer relationship management, performance evaluation and information management.
- Business Financing—SME diagnostics, business evaluation, operation of policy fund, investment management, export assistance, risk management and credit ratings management.
- Global Marketing—assistance with export, overseas expansion and marketing, operation of overseas offices, operation of APEC SME Innovation Center, international cooperation and network expansion and online export support.
- Human Resources and Technology Support—human resources development and operation of Youth Startup Academy and SME Training Institutes.
- Enterprise Resources—loan collection, on-site business support, operation and management of regional offices, policy fund support and overseas marketing.

Employees

As of June 30, 2016, we had a total of 926 employees, consisting of 914 permanent employees and 12 temporary employees hired on a contractual basis, among whom 687 employees were members of our labor union. Our employees who have worked for more than one year are entitled to lump-sum payments based on salary rates and length of service at the time they leave. For more detailed information about our employee's retirement and severance benefits, see note 3(8) of the SME Fund's financial statements as of December 31, 2014 and 2015 included in this Offering Circular.

Litigation

As of December 31, 2015, we were a defendant in four different court proceedings related to the SME Fund. As of such date, those proceedings included claims against us amounting to ₩1 billion in the aggregate. While we are unable to predict the ultimate disposition of these claims at present, our management does not believe that the ultimate disposition of these claims will have a material adverse effect on us. For more detailed information about the SME Fund's significant pending litigations, see note 17 of the SME Fund's financial statements as of December 31, 2014 and 2015 included in this Offering Circular.

Subsidiaries

The table below sets forth brief details of our subsidiaries as of December 31, 2015:

	<u>Ownership</u> (%)	<u>Book Value</u> (billions of Won)	<u>Net Asset Value</u> (billions of Won)
Small Business Distribution Center Co., Ltd.	100%	₩ 92	₩ 92
Small and medium Business Corporation Registrar	100	3	3
Korea Venture Investment Corporation	100	77	77
Korea Fund of Funds	59	1,453	1,453

The Small Business Distribution Center Co., Ltd. is our wholly-owned subsidiary and was founded in 1995 in accordance with the SME Promotion Act to assist with the production and distribution of goods of SMEs, and the establishment and operation of exhibition facilities in Korea and abroad.

The Small and medium Business Corporation Registrar is our wholly-owned subsidiary and was established in 1995 by the MoTIE in accordance with the Quality Management and Safety Control of Industrial Products Act to promote the competitiveness of Korean SMEs abroad. The SMBA has officially designated the Small and medium Business Corporation Registrar as a quality certification institute.

The Korea Venture Investment Corporation is our wholly owned-subsubsidiary and was founded in 2005 in accordance with the Act on Special Measures for the Promotion of Venture Businesses to promote the growth and development of SMEs and startup companies in Korea. It was formerly known as Dasan Venture Corporation.

The Korea Fund of Funds was established in 2005 in accordance with the Special Measures for the Promotion of Venture Business Act for the provision of a stable capital source for venture investment. The fund is managed by the Korea Venture Investment Corporation.

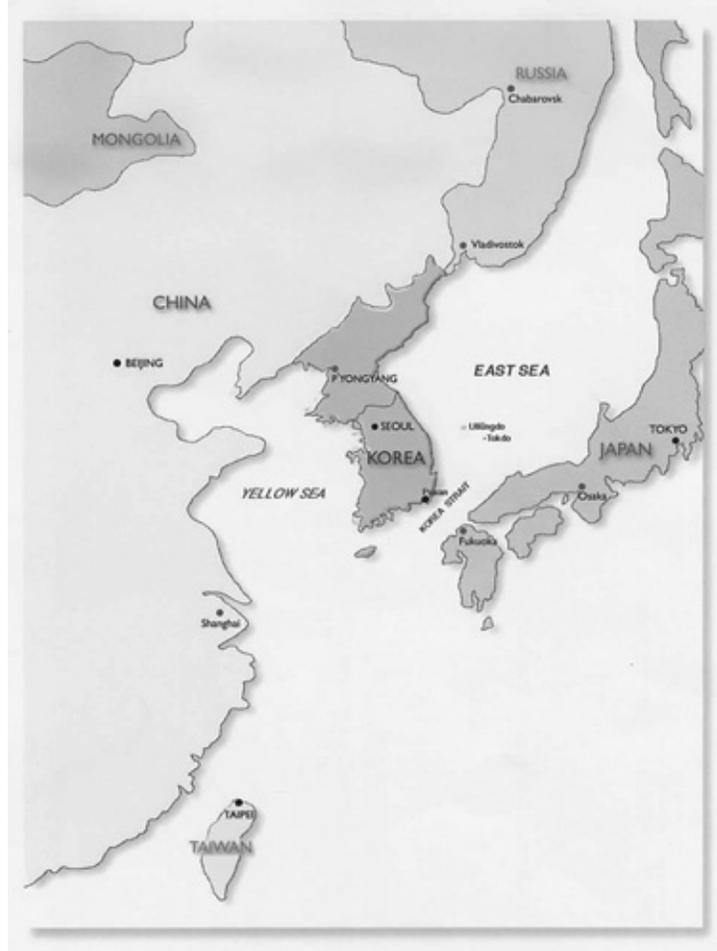
THE REPUBLIC OF KOREA

Land and History

Territory and Population

Located generally south of the 38th parallel on the Korean peninsula, The Republic of Korea covers about 38,000 square miles, approximately one-fourth of which is arable. The Republic has a population of approximately 51 million people. The country's largest city and capital, Seoul, has a population of about 10 million people.

Map of the Republic of Korea



Political History

Dr. Rhee Seungman, who was elected President in each of 1948, 1952, 1956 and 1960, dominated the years after the Republic's founding in 1948. Shortly after President Rhee's resignation in 1960 in response to student-led demonstrations, a group of military leaders headed by Park Chung Hee assumed power by coup. The military leaders established a civilian government, and the country elected Mr. Park as President in October 1963. President Park served as President until his assassination in 1979 following a period of increasing strife between the Government and its critics. The Government declared martial law and formed an interim government under Prime Minister Choi Kyu Hah, who became the next President. After clashes between the Government and its critics, President Choi resigned, and General Chun Doo Hwan, who took control of the Korean army, became President in 1980.

In late 1980, the country approved, by national referendum, a new Constitution, providing for indirect election of the President by an electoral college and for certain democratic reforms, and shortly thereafter, in early 1981, re-elected President Chun.

Responding to public demonstrations in 1987, the legislature revised the Constitution to provide for direct election of the President. In December 1987, Roh Tae Woo won the Presidency by a narrow plurality, after opposition parties led by Kim Young Sam and Kim Dae Jung failed to unite behind a single candidate. In February 1990, two opposition political parties, including the one led by Kim Young Sam, merged into President Roh's ruling Democratic Liberal Party.

In December 1992, the country elected Kim Young Sam as President. The election of a civilian and former opposition party leader considerably lessened the controversy concerning the legitimacy of the political regime. President Kim's administration reformed the political sector and deregulated and internationalized the Korean economy.

In December 1997, the country elected Kim Dae Jung as President. President Kim's party, the Millennium Democratic Party (formerly known as the National Congress for New Politics), formed a coalition with the United Liberal Democrats led by Kim Jong Pil, with Kim Jong Pil becoming the first prime minister in President Kim's administration. The coalition, which temporarily ended before the election held in April 2000, continued with the appointment of Lee Han Dong of the United Liberal Democrats as the Prime Minister in June 2000. The coalition again ended in September 2001.

In December 2002, the country elected Roh Moo Hyun as President. President Roh and his supporters left the Millennium Democratic Party in 2003 and formed a new party, the Uri Party, in November 2003. On August 15, 2007, 85 members of the National Assembly, previously belonging to the Uri Party, or the Democratic Party, formed the United New Democratic Party (the "UNDP"). The Uri Party merged into the UNDP on August 20, 2007. In February 2008, the UNDP merged back into the Democratic Party. In December 2011, the Democratic Party merged with the Citizens Unity Party to form the Democratic United Party, which changed its name to the Democratic Party in May 2013.

In December 2007, the country elected Lee Myung-Bak as President. He commenced his term on February 25, 2008. The Lee administration pursued a lively market economy through deregulation, free trade and the attraction of foreign investment.

In December 2012, the country elected Park Geun-hye as President. She commenced her term on February 25, 2013. The Park administration's key policy priorities include:

- facilitating the growth of small and medium-enterprises and job creation;
- seeking a productive welfare system based on customized welfare benefits and job training;
- promoting clean and renewable energy technologies;
- facilitating new growth engine industries;
- taking initiatives on the denuclearization of North Korea; and
- establishing an efficient government by reorganizing government functions.

Government and Politics

Government and Administrative Structure

Governmental authority in the Republic is centralized and concentrated in a strong Presidency. The President is elected by popular vote and can only serve one term of five years. The President chairs the State Council, which consists of the prime minister, the deputy prime ministers, the respective heads of Government ministries and the ministers of state. The President can select the members of the State Council and appoint or remove all other Government officials, except for elected local officials.

The President can veto new legislation and take emergency measures in cases of natural disaster, serious fiscal or economic crisis, state of war or other similar circumstances. The President must promptly seek the concurrence of the National Assembly for any emergency measures taken and failing to do so automatically invalidates the emergency measures. In the case of martial law, the President may declare martial law without the consent of the National Assembly; provided, however, that the National Assembly may request the President to rescind such martial law.

The National Assembly exercises the country's legislative power. The Election for Public Offices Act provide for the direct election of about 82% of the members of the National Assembly and the distribution of the remaining seats proportionately among parties winning more than 5 seats in the direct election or receiving over 3% of the popular vote. National Assembly members serve four-year terms. The National Assembly enacts laws, ratifies treaties and approves the national budget. The executive branch drafts most legislation and submits it to the National Assembly for approval.

The country's judicial branch comprises the Supreme Court, the Constitutional Court and lower courts of various levels. The President appoints the Chief Justice of the Supreme Court and appoints the other Justices of the Supreme Court upon the recommendation of the Chief Justice. All appointments to the Supreme Court require the consent of the National Assembly. The Chief Justice, with the consent of the conference of Supreme Court Justices, appoints all the other judges in Korea. Supreme Court Justices serve for six years and all other judges serve for ten years. Other than the Chief Justice, justices and judges may be reappointed to successive terms.

The President formally appoints all nine judges of the Constitutional Court, but three judges must be designated by the National Assembly and three by the Chief Justice of the Supreme Court. Constitutional Court judges serve for six years and may be reappointed to successive terms.

Administratively, the Republic comprises eight provinces, one special autonomous province (Jeju), one special city (Seoul), six metropolitan cities (Busan, Daegu, Incheon, Gwangju, Daejeon and Ulsan) and one special autonomous city (Sejong). From 1961 to 1995, the national government controlled the provinces and the President appointed provincial officials. Local autonomy, including the election of provincial officials, was reintroduced in June 1995.

Political Parties

The 20th legislative general election was held on April 13, 2016 and the term of the National Assembly members elected in the 20th legislative general election commenced on May 30, 2016. Currently, there are three major political parties: the Saenuri Party, or SP, to which President Park Geun-hye belongs, The Minjoo Party of Korea, or MPK (formerly known as the New Politics Alliance for Democracy, or NPAD, before certain of its members left in December 2015 to form a new party), and People's Party, or PP, which was established in February 2016 by certain former members of the NPAD.

As of August 19, 2016, the parties control the following number of seats in the National Assembly:

	<u>SP</u>	<u>MPK</u>	<u>PP</u>	<u>Others</u>	<u>Total</u>
Number of seats	129	121	38	12	300

Relations with North Korea

Relations between the Republic and North Korea have been tense over most of the Republic’s history. The Korean War, which took place between 1950 and 1953 began with the invasion of the Republic by communist forces from North Korea and, following a military stalemate, an armistice was reached establishing a demilitarized zone monitored by the United Nations in the vicinity of the 38th parallel.

North Korea maintains a regular military force estimated at more than 1,000,000 troops, mostly concentrated near the northern border of the demilitarized zone. The Republic’s military forces, composed of approximately 650,000 regular troops and almost 3.0 million reserves, maintain a state of military preparedness along the southern border of the demilitarized zone. In addition, the United States has historically maintained its military presence in the Republic. In October 2004, the United States and the Republic agreed to a three-phase withdrawal of approximately one-third of the 37,500 troops stationed in the Republic by the end of 2008. By the end of 2004, 5,000 U.S. troops departed the Republic in the first phase of such withdrawal and in the plan’s second phase, the United States removed 5,000 troops by the end of 2006. In the final phase, another 2,500 U.S. troops were scheduled to depart by the end of 2008. In April 2008, however, the United States and the Republic decided not to proceed with the final phase of withdrawal and agreed to maintain 28,500 U.S. troops in the Republic. In February 2007, the United States and the Republic agreed to dissolve their joint command structure by 2012, which would allow the Republic to assume the command of its own armed forces in the event of war on the Korean peninsula. In June 2010, however, the United States and the Republic agreed to delay the dissolution of their joint command structure to 2015. In October 2014, the United States and the Republic further agreed to implement a conditions-based approach to the dissolution of their joint command structure at an appropriate future date.

Relations between Korea and North Korea have been tense throughout Korea’s modern history. The level of tension between the two Koreas has fluctuated and may increase abruptly as a result of current and future events. In particular, since the death of Kim Jong-il in December 2011, there has been increased uncertainty with respect to the future of North Korea’s political leadership and concern regarding its implications for political and economic stability in the region. Although Kim Jong-il’s third son, Kim Jong-eun has assumed power as his father’s designated successor, the long-term outcome of such leadership transition remains uncertain.

In addition, there have been heightened security concerns in recent years stemming from North Korea’s nuclear weapons and long-range missile programs as well as its hostile military and other actions against Korea. Some of the significant incidents in recent years include the following:

- North Korea renounced its obligations under the Nuclear Non-Proliferation Treaty in January 2003 and conducted three rounds of nuclear tests between October 2006 to February 2013, which increased tensions in the region and elicited strong objections worldwide. In January 2016, North Korea announced that it had successfully tested a hydrogen bomb, its fourth nuclear test and allegedly first test using hydrogen, which is more explosive than plutonium. In February 2016, North Korea tested its intercontinental ballistic missile technology and launched a long-range missile, which it claimed to have launched a satellite into orbit. In response, the Government condemned the provocations and flagrant violations of relevant United Nations Security Council resolutions and withdrew Korean personnel from the inter-Korea Gaesong Industrial Complex and announced its closing. In March 2016, the United Nations Security Council unanimously passed a resolution condemning North Korea’s actions and significantly expanding the scope of sanctions applicable to North Korea.
- In June 2016, North Korea test fired an intermediate-range ballistic missile and declared that it had the capability to strike U.S. interests in the Pacific and would continue to increase its “pre-emptive nuclear

attack capability.” In response, the Government, along with the United Nations Security Council, strongly condemned the provocation and flagrant violations of relevant United Nations Security Council resolutions.

- In August 2015, two Korean soldiers were seriously wounded in landmine explosions while on routine patrol of the southern side of the demilitarized zone. The Government and the United Nations Command announced that the landmines were emplaced by North Korea, and in response, the Korean army restarted its loudspeaker propaganda broadcasts directed at the northern side of the demilitarized zone. The North Korean army retaliated by firing artillery rounds at the loudspeakers resulting in both sides being placed on the highest level of military readiness. High-ranking officials from the Government and North Korea subsequently met for discussions intending to diffuse military tensions and released a joint statement whereby, among other things, North Korea expressed regret over the landmine explosions that wounded the Korean soldiers.
- In March 2010, a Korean naval vessel was destroyed by an underwater explosion, killing many of the crewmen on board. The Government formally accused North Korea of causing the sinking, while North Korea denied responsibility. Moreover, in November 2010, North Korea fired more than one hundred artillery shells that hit Korea’s Yeonpyeong Island near the Northern Limit Line, which acts as the de facto maritime boundary between Korea and North Korea on the west coast of the Korean peninsula, causing casualties and significant property damage. The Government condemned North Korea for the attack and vowed stern retaliation should there be further provocation.

North Korea’s economy also faces severe challenges, which may aggravate social and political pressures within North Korea. There can be no assurance that the level of tension on the Korean peninsula will not escalate in the future or that such escalation will not have a material adverse impact on the Republic’s economy. Any further increase in tension, which may occur, for example, if North Korea experiences a leadership crisis, high-level contacts between the Republic and North Korea break down or military hostilities occur, could have a material adverse effect on the Republic’s economy. Over the longer term, reunification of the two Koreas could occur. Reunification may entail a significant economic commitment by the Republic.

Foreign Relations and International Organizations

The Republic maintains diplomatic relations with most nations of the world, most importantly with the United States with which it entered into a mutual defense treaty and several economic agreements. The Republic also has important relationships with Japan and China, its largest trading partners together with the United States.

The Republic belongs to a number of supranational organizations, including:

- United Nations;
- the International Monetary Fund, or the IMF;
- the World Bank;
- the Asian Development Bank, or ADB;
- the Multilateral Investment Guarantee Agency;
- the International Finance Corporation;
- the International Development Association;
- the African Development Bank;
- the European Bank for Reconstruction and Development;
- the Bank for International Settlements;
- the World Trade Organization, or WTO;

- the Inter-American Development Bank, or IDB; and
- the Organization for Economic Cooperation and Development, or OECD.

The Economy

The following table sets forth information regarding certain of the Republic's key economic indicators for the periods indicated.

	As of or for the year ended December 31,				
	2011	2012	2013	2014	2015
	(billions of dollars and trillions of Won, except percentages)				
GDP Growth (at current prices)	5.3%	3.4%	3.8%	4.0%	4.9%
GDP Growth (at chained 2010 year prices)	3.7%	2.3%	2.9%	3.3%	2.6%
Inflation	4.0%	2.2%	1.3%	1.3%	0.7%
Unemployment ⁽¹⁾	3.4%	3.2%	3.1%	3.5%	3.6%
Trade Surplus ⁽²⁾	\$ 30.8	\$ 28.3	\$ 44.0	\$ 47.2	\$ 90.3
Foreign Currency Reserves	\$ 306.4	\$ 327.0	\$ 346.5	\$ 363.6	\$ 368.0
External Liabilities ⁽³⁾	\$ 400.0	\$ 408.9	\$ 423.5	\$ 424.4	\$ 396.6 ⁽⁶⁾
Fiscal Balance	₩ 18.6	₩ 18.5	₩ 14.2	₩ 8.5 ⁽⁶⁾	₩ (0.2) ⁽⁶⁾
Direct Internal Debt of the Government ⁽⁴⁾ (as % of GDP ⁽⁵⁾)	29.7%	30.9%	32.8%	34.6 ⁽⁶⁾	37.4 ⁽⁶⁾
Direct External Debt of the Government ⁽⁴⁾ (as % of GDP ⁽⁵⁾)	0.7%	0.6%	0.6%	0.5 ⁽⁶⁾	0.5 ⁽⁶⁾

Notes:

- (1) Average for year.
- (2) Derived from customs clearance statistics on a C.I.F. basis, meaning that the price of goods include insurance and freight cost.
- (3) Calculated under the criteria based on the sixth edition of Balance of Payment Manual, or BPM6, published by the International Monetary Fund in December 2010.
- (4) Does not include guarantees by the Government. See “—Debt—External and Internal Debt of the Government—Guarantees by the Government” for information on outstanding guarantees by the Government.
- (5) At chained 2010 year prices.
- (6) Preliminary.

Source: The Bank of Korea

Worldwide Economic and Financial Difficulties

In recent years, the global financial markets have experienced significant volatility as a result of, among other things:

- the financial difficulties affecting many governments worldwide, in particular in southern Europe and Latin America;
- the slowdown of economic growth in China and other major emerging market economies;
- interest rate fluctuations as well as the possibility of increases in policy rates by the U.S. Federal Reserve and other central banks;
- political and social instability in various countries in the Middle East and Northern Africa, including Iraq, Syria and Yemen, as well as in the Ukraine and Russia; and
- fluctuations in oil and commodity prices.

In light of the high level of interdependence of the global economy, any of the foregoing developments could have a material adverse effect on the Korean economy and financial markets.

As a result of adverse global and Korean economic conditions, there has been significant volatility in the Korea Composite Stock Index in recent years, due to adverse global financial and economic conditions. See “—The Financial System—Securities Markets”. There is no guarantee that the stock prices of Korean companies will not decline again in the future. Future declines in the index and large amounts of sales of Korean securities by foreign investors and subsequent repatriation of the proceeds of such sales may continue to adversely affect the value of the Won, the foreign currency reserves held by financial institutions in Korea, and the ability of Korean companies and banks to raise capital. In addition, the value of the Won relative to major foreign currencies in general and the U.S. dollar in particular has fluctuated widely in recent years. A depreciation of the Won will increase the cost of imported goods and services and the Won revenue needed by Korean companies to service foreign currency-denominated debt.

In the event that such difficult conditions in the global credit markets continue or the global economy deteriorates in the future, the Korean economy could be adversely affected and Korean banks may be forced to fund their operations at a higher cost or may be unable to raise as much funding as they need to support their lending and other activities.

Furthermore, while many governments worldwide are considering or are in the process of implementing “exit strategies”, in the form of reduced government spending, higher interest rates or otherwise, with respect to the economic stimulus measures adopted in response to the global financial crisis, such strategies may, for reasons related to timing, magnitude or other factors, have the unintended consequence of prolonging or worsening global economic and financial difficulties.

In addition to the global developments, domestic developments that could lead or contribute to a material adverse effect on the Korean economy include, among other things, the following:

- steadily rising household debt consisting of housing loans and merchandise credit, which increased to approximately ₩1,207.0 trillion as of December 31, 2015 from ₩843.2 trillion as of December 31, 2010, primarily due to increases in mortgage loans and purchases with credit cards;
- a slowdown in consumer spending and depressed consumer sentiment, due in part to national tragedies including the sinking of the Sewol passenger ferry in April 2014, which led to the death of hundreds of passengers, and the outbreak of infectious diseases, such as the outbreak of the Middle East Respiratory Syndrome (“MERS”) in May 2015, which resulted in the death of over 30 people and the quarantine of thousands;
- a decrease in tax revenue and a substantial increase in the Korean government’s expenditures for pension and social welfare programs, due in part to an aging population (defined as the population of people aged 65 years or older) that accounts for 13.1% of the Republic’s total population as of December 31, 2015, an increase from 7.2% as of December 31, 2000, and is expected to surpass 15% in 2020 and 20% in 2026, which could lead to the Korean government’s budget deficit;
- increasing delinquencies and credit defaults by consumer and small- and medium-sized enterprise borrowers;
- decreases in the market prices of Korean real estate; and
- the occurrence of severe health epidemics, including epidemics that affect the livestock industry.

Gross Domestic Product

GDP measures the market value of all final goods and services produced within a country for a given period and reveals whether a country’s productive output rises or falls over time. Economists present GDP in both current market prices and “real” or “inflation-adjusted” terms. In March 2009, the Republic adopted a method known as the “chain-linked” measure of GDP, replacing the previous fixed-base, or “constant” measure of GDP, to show the real growth of the aggregate economic activity, as recommended by the System of National Accounts

1993. GDP at current market prices values a country's output using the actual prices of each year, whereas the "chain-linked" measure of GDP is compiled by using "chained indices" linking volume growth between consecutive time periods. In March 2014, the Republic published a revised GDP calculation method by implementing the System of National Accounts 2008 and updating the reference year from 2005 to 2010 to align Korean national accounts statistics with the recommendations of the new international standards for compiling national economic accounts and to maintain comparability with other nations' accounts. The main components of these revisions include, among other things, (i) recognizing expenditures for research and development and creative activity for the products of entertainment, literary and artistic originals as fixed investment, (ii) incorporating a wide array of new and revised source data such as the economic census, the population and housing census and 2010 benchmark input-output tables, which provide thorough and detailed information on the structure of the Korean economy, (iii) developing supply-use tables, which provide a statistical tool for ensuring consistency among the production, expenditure and income approaches to measuring GDP and (iv) recording merchandise trade transactions based on ownership changes rather than movements of goods across the national frontier.

The following table sets out the composition of the Republic's GDP at current market and chained 2010 year prices and the annual average increase in the Republic's GDP.

Gross Domestic Product						
	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015⁽¹⁾</u>	<u>As % of GDP 2015⁽¹⁾</u>
	(billions of Won)					
Gross Domestic Product at						
Current Market Prices:						
Private	679,141.5	707,614.0	727,799.9	748,200.8	771,211.9	49.5
Government	194,381.2	204,324.2	214,467.3	224,724.2	237,135.1	15.2
Gross Capital Formation	439,236.1	427,028.5	416,000.3	435,078.1	444,014.9	28.5
Exports of Goods and						
Services	742,936.0	776,062.4	770,114.8	747,134.3	715,411.3	45.9
Less Imports of Goods and						
Services	(723,013.8)	(737,572.4)	(698,936.9)	(669,058.0)	(606,942.0)	(38.9)
Statistical Discrepancy	—	—	—	—	(2,239.7)	(0.1)
Expenditures on Gross						
Domestic Product	1,332,681.0	1,377,456.7	1,429,445.4	1,486,079.3	1,558,591.6	100.0
Net Factor Income from the						
Rest of the World	7,848.8	14,138.8	10,199.0	4,684.5	7,223.9	0.5
Gross National Income ⁽²⁾ ...	1,340,529.8	1,391,595.5	1,439,644.4	1,490,763.9	1,565,815.5	100.5
Gross Domestic Product at						
Chained 2010 Year Prices:						
Private	655,181.1	667,781.2	680,349.5	692,236.0	707,151.7	48.3
Government	187,158.2	193,473.5	199,783.4	205,869.2	212,797.8	14.5
Gross Capital Formation	419,282.7	409,639.9	409,153.8	430,685.5	459,783.1	31.4
Exports of Goods and						
Services	719,943.2	756,558.4	788,788.0	804,797.1	811,040.9	55.4
Less Imports of Goods and						
Services	(668,931.5)	(685,009.4)	(696,724.6)	(706,938.4)	(729,744.7)	(49.8)
Statistical Discrepancy	(740.9)	(142.1)	(172.8)	1,019.1	2,508.1	0.2
Expenditures on Gross						
Domestic Product ⁽³⁾	1,311,892.7	1,341,966.5	1,380,832.6	1,426,972.4	1,464,244.0	100.0
Net Factor Income from the						
Rest of the World in the						
Terms of Trade	7,573.1	13,577.8	10,037.5	4,706.4	7,126.7	0.5

	2011	2012	2013	2014	2015 ⁽¹⁾	As % of GDP 2015 ⁽¹⁾
	(billions of Won)					
Trading Gains and Losses from Changes in the Terms of Trade	(32,183.6)	(33,075.1)	(19,138.8)	(14,000.4)	39,146.7	2.7
Gross National Income ⁽⁴⁾ . . .	1,287,282.2	1,322,449.9	1,371,733.1	1,417,814.2	1,510,626.5	103.2
Percentage Increase (Decrease) of GDP over Previous Year At						
Current Prices	5.3	3.4	3.8	4.0	4.9	
At Chained 2010 Year Prices	3.7	2.3	2.9	3.3	2.6	

Notes:

- (1) Preliminary.
- (2) GDP plus net factor income from the rest of the world is equal to the Republic's gross national product.
- (3) Under the "chain-linked" measure of GDP, the components of GDP will not necessarily add to the total GDP.
- (4) Under the "chain-linked" measure of Gross National Income, the components of Gross National Income will not necessarily add to the total Gross National Income.

Source: The Bank of Korea.

The following table sets out the Republic's GDP by economic sector at current market prices:

**Gross Domestic Product by Economic Sector
(at current market prices)**

	2011	2012	2013	2014	2015 ⁽¹⁾	As % of GDP 2015 ⁽¹⁾
	(billions of Won)					
Industrial Sectors:						
Agriculture, Forestry and Fisheries	30,454.0	30,775.1	30,437.2	31,560.3	32,741.0	2.1
Mining and Manufacturing	381,808.0	390,288.6	406,127.7	411,030.4	420,585.3	27.0
Mining and Quarrying	2,287.0	2,278.5	2,471.0	2,520.2	2,543.3	0.2
Manufacturing	379,521.0	388,010.1	403,656.7	408,510.2	418,042.0	26.8
Electricity, Gas and Water Supply	23,994.1	26,178.2	30,238.7	37,373.8	45,120.7	2.9
Construction	58,587.3	59,959.4	64,250.5	67,266.7	72,751.3	4.7
Services:	715,112.9	744,253.9	772,184.1	807,624.1	846,410.3	54.3
Wholesale and Retail Trade, Restaurants and Hotels . .	140,705.3	146,807.7	150,251.9	152,205.2	156,097.0	10.0
Transportation and Storage	42,458.7	43,570.7	46,772.0	50,306.8	57,371.9	3.7
Finance and Insurance	77,872.6	75,808.5	72,478.1	75,859.8	77,990.7	5.0
Real Estate and Leasing . . .	94,716.1	98,923.6	103,527.1	109,549.0	115,169.7	7.4
Information and Communication	46,827.0	48,774.2	50,589.2	52,510.8	54,125.7	3.5
Business Activities	83,277.4	88,828.1	94,758.4	100,936.7	105,893.4	6.8
Public Administration and Defense	83,290.8	88,654.6	93,776.3	98,333.5	104,678.4	6.7
Education	66,559.6	68,546.3	71,599.3	74,007.8	76,582.5	4.9
Health and Social Work . . .	46,656.1	50,031.3	52,851.5	57,129.7	61,150.7	3.9

	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015⁽¹⁾</u>	<u>As % of GDP 2015⁽¹⁾</u>
	(billions of Won)					
Cultural and Other Services	32,749.4	34,309.0	35,580.3	36,784.7	37,350.4	2.4
Taxes Less Subsidies on Products	122,724.8	126,001.4	126,207.2	131,224.0	140,983.0	9.0
Gross Domestic Product at Current Market Prices	1,332,681.0	1,377,456.7	1,429,445.4	1,486,079.3	1,558,591.6	100.0
Net Factor Income from the Rest of the World	7,848.8	14,138.8	10,199.0	4,684.5	7,223.9	0.5
Gross National Income at Current Market Price	1,340,529.8	1,391,595.5	1,439,644.4	1,490,763.9	1,565,815.5	100.5

Note:

(1) Preliminary.

Source: The Bank of Korea.

The following table sets out the Republic's GDP per capita:

**Gross Domestic Product per capita
(at current market prices)**

	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015⁽¹⁾</u>
GDP per capita (thousands of Won)	26,772	27,547	28,464	29,472	30,792
GDP per capita (U.S. dollar)	24,160	24,445	25,993	27,983	27,214
Average Exchange Rate (in Won per U.S. dollar)	1,108.1	1,126.9	1,095.0	1,053.2	1,131.5

Note:

(1) Preliminary.

Source: The Bank of Korea.

The following table sets out the Republic's Gross National Income, or GNI, per capita:

**Gross National Income per capita
(at current market prices)**

	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015⁽¹⁾</u>
GNI per capita (thousands of Won)	26,929	27,829	28,667	29,565	30,935
GNI per capita (U.S. dollar)	24,302	24,696	26,179	28,071	27,340
Average Exchange Rate (in Won per U.S. dollar)	1,108.1	1,126.9	1,095.0	1,053.2	1,131.5

Note:

(1) Preliminary.

Source: The Bank of Korea.

The following table sets out the Republic's GDP by economic sector at chained 2010 year prices:

Gross Domestic Product by Economic Sector						
(at chained 2010 year prices)						
	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015⁽¹⁾</u>	<u>As % of GDP</u>
	(billions of Won)					<u>2015⁽¹⁾</u>
Industrial Sectors:						
Agriculture, Forestry and Fisheries	27,744.6	27,506.9	28,357.7	29,378.2	28,951.1	2.0
Mining and Manufacturing	376,958.3	385,853.1	399,73.1	413,839.1	418,970.9	28.6
Mining and Quarrying	2,176.3	2,170.5	2,347.1	2,344.40	2,327.7	0.2
Manufacturing	374,782.0	383,682.6	397,426.0	411,494.7	416,643.2	28.5
Electricity, Gas and Water Supply	25,687.4	26,710.3	26,629.2	27,327.9	29,027.3	2.0
Construction	55,432.2	54,430.5	56,044.1	56,470.9	58,174.8	4.0
Services:	699,580.8	718,906.2	739,463.1	763,853.5	785,490.9	53.6
Wholesale and Retail Trade, Restaurants and Hotels	137,058.1	141,698.2	145,620.3	149,150.5	152,318.6	10.4
Transportation and Storage	46,157.9	46,877.6	47,556.1	48,646.9	49,974.0	3.4
Finance and Insurance	72,741.3	75,547.3	78,583.9	83,020.5	88,215.6	6.0
Real Estate and Leasing	93,383.7	93,182.9	93,999.5	97,112.9	98,937.0	6.8
Information and Communication	47,931.6	50,199.3	52,773.2	55,164.8	56,455.4	3.9
Business Activities	80,913.7	83,352.8	87,244.6	91,424.0	95,055.1	6.5
Public Administration and Defense	80,639.1	82,940.5	85,024.5	87,052.8	89,401.5	6.1
Education	63,806.6	64,386.6	64,773.0	64,865.2	65,235.5	4.5
Health and Social Work	45,483.3	48,693.4	51,247.1	54,740.1	57,804.5	3.9
Cultural and Other Services	31,465.5	31,972.6	32,683.2	33,106.0	33,066.5	2.3
Taxes Less Subsidies on Products	126,489.5	128,708.4	130,627.4	136,454.6	143,681.6	9.8
Gross Domestic Product at Chained 2010 Year Prices⁽²⁾	1,311,892.7	1,341,966.5	1,380,832.6	1,426,972.4	1,464,244.0	100.0

Notes:

(1) Preliminary.

(2) Under the "chain-linked" measure of GDP, the components of GDP will not necessarily add to the total GDP.

Source: The Bank of Korea.

GDP growth in 2011 was 3.7% at chained 2010 year prices, as aggregate private and general government consumption expenditures increased by 2.7%, exports of goods and services increased by 15.1% and gross domestic fixed capital formation increased by 0.8%, each compared with 2010.

GDP growth in 2012 was 2.3% at chained 2010 year prices, as aggregate private and general government consumption expenditures increased by 2.2% and exports of goods and services increased by 5.1%, which more than offset a decrease in gross domestic fixed capital formation by 0.5%, each compared with 2011.

GDP growth in 2013 was 2.9% at chained 2010 year prices, as aggregate private and general government consumption expenditures increased by 2.2%, exports of goods and services increased by 4.3% and gross domestic fixed capital formation increased by 3.3%, each compared with 2012.

GDP growth in 2014 was 3.3% at chained 2010 year prices, as aggregate private and general government consumption expenditures increased by 2.0%, exports of goods and services increased by 2.8% and gross domestic fixed capital formation increased by 3.1%, each compared with 2013.

Based on preliminary data, GDP growth in 2015 was 2.6% at chained 2010 year prices, as aggregate private and general government consumption expenditures increased by 2.4%, gross domestic fixed capital formation increased by 3.8% and exports of goods and services increased by 0.4%, each compared with 2014. Based on preliminary data, GDP growth in the first half of 2016 was 3.0% at chained 2010 year prices, as aggregate private and general government consumption expenditures increased by 3.0%, gross domestic fixed capital formation increased by 4.2% and exports of goods and services increased by 1.2%, each compared with the corresponding period of 2015.

Principal Sectors of the Economy

Industrial Sectors

The following table sets out production indices for the principal industrial products of the Republic and their relative contribution to total industrial production:

Industrial Production (2010 = 100)						
	Index Weight ⁽¹⁾	2011	2012	2013	2014	2015 ⁽²⁾
All Industries	10,000.0	106.0	107.4	108.2	108.2	107.5
Mining and Manufacturing	9,611.6	106.0	107.5	108.2	108.3	107.5
Mining	33.9	104.5	99.8	103.8	95.7	96.8
Petroleum, Crude Petroleum and Natural Gas	8.7	91.6	90.2	86.2	71.1	59.1
Metal Ores	0.9	124.9	108.5	98.4	99.9	78.9
Non-metallic Minerals	24.3	108.4	102.9	110.3	104.3	111.0
Manufacturing	9,577.7	106.0	107.5	108.2	108.3	107.6
Food Products	434.4	101.9	103.4	103.7	104.7	106.0
Beverage Products	82.4	103.5	108.2	108.8	110.0	111.6
Tobacco Products	43.2	101.6	105.6	96.5	103.9	96.3
Textiles	160.6	101.5	99.1	97.6	95.8	92.4
Wearing Apparel, Clothing Accessories and Fur Articles	145.2	100.6	97.9	93.6	88.1	85.7
Tanning and Dressing of Leather, Luggage and Footwear	42.1	101.1	98.2	111.5	109.8	100.8

	Index Weight ⁽¹⁾	2011	2012	2013	2014	2015 ⁽²⁾
Wood and Products of Wood and Cork (Except Furniture)	31.7	97.5	87.9	92.9	89.1	91.7
Pulp, Paper and Paper Products	126.8	102.3	102.7	105.1	105.2	104.1
Printing and Reproduction of Recorded Media	50.2	91.8	90.5	86.8	86.5	84.9
Coke, hard-coal and lignite fuel briquettes and Refined Petroleum Products	471.0	106.9	109.1	104.6	108.9	115.3
Chemicals and Chemical Products	847.5	102.7	106.6	110.9	111.8	113.3
Pharmaceuticals, Medicinal Chemicals and Botanical Products	144.1	100.3	101.2	103.2	104.6	107.1
Rubber and Plastic Products	421.1	105.1	106.4	109.9	110.4	109.9
Non-metallic Minerals	271.7	100.3	95.2	100.6	96.7	99.2
Basic Metals	827.6	106.2	106.8	106.0	109.9	107.8
Fabricated Metal Products	557.8	108.9	117.9	117.3	121.2	115.4
Electronic Components, Computer, Radio, Television and Communication Equipment and Apparatuses	1,794.3	107.1	109.7	113.6	111.5	113.2
Medical, Precision and Optical Instruments, Watches and Clocks	148.1	105.6	111.6	124.2	110.6	104.8
Electrical Equipment	479.5	100.8	98.8	97.0	97.7	94.3
Other Machinery and Equipment	803.6	109.3	107.0	102.7	104.8	100.8
Motor Vehicles, Trailers and Semitrailers	1,076.4	114.7	114.5	116.1	118.9	120.2
Other Transport Equipment	506.5	101.7	107.1	101.7	89.5	79.5
Furniture	69.5	105.4	98.2	97.2	104.2	112.1
Other Products	42.4	102.2	103.8	104.9	104.8	101.0
Electricity, Gas	388.4	104.5	106.4	106.8	107.6	106.9
Total Index	10,000.0	106.0	107.4	108.2	108.2	107.5

Notes:

(1) Index weights were established on the basis of an industrial census in 2010 and reflect the average annual value added by production in each of the classifications shown, expressed as a percentage of total value added in the mining, manufacturing and electricity and gas industries in that year.

(2) Preliminary.

Source: The Bank of Korea; Korea National Statistical Office.

Industrial production increased by 6.0% in 2011, primarily due to increased exports and domestic consumption. Industrial production increased by 1.3% in 2012, primarily due to increased domestic consumption. Industrial production increased by 0.7% in 2013, primarily due to increased exports. Industrial production remained unchanged in 2014. Based on preliminary data, industrial production decreased by 0.6% in 2015, primarily due to decreased exports.

Manufacturing

The manufacturing sector increased production by 6.0% in 2011, primarily due to increased domestic consumption and exports, by 1.4% in 2012, primarily due to increased demand for consumer electronics products, electronic equipment and chemical products, by 0.7% in 2013, primarily due to increased demand for consumer electronics products, electronic equipment, chemical products, medical equipment and transport equipment, and by 0.1% in 2014, primarily due to increased demand for basic metals, machinery and equipment and motor vehicles, trailers and semitrailers. Based on preliminary data, the manufacturing sector decreased production by 0.6% in 2015, primarily due to decreased demand for basic metals, fabricated metal products, other machinery and equipment, and other transport equipment.

Automobiles. In 2011, automobile production increased by 9.0%, domestic sales volume recorded an increase of 0.6% and export sales volume recorded an increase of 13.7%, compared with 2010, primarily due to increased demand for automobiles in the United States, Brazil, Russia and China. In 2012, automobile production decreased by 2.1%, domestic sales volume recorded a decrease of 4.3% and export sales volume recorded an increase of 0.6%, compared with 2011, primarily due to decreased domestic demand for automobiles. In 2013, automobile production decreased by 0.9%, domestic sales volume recorded a decrease of 2.0% and export sales volume recorded a decrease of 2.6%, compared with 2012, primarily due to decreased supply of automobiles resulting mainly from partial strikes by unionized workers of automobile manufacturers in August 2013 and the appreciation of the Won against the US dollar and the Japanese Yen. In 2014, automobile production increased by 0.1% and domestic sales volume recorded an increase of 4.6%, compared with 2013, primarily due to increased domestic demand for recreational vehicles, and export sales volume recorded a decrease of 0.8%, compared with 2013, primarily due to decreased demand for automobiles in Eastern Europe and South America. Based on preliminary data, in 2015, automobile production increased by 0.7% and domestic sales volume recorded an increase of 7.7%, compared with 2014, primarily due to continued increase in domestic demand for recreational vehicles, and export sales volume recorded a decrease of 2.8%, compared with 2014, primarily due to decreased demand for automobiles in China, Russia, Eastern Europe and South America.

Electronics. In 2011, electronics production amounted to ₩314,314 billion, an increase of 1.5% from the previous year, and exports amounted to US\$156.6 billion, an increase of 1.8% from the previous year, primarily due to continued increase in global demand for mobile phones and tablet computers. In 2011, export sales of semiconductor memory chips constituted approximately 9.0% of the Republic's total exports. In 2012, electronics production amounted to ₩314,558 billion, an increase of 0.1% from the previous year, primarily due to increased domestic demand for mobile phones and non-memory semiconductors, and exports amounted to US\$155.2 billion, a decrease of 0.9% from the previous year, primarily due to adverse economic conditions in European countries. In 2012, export sales of semiconductor memory chips constituted approximately 9.2% of the Republic's total exports. In 2013, electronics production amounted to ₩334,402 billion, an increase of 6.3% from the previous year, and exports amounted to US\$169.4 billion, an increase of 9.1% from the previous year, primarily due to increases in demand for mobile phones in emerging markets and global demand for non-memory semiconductors. In 2013, export sales of semiconductor memory chips constituted approximately 10.2% of the Republic's total exports. In 2014, electronics production amounted to ₩330,716 billion, an increase of 1.5% from the previous year, and exports amounted to US\$173.9 billion, an increase of 2.7% from the previous year, primarily due to increases in demand for mobile phones and semiconductors. In 2014, export sales of semiconductor memory chips constituted approximately 10.9% of the Republic's total exports. Based on preliminary data, in 2015, electronics production amounted to ₩325,906 billion, a decrease of 1.5% from the previous year, and exports amounted to US\$172.9 billion, a decrease of 0.6% from the previous year, primarily due to adverse global economic conditions and the expansion of overseas production. In 2015, export sales of semiconductor memory chips constituted approximately 11.9% of the Republic's total exports.

Iron and Steel. In 2010, crude steel production totaled 58.9 million tons, an increase of 20.2% from 2009, and domestic sales volume and export sales volume increased by 21.6% and 21.1%, respectively, primarily due to the recovery of global demand for crude steel products. In 2011, crude steel production totaled 68.5 million tons, an increase of 16.3% from 2010, and domestic sales volume and export sales volume increased by 5.8% and 16.9%, respectively, primarily due to continued increase in global demand for crude steel products. In 2012, crude steel production totaled 69.1 million tons, an increase of 0.9% from 2011, and domestic sales volume decreased by 5.1% but export sales volume increased by 4.8%, primarily due to adverse conditions in the domestic shipbuilding and construction industries. In 2013, crude steel production totaled 66.1 million tons, a decrease of 4.4% from 2012, and domestic sales volume and export sales volume decreased by 4.3% and 4.2%, respectively, primarily due to the appreciation of the Won against the US dollar and the Japanese Yen and excess supply from China. In 2014, crude steel production totaled 71.5 million tons, an increase of 8.3% from 2013, and domestic sales volume and export sales volume increased by 7.2% and 10.5%, respectively, primarily due to the recovery of domestic and global demand for crude steel products. Based on preliminary data, in 2015, crude steel production totaled 69.7 million tons, a decrease of 2.6% from 2014, and export sales volume decreased by 2.2%, primarily due to excess supply from China and adverse conditions in the domestic and global shipbuilding and construction industries.

Shipbuilding. In 2011, the Republic's shipbuilding orders amounted to approximately 12 million compensated gross tons, an increase of 50.0% compared to 2010, primarily due to increased demand for large container carriers, LNG carriers and floating production storage and offloading vessels. In 2012, the Republic's shipbuilding orders amounted to approximately 8 million compensated gross tons, a decrease of 33.3% compared to 2011, primarily due to a downturn in the shipping and shipbuilding industry. In 2013, the Republic's shipbuilding orders amounted to approximately 19 million compensated gross tons, an increase of 137.5% compared to 2012, primarily due to increased demand for LNG carriers, bulk carriers and container carriers. In 2014, the Republic's shipbuilding orders amounted to approximately 13 million compensated gross tons, a decrease of 31.6% compared to 2013, primarily due to a downturn in the domestic and global shipbuilding industry. Based on preliminary data, in 2015, the Republic's shipbuilding orders amounted to approximately 10 million compensated gross tons, a decrease of 23.1% compared to 2014, primarily due to the continued downturn in the domestic and global shipbuilding industry.

Agriculture, Forestry and Fisheries

The Government's agricultural policy has traditionally focused on:

- grain production;
- development of irrigation systems;
- land consolidation and reclamation;
- seed improvement;
- mechanization measures to combat drought and flood damage; and
- increasing agricultural incomes.

Recently, however, the Government has increased emphasis on cultivating profitable crops and strengthening international competitiveness in anticipation of opening the domestic agricultural market.

In 2011, rice production decreased 2.3% from 2010 to 4.2 million tons. In 2012, rice production decreased 4.7% from 2011 to 4.0 million tons. In 2013, rice production increased 5.0% from 2012 to 4.2 million tons. In 2014, rice production remained at 4.2 million tons. In 2015, rice production increased 2.4% from 2014 to 4.3 million tons. Due to limited crop yields resulting from geographical and physical constraints, the Republic depends on imports for certain basic foodstuffs.

The Government is seeking to develop the fishing industry by encouraging the building of large fishing vessels and modernizing fishing equipment, marketing techniques and distribution outlets.

In 2011, the agriculture, forestry and fisheries industry decreased by 2.1% compared to 2010, primarily due to unfavorable weather conditions, including heavy rains, during the summer and a decrease in fishing catch. In 2012, the agriculture, forestry and fisheries industry decreased by 0.6% compared to 2011, primarily due to unfavorable weather conditions, including severe typhoons, which more than offset an increase in the livestock industry. In 2013, the agriculture, forestry and fisheries industry increased by 3.1% compared to 2012, primarily due to an increase in the cultivation and livestock industry. Based on preliminary data, in 2014, the agriculture, forestry and fisheries industry increased by 2.6% compared to 2013, primarily due to increases in the price of certain livestock items, which led to increases in production and the establishment of new agriculture and fishery companies. Based on preliminary data, in 2015, the agriculture, forestry and fisheries industry decreased by 1.6% compared to 2014, primarily due to unfavorable weather conditions.

Construction

In 2011, the construction industry decreased by 4.3% compared to 2010, primarily due to a decrease in the construction of residential and commercial buildings. In 2012, the construction industry decreased by 1.6% compared to 2011, primarily due to a decrease in the construction of residential buildings and port facilities. In

2013, the construction industry increased by 3.0% compared to 2012, primarily due to an increase in the construction of residential and commercial buildings. In 2014, the construction industry increased by 0.6% compared to 2013, primarily due to an increase in the construction of private residential buildings. Based on preliminary data, in 2015, the construction industry increased by 3.2% compared to 2014, primarily due to an increase in the construction of private residential and commercial buildings.

Electricity and Gas

The following table sets out the Republic's dependence on imports for energy consumption:

Dependence on Imports for Energy Consumption

	<u>Total Primary Energy Supply</u>	<u>Imports</u>	<u>Imports Dependence Ratio</u>
	(millions of tons of oil equivalents, except ratios)		
2011	276.6	267.0	96.5
2012	278.7	267.6	96.0
2013	280.3	268.2	95.7
2014	282.9	269.4	95.2
2015 ⁽¹⁾	285.0	271.4	95.2

Note:

(1) Preliminary.

Source: Korea Energy Economics Institute; Korea National Statistical Office.

Korea has almost no domestic oil or gas production and depends on imported oil and gas to meet its energy requirements. Accordingly, the international prices of oil and gas significantly affect the Korean economy. Any significant long-term increase in the prices of oil and gas will increase inflationary pressures in Korea and adversely affect the Republic's balance of trade.

To reduce its dependence on oil and gas imports, the Government has encouraged energy conservation and energy source diversification emphasizing nuclear energy. The following table sets out the principal primary sources of energy consumed in the Republic, expressed in oil equivalents and as a percentage of total energy consumption.

Consumption of Energy by Source

	<u>Coal</u>		<u>Petroleum</u>		<u>Nuclear</u>		<u>Others⁽¹⁾</u>		<u>Total</u>	
	<u>Quantity</u>	<u>%</u>	<u>Quantity</u>	<u>%</u>	<u>Quantity</u>	<u>%</u>	<u>Quantity</u>	<u>%</u>	<u>Quantity</u>	<u>%</u>
	(millions of tons of oil equivalents, except percentages)									
2011	83.5	30.2	105.1	38.0	33.2	12.0	54.8	19.8	276.6	100.0
2012	81.1	29.1	106.2	38.1	31.8	11.4	59.6	21.4	278.7	100.0
2013	81.9	29.2	105.8	37.7	29.3	10.5	63.3	22.6	280.3	100.0
2014	84.6	29.9	104.9	37.1	33.0	11.7	60.4	21.4	282.9	100.0
2015	84.5	29.6	109.4	38.4	34.8	12.2	56.4	19.8	285.0	100.0

Note:

(1) Includes natural gas, hydroelectric power and renewable energy.

Source: Korea Energy Economics Institute; The Bank of Korea.

The Republic's first nuclear power plant went into full operation in 1978 with a rated generating capacity of 587 megawatts. As of December 31, 2015, the Republic had 24 nuclear plants with a total estimated nuclear power generating capacity of 21,716 megawatts and six nuclear plants under construction. In January 2014, the Ministry of Trade, Industry and Energy released its Second Energy Master Plan and revised the target proportion

of nuclear supply in the Korea's energy supply mix from 41% by 2030 to a range from 22% to 29% by 2035. In addition, in July 2015, the Ministry of Trade, Industry and Energy approved the construction of two additional nuclear power plants, which together with previously announced plans to build nuclear power plants would bring the number of nuclear power plants to 36 by 2029. The Government plans to expand infrastructure to supply natural gas to households, pursue a long-term strategy of overseas energy development projects to ensure supply stability, increase clean and renewable energy and provide support for research and development pertaining to green technologies.

Services Sector

In 2011, the service industry increased by 3.0% compared to 2010 as the transportation and storage sector increased by 3.8%, the wholesale and retail trade, restaurants and hotels sector increased by 5.1% and the real estate and leasing sector increased by 2.2%, each compared with 2010. In 2012, the service industry increased by 2.7% compared to 2011 as the health and social work sector increased by 7.1%, the finance and insurance sector increased by 3.6% and the wholesale and retail trade, restaurants and hotels sector increased by 3.4%, each compared with 2011. In 2013, the service industry increased by 2.8% compared to 2012 as the business activities sector increased by 4.7%, the finance and insurance sector increased by 3.6% and the health and social work sector increased by 5.2%, each compared with 2012. In 2014, the service industry increased by 3.1% compared to 2013 as the health and social work sector increased by 7.5%, the finance and insurance sector increased by 5.7% and the business activities sector increased by 4.1%, each compared with 2013. Based on preliminary data, in 2015, the service industry increased by 2.8% compared to 2014 as the finance and insurance sector increased by 6.7%, the business activities sector increased by 3.6% and the health and social work sector increased by 5.8%, each compared with 2014.

Prices, Wages and Employment

The following table shows selected price and wage indices and unemployment rates:

	Producer Price Index⁽¹⁾	Increase (Decrease) Over Previous Year	Consumer Price Index⁽¹⁾	Increase (Decrease) Over Previous Year	Wage Index⁽¹⁾⁽²⁾	Increase (Decrease) Over Previous Year	Unemployment Rate⁽¹⁾⁽³⁾
	(2010=100)	(%)	(2010=100)	(%)	(2010=100)	(%)	(%)
2011	106.7	6.7	104.0	4.0	100.3	0.3	3.4
2012	107.5	0.7	106.3	2.2	109.1	8.8	3.2
2013	105.7	(1.6)	107.7	1.3	116.4	6.7	3.1
2014	105.2	(0.5)	109.0	1.3	123.1	5.8	3.5
2015	110.0	(4.0)	109.8	0.7	N/A ⁽⁴⁾	N/A ⁽⁴⁾	3.6

Notes:

- (1) Average for year.
- (2) Nominal wage index of average earnings in manufacturing industry.
- (3) Expressed as a percentage of the economically active population.
- (4) Not available.

Source: The Bank of Korea; Korea National Statistical Office.

In 2011, the inflation rate increased to 4.0%, primarily due to increased oil prices in the first quarter as well as decreased supply in agricultural goods caused by unusually low temperatures in the spring and heavy rainfall in the summer. In 2012, the inflation rate decreased to 2.2%, primarily due to weakened aggregate demand and the implementation of new policies, including free school lunches. In 2013, the inflation rate decreased to 1.3%, primarily due to increased supply of agricultural goods. In 2014, the inflation rate remained at 1.3%, primarily due to increases in the prices of electricity, gas, water supply, food products and education, which were offset by lower oil prices. In 2015, the inflation rate decreased to 0.7%, primarily due to lower oil prices. The inflation rate was 1.0% in the first quarter of 2016.

In 2011, the unemployment rate decreased to 3.4%, primarily due to an increase in the number of workers employed in the service industry (including healthcare, social welfare and education). In 2012, the unemployment rate decreased to 3.2%, primarily due to the continued increase in the number of workers employed in the service industry. In 2013, the unemployment rate decreased to 3.1%, primarily due to the continued increase in the number of workers employed in the service industry. In 2014, the unemployment rate increased to 3.5%, primarily due to the sluggishness of the domestic economy. In 2015, the unemployment rate increased to 3.6%, primarily due to the continued sluggishness of the domestic economy. The unemployment rate was 4.3% in the first quarter of 2016.

From 1992 to 2009, the economically active population of the Republic increased by approximately 24.8% to 24.3 million, while the number of employees increased by approximately 23.7% to 23.5 million. The economically active population over 15 years old as a percentage of the total over-15 population has remained between 60% and 63% over the past decade. Literacy among workers under 50 is almost universal. As of December 31, 2015, the economically active population of the Republic was 26.9 million and the number of employees was 25.9 million.

The following table shows selected employment information by industry and by gender:

	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>
	(all figures in percentages, except as indicated)				
Labor force (in thousands of persons)	24,244	24,681	25,066	25,599	25,936
Employment by Industry:					
Agriculture, Forestry and Fishing	6.4	6.2	6.1	5.7	5.2
Mining and Manufacturing	16.9	16.7	16.8	17.0	17.4
S.O.C & Services	76.7	77.1	77.2	77.4	77.5
Electricity, Transport, Communication and Finance	12.2	12.1	12.2	11.9	11.8
Business, Private & Public Service and Other					
Services	34.6	35.1	35.5	35.5	35.6
Construction	7.2	7.2	7.0	7.0	7.0
Wholesale & Retail Trade, Hotels and Restaurants	22.7	22.7	22.5	23.0	23.0
Total Employed	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>
Employment by Gender:					
Male	58.4	58.3	58.1	58.0	57.7
Female	41.6	41.7	41.9	42.0	42.3
Total Employed	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>

Source: The Bank of Korea

As of July 1, 2004, the Republic adopted a five-day workweek for large corporations with over 1,000 employees, publicly-owned (state-run) companies, banks and insurance companies, reducing working hours from 44 to 40 hours a week. The adoption of the five-day workweek has been extended to companies with over 300 employees and to government employees as of July 1, 2005 and to companies with over 100 employees as of July 1, 2006. Companies with more than 50 employees adopted the five-day workweek as of July 1, 2007 and those with over 20 adopted the five-day workweek as of July 1, 2008. Companies with less than 20 employees also adopted the five-day workweek on July 1, 2011.

Approximately 10.3% of the Republic's workers were unionized as of December 31, 2014. Labor unrest in connection with demands by unionized workers for better wages and working conditions and greater job security occur from time to time in the Republic. Some of the significant incidents in recent years include the following:

- In July 2011, unionized employees at Standard Chartered Korea (formerly, SC First Bank) engaged in a two-month strike, the longest in the Republic's banking sector, demanding that the bank scrap performance-related pay reforms.

- In June 2012, unionized taxi drivers went on their first nationwide strike demanding fare increases and protesting against increased fuel costs.
- In August 2012, unionized workers of Hyundai Motor Company went on a series of partial strikes demanding a higher bonus increase and the end of overnight shifts.
- In August 2013, unionized workers at Hyundai Motor Company and Kia Motors Corporation went on partial strikes demanding higher wages.
- In December 2013, unionized workers at the state owned Korea Railroad Corporation (“Korail”) went on strike against Korail’s plan to establish a separate company to operate a new bullet train line fearing that such plan would eventually lead to privatization of Korail and layoffs of existing workers.
- In November 2014, unionized workers at Hyundai Heavy Industries went on a series of partial strikes demanding higher wages.
- In April 2015, tens of thousands of members of the Korean Confederation of Trade Unions, which includes teacher and civil servant union groups, went on general strike demanding that the Government scrap its plans to reform the labor market and pension program for public workers.

Actions such as these by labor unions may hinder implementation of the labor reform measures and disrupt the Government’s plans to create a more flexible labor market. Although much effort is being expended to resolve labor disputes in a peaceful manner, there can be no assurance that further labor unrest will not occur in the future. Continued labor unrest in key industries of the Republic may have an adverse effect on the economy.

In 1997, the Korean Confederation of Trade Unions organized a political alliance, which led to the formation of the Democratic Labor Party in January 2000. The Democratic Labor Party merged with The New People’s Participation Party and changed its name to The Unified Progressive Party (“UPP”) in December 2011. In October 2012, the UPP split and seven UPP members of the National Assembly and their supporters formed a new party, the Progressive Justice Party, which changed its name to the Justice Party in July 2013. In December 2014, the Constitutional Court ordered the dissolution of the UPP and the removal of the party’s five lawmakers from the National Assembly for violating the Republic’s Constitution after certain of its members were convicted of trying to instigate an armed rebellion and supporting North Korea. In the legislative general election held on April 13, 2016, the Justice Party won six seats in the National Assembly, and the members-elect will begin their four-year terms on May 30, 2016.

The Financial System

Structure of the Financial Sector

The Republic’s financial sector includes the following categories of financial institutions:

- The Bank of Korea;
- banking institutions;
- non-bank financial institutions; and
- other financial entities, including:
 - financial investment companies;
 - credit guarantee institutions;
 - venture capital companies; and
 - miscellaneous others.

To increase transparency in financial transactions and enhance the integrity and efficiency of the financial markets, Korean law requires that financial institutions confirm that their clients use their real names when

transacting business. To ease the liquidity crisis, the Government altered the real-name financial transactions system during 1998, to allow the sale or deposit of foreign currencies through domestic financial institutions and the purchase of certain bonds, including Government bonds, without identification. The Government also strengthened confidentiality protection for private financial transactions.

In July 2007, the Korean National Assembly passed the Financial Investment Services and Capital Markets Act or FSCMA, under which various industry-based capital markets regulatory systems currently were consolidated into a single regulatory system. The FSCMA, which became effective in February 2009, expands the scope of permitted investment-related financial products and activities through expansive definitions of financial instruments and function-based regulations that allow financial investment companies to offer a wider range of financial services, as well as strengthening investor protection and disclosure requirements.

Prior to the effective date of the Financial Investment Services and Capital Markets Act, separate laws regulated various types of financial institutions depending on the type of the financial institution (for example, securities companies, futures companies, trust business companies and asset management companies) and subjected financial institutions to different licensing and ongoing regulatory requirements (for example, under the Securities and Exchange Act, the Futures Business Act and the Indirect Investment Asset Management Business Act). By applying one uniform set of rules to financial businesses having the same economic function, the Financial Investment Services and Capital Markets Act attempts to improve and address issues caused by the previous regulatory system under which the same economic function relating to capital markets-related business were governed by multiple regulations. To this end, the Financial Investment Services and Capital Markets Act categorizes capital markets-related businesses into six different functions, as follows:

- investment dealing (trading and underwriting of financial investment products);
- investment brokerage (brokerage of financial investment products);
- collective investment (establishment of collective investment schemes and the management thereof);
- investment advice;
- discretionary investment management; and
- trusts (together with the five businesses set forth above, “Financial Investment Businesses”).

Accordingly, all financial businesses relating to financial investment products are reclassified as one or more of the Financial Investment Businesses described above, and financial institutions are subject to the regulations applicable to their relevant Financial Investment Businesses, irrespective of what type of financial institution it is. For example, under the Financial Investment Services and Capital Markets Act, derivative businesses conducted by securities companies and future companies will be subject to the same regulations under the Financial Investment Services and Capital Markets Act, at least in principle.

The banking business and the insurance business are not subject to the Financial Investment Services and Capital Markets Act and will continue to be regulated under separate laws; provided, however, that they are subject to the Financial Investment Services and Capital Markets Act if their activities involve any Financial Investment Businesses requiring a license based on the Financial Investment Services and Capital Markets Act.

Banking Industry

The banking industry comprises commercial banks and specialized banks. Commercial banks serve the general public and corporate sectors. They include nationwide banks, regional banks and branches of foreign banks. Regional banks provide services similar to nationwide banks, but operate in a geographically restricted region. Branches of foreign banks have operated in the Republic since 1967 but provide a relatively small proportion of the country’s banking services. As of December 31, 2015, there were six nationwide banks, six regional banks and 42 foreign banks with branches operating in the Republic.

Specialized banks meet the needs of specific sectors of the economy in accordance with Government policy; they are organized under, or chartered by, special laws. Specialized banks include:

- The Korea Development Bank;
- The Export-Import Bank of Korea;
- The Industrial Bank of Korea;
- National Federation of Fisheries Cooperatives; and
- NH Bank.

The economic difficulties in 1997 and 1998 caused an increase in Korean banks' non-performing assets and a decline in capital adequacy ratios of Korean banks. From 1998 through 2002, the Financial Services Commission amended banking regulations several times to adopt more stringent criteria for non-performing assets that more closely followed international standards. Non-performing assets are assets classified as doubtful or estimated loss under Korean banking regulations.

The following table sets out the total loans (including loans in Won and loans in foreign currencies) and non-performing assets of Korean banks.

	Total Loans	Non-Performing Assets ⁽¹⁾	Percentage of Total
	(trillions of won)	(trillions of won)	(percentage)
December 31, 2011	1,387.6	18.8	1.4
December 31, 2012	1,390.9	18.5	1.3
December 31, 2013	1,441.6	25.7	1.8
December 31, 2014	1,557.9	24.2	1.6
December 31, 2015	1,664.3	28.5	1.7

Note:

(1) Assets classified as substandard or below.

Source: Financial Supervisory Service.

As of December 31, 2014, loans denominated in Won held by these banks increased by 8.0% to ₩1,255.8 trillion from ₩1,162.8 trillion as of December 31, 2013, primarily due to (i) an increase in household loans by 8.2% to ₩518.2 trillion as of December 31, 2014 from ₩479.0 trillion as of December 31, 2013, (ii) an increase in loans to small and medium-enterprises by 6.8% to ₩522.4 trillion as of December 31, 2014 from ₩489.0 trillion as of December 31, 2013 and (iii) an increase in loans to large corporations by 10.5% to ₩183.5 trillion as of December 31, 2014 from ₩166.1 trillion as of December 31, 2013. Based on preliminary data, as of December 31, 2015, loans denominated in Won held by these banks increased by 16.3% to ₩1,352.9 trillion from ₩1,162.8 trillion as of December 31, 2014, primarily due to (i) an increase in household loans by 8.6% to ₩562.8 trillion as of December 31, 2015 from ₩518.2 trillion as of December 31, 2014 and (ii) an increase in loans to small and medium-enterprises by 10.4% to ₩576.6 trillion as of December 31, 2015 from ₩522.4 trillion as of December 31, 2014.

In 2011, these banks posted an aggregate net profit of ₩11.8 trillion, compared to an aggregate net profit of ₩9.3 trillion in 2010, primarily due to decreased non-performing loans. In 2012, these banks posted an aggregate net profit of ₩8.7 trillion, compared to an aggregate net profit of ₩11.8 trillion in 2011, primarily due to a decrease in gain on sale of equity securities and an increase in impairment loss on available-for-sale securities. In 2013, these banks posted an aggregate net profit of ₩3.9 trillion, compared to an aggregate net profit of ₩8.7 trillion in 2012, primarily due to decreased net interest income and increased loan loss provisions. In 2014, these banks posted an aggregate net profit of ₩6.0 trillion, compared to an aggregate net profit of ₩3.9 trillion in 2013, primarily due to decreased loan loss provisions. Based on preliminary data, in 2015, these banks posted an aggregate net profit of ₩3.5 trillion, compared to an aggregate net profit of ₩6.0 trillion in 2014, primarily due to increased loan loss provisions.

Non-Bank Financial Institutions

Non-bank financial institutions include:

- savings institutions, including trust accounts of banks, mutual savings banks, credit unions, mutual credit facilities, community credit cooperatives and postal savings;
- life insurance institutions; and
- credit card companies.

As of December 31, 2015, 79 mutual savings banks, 23 life insurance institutions, which includes joint venture life insurance institutions and wholly-owned subsidiaries of foreign life insurance companies, and eight credit card companies operated in the Republic.

Money Markets

In the Republic, the money markets consist of the call market and markets for a wide range of other short-term financial instruments, including treasury bills, monetary stabilization bonds, negotiable certificates of deposits, repurchase agreements and commercial paper.

Securities Markets

On January 27, 2005, the Korea Exchange was established pursuant to the now repealed Korea Securities and Futures Exchange Act by consolidating the Korea Stock Exchange, the Korea Futures Exchange, the KOSDAQ Stock Market, Inc., or the KOSDAQ, and the KOSDAQ Committee of the Korea Securities Dealers Association, which had formerly managed the KOSDAQ. There are three major markets operated by the Korea Exchange: the KRX KOSPI Market, the KRX KOSDAQ Market, and the KRX Derivatives Market. The Korea Exchange has two trading floors located in Seoul, one for the KRX KOSPI Market and one for the KRX KOSDAQ Market, and one trading floor in Busan for the KRX Derivatives Market. The Korea Exchange is a joint stock company with limited liability, the shares of which are held by (i) financial investment companies that were formerly members of the Korea Futures Exchange or the Korea Stock Exchange and (ii) the stockholders of the KOSDAQ. Currently, the Korea Exchange is the only stock exchange in Korea and is operated by membership, having as its members Korean financial investment companies and some Korean branches of foreign financial investment companies.

The Korea Exchange publishes the Korea Composite Stock Price Index every ten seconds, which is an index of all equity securities listed on the Korea Exchange. The Korea Composite Stock Price Index is computed using the aggregate value method, whereby the market capitalizations of all listed companies are aggregated, subject to certain adjustments, and this aggregate is expressed as a percentage of the aggregate market capitalization of all listed companies as of the base date, January 4, 1980.

The following table shows the value of the Korea Composite Stock Price Index as of the dates indicated:

December 30, 2010	2,051.0	October 31, 2013	2,030.1
January 31, 2011	2,069.7	November 29, 2013	2,044.9
February 28, 2011	1,939.3	December 30, 2013	2,011.3
March 31, 2011	2,106.7	January 29, 2014	1,941.2
April 30, 2011	2,192.4	February 28, 2014	1,980.0
May 31, 2011	2,142.5	March 31, 2014	1,985.6
June 30, 2011	2,100.7	April 30, 2014	1,961.8
July 29, 2011	2,133.2	May 30, 2014	1,995.0
August 31, 2011	1,880.1	June 30, 2014	2,002.2
September 30, 2011	1,769.7	July 31, 2014	2,076.1
October 31, 2011	1,909.0	August 29, 2014	2,068.5
November 30, 2011	1,847.5	September 30, 2014	2,020.1
December 29, 2011	1,825.7	October 31, 2014	1,964.4
January 31, 2012	1,955.8	November 28, 2014	1,980.8
February 29, 2012	2,030.3	December 31, 2014	1,915.6
March 31, 2012	2,014.0	January 30, 2015	1,949.3
April 30, 2012	1,982.0	February 27, 2015	1,985.8
May 31, 2012	1,843.5	March 31, 2015	2,041.0
June 29, 2012	1,854.0	April 30, 2015	2,127.2
July 31, 2012	1,882.0	May 29, 2015	2,114.8
August 31, 2012	1,905.1	June 30, 2015	2,074.2
September 28, 2012	1,996.2	July 31, 2015	2,030.2
October 31, 2012	1,912.1	August 29, 2015	1,941.5
November 30, 2012	1,932.9	September 30, 2015	1,962.8
December 28, 2012	1,997.1	October 30, 2015	2,029.5
January 31, 2013	1,961.9	November 30, 2015	1,992.0
February 28, 2013	2,026.5	December 30, 2015	1,960.3
March 29, 2013	2,004.9	January 29, 2016	1,912.1
April 30, 2013	1,964.0	February 29, 2016	1,916.7
May 30, 2013	2,001.1	March 31, 2016	1,995.8
June 28, 2013	1,863.3	April 29, 2016	1,994.2
July 31, 2013	1,914.0	May 31, 2016	1,983.4
August 30, 2013	1,926.4	June 30, 2016	1,970.4
September 30, 2013	1,997.0	July 29, 2016	2,016.2

On December 27, 1997, the last day of trading in 1997, the index stood at 376.3, a sharp decline from 647.1 on September 30, 1997. The fall resulted from growing concerns about the Republic's weakening financial and corporate sectors, the Republic's falling foreign currency reserves, the sharp depreciation of the Won against the U.S. Dollar and other external factors, such as a sharp decline in stock prices in Hong Kong on October 24, 1997 and financial turmoil in Southeast Asian countries. The Korea Composite Stock Price Index recovered to reach 2,064.9 in late 2007 but since then the index declined. As liquidity and credit concerns and volatility in the global financial markets increased significantly since September 2008, there was a significant overall decline in the stock prices of Korean companies during the fourth quarter of 2008 and first half of 2009 and continuing volatility since then. The index was 2,056.2 on August 19, 2016.

Supervision System

The Office of Bank Supervision, the Securities Supervisory Board, the Insurance Supervisory Board and all other financial sector regulatory bodies merged in January 1999 to form the Financial Services Commission. The Financial Services Commission acts as the executive body over the Financial Supervisory Service. The Financial Services Commission reports to, but operates independently of, the Prime Minister's office.

The Ministry of Strategy and Finance focuses on financial policy and foreign currency regulations. The Bank of Korea manages monetary policy focusing on price stabilization.

Deposit Insurance System

The Republic's deposit insurance system insures amounts on deposit with banks, non-bank financial institutions, securities companies and life insurance companies. Since January 2001, deposits at any single financial institution are insured only up to ₩50 million per person regardless of the amount deposited.

The Government excluded certain deposits, such as repurchase agreements, from the insurance scheme, expanded the definition of unsound financial institutions to which the insurance scheme would apply and gradually increased the insurance premiums payable by insured financial institutions.

Monetary Policy

The Bank of Korea

The Bank of Korea was established in 1950 as Korea's central bank and the country's sole currency issuing bank. A seven-member Monetary Policy Committee, chaired by the Governor of The Bank of Korea, formulates and controls monetary and credit policies.

Inflation targeting is the basic system of operation for Korean monetary policy. The consumer price index is used as The Bank of Korea's target indicator. To achieve its established inflation target, the Monetary Policy Committee of The Bank of Korea determines and announces the "Bank of Korea Base Rate," the reference rate applied in transactions such as repurchase agreements between The Bank of Korea and its financial institution counterparts. The Bank of Korea uses open market operations as its primary instrument to keep the call rate in line with the Monetary Policy Committee's target rate. In addition, The Bank of Korea is able to establish policies regarding its lending to banks in Korea and their reserve requirements.

Interest Rates

On July 12, 2007, The Bank of Korea raised the policy rate to 4.75% from 4.5%, and raised it further to 5.0% on August 9, 2007. The rationale for this change was the concern that the ample market liquidity might put upside pressure on inflation in the medium to long term as the economic upswing continued. On August 7, 2008, The Bank of Korea raised the policy rate to 5.25% from 5.0%, taking the view that inflation in consumer prices had picked up its pace, due to the direct and indirect effects of high oil prices, at a time when domestic economic activity had slackened. On October 9, 2008, The Bank of Korea cut its policy rate to 5.0% from 5.25%, and continued to lower it further to 4.25% on October 27, 2008, 4.0% on November 7, 2008, 3.0% on December 11, 2008, 2.5% on January 9, 2009 and 2.0% on February 12, 2009, in order to address financial market instability and to help combat the slowdown of the domestic economy. On July 9, 2010, The Bank of Korea raised the policy rate to 2.25% from 2.0%, which was further raised to 2.5% on November 16, 2010, in response to signs of inflationary pressures and the continued growth of domestic economy. On January 13, 2011, The Bank of Korea raised the policy rate to 2.75%, which was further increased to 3.0% on March 10, 2011 and to 3.25% on June 10, 2011, in response to inflationary pressures driven mainly by rises in the prices of petroleum products and farm products. The Bank of Korea lowered its policy rate to 3.0% from 3.25% on July 12, 2012, which was further lowered to 2.75% on October 11, 2012, 2.5% on May 9, 2013, 2.25% on August 14, 2014, 2.0% on October 15, 2014, 1.75% on March 12, 2015, 1.5% on June 11, 2015 and 1.25% on June 9, 2016, in order to address the sluggishness of the global and domestic economy.

With the deregulation of interest rates on banks' demand deposits on February 2, 2004, The Bank of Korea completed the interest rate deregulation based upon the "Four-Stage Interest Rate Liberalization Plan" announced in 1991. The prohibition on the payment of interest on ordinary checking accounts was, however, maintained.

Money Supply

The following table shows the volume of the Republic's money supply:

	December 31,				
	2011	2012	2013	2014	2015
	(billions of Won)				
Money Supply (M1) ⁽¹⁾	442,077.5	470,010.6	515,643.4	585,822.6	708,452.9
Quasi-money ⁽²⁾	1,309,380.9	1,365,631.0	1,405,151.6	1,491,411.4	1,538,922.1
Money Supply (M2) ⁽³⁾	1,751,458.4	1,835,641.6	1,920,795.0	2,077,234.0	2,247,375.0
Percentage Increase Over Previous					
Year	5.5%	4.8%	4.6%	8.1%	8.2%

Notes:

- (1) Consists of currency in circulation and demand and instant access savings deposits at financial institutions.
- (2) Includes time and installment savings deposits, marketable instruments, yield-based dividend instruments and financial debentures, excluding financial instruments with a maturity of more than two years.
- (3) Money Supply (M2) is the sum of Money Supply (M1) and quasi-money.

Source: The Bank of Korea.

Exchange Controls

Authorized foreign exchange banks, as registered with the Ministry of Strategy and Finance, handle foreign exchange transactions. The ministry has designated other types of financial institutions to handle foreign exchange transactions on a limited basis.

Korean laws and regulations generally require a report to either the Ministry of Strategy and Finance, The Bank of Korea or authorized foreign exchange banks, as applicable, for issuances of international bonds and other instruments, overseas investments and certain other transactions involving foreign exchange payments.

In 1994 and 1995, the Government relaxed regulations of foreign exchange position ceilings and foreign exchange transaction documentation and created free Won accounts which may be opened by non-residents at Korean foreign exchange banks. The Won funds deposited into the free Won accounts may be converted into foreign currencies and remitted outside Korea without any governmental approval. In December 1996, after joining the OECD, the Republic freed the repatriation of investment funds, dividends and profits, as well as loan repayments and interest payments. The Government continues to reduce exchange controls in response to changes in the world economy, including the new trade regime under the WTO, anticipating that such foreign exchange reform will improve the Republic's competitiveness and encourage strategic alliances between domestic and foreign entities.

In September 1998, the National Assembly passed the Foreign Exchange Transactions Act, which became effective in April 1999 and has subsequently been amended numerous times. In principle, most currency and capital transactions, including, among others, the following transactions, have been liberalized:

- the investment in real property located overseas by Korean companies and financial institutions;
- the establishment of overseas branches and subsidiaries by Korean companies and financial institutions;
- the investment by non-residents in deposits and trust products having more than one year maturities; and
- the issuance of debentures by non-residents in the Korean market.

To minimize the adverse effects from further opening of the Korean capital markets, the Ministry of Strategy and Finance is authorized to introduce a variable deposit requirement system to restrict the influx of short-term speculative funds.

The Government has also embarked on a second set of liberalization initiatives starting in January 2001, under which ceilings on international payments for Korean residents have been eliminated, including overseas travel expenses, overseas inheritance remittances and emigration expenses. Overseas deposits, trusts, acquisitions of foreign securities and other foreign capital transactions made by residents and the making of deposits in Korean currency by non-residents have also been liberalized. In line with the foregoing liberalization, measures will also be adopted to curb illegal foreign exchange transactions and to stabilize the foreign exchange market.

Effective as of January 1, 2006, the Government liberalized the regulations governing “capital transactions.” The regulations provide that no regulatory approvals are required for any capital transactions. The capital transactions previously subject to approval requirements are now subject only to reporting requirements.

In January 2010, the Financial Supervisory Services released *FX Derivative Transactions Risk Management Guideline* to prevent over-hedging of foreign exchange risk by corporate investors. According to the guideline as amended in July 2010, if a corporate investor, other than a financial institution or a public enterprise, wishes to enter into a foreign exchange forward, option or swap agreement with a bank, the bank is required to verify whether the corporate investor’s assets, liabilities or contracts face foreign exchange risks that could be mitigated by a foreign exchange forward, option or swap agreement. In addition, the bank is required to ensure that the corporate investor’s risk hedge ratio, which is the ratio of the aggregate notional amount to the aggregate amount of risk, does not exceed 100%.

Foreign Exchange

The following table shows the exchange rate between the Won and the U.S. Dollar (in Won per U.S. Dollar) as announced by the Seoul Money Brokerage Services, Ltd. as of the dates indicated:

	<u>Won/U.S. Dollar Exchange Rate</u>		<u>Won/U.S. Dollar Exchange Rate</u>
December 30, 2010	1,138.9	October 31, 2013	1,061.4
January 31, 2011	1,114.3	November 29, 2013	1,062.1
February 28, 2011	1,127.9	December 31, 2013	1,055.3
March 31, 2011	1,107.2	January 29, 2014	1,079.2
April 29, 2011	1,072.3	February 28, 2014	1,067.7
May 31, 2011	1,080.6	March 31, 2014	1,068.8
June 30, 2011	1,078.1	April 30, 2014	1,031.7
July 29, 2011	1,052.6	May 30, 2014	1,021.6
August 31, 2011	1,071.7	June 30, 2014	1,014.4
September 30, 2011	1,179.5	July 31, 2014	1,024.3
October 31, 2011	1,104.9	August 29, 2014	1,013.6
November 30, 2011	1,150.3	September 30, 2014	1,059.6
December 30, 2011	1,153.3	October 31, 2014	1,054.0
January 31, 2012	1,125.0	November 28, 2014	1,101.1
February 29, 2012	1,126.5	February 28, 2014	1,067.7
March 30, 2012	1,137.8	December 31, 2014	1,099.2
April 30, 2012	1,134.2	January 30, 2015	1,090.8
May 31, 2012	1,177.8	February 27, 2015	1,099.2
June 29, 2012	1,153.8	March 31, 2015	1,105.0
July 31, 2012	1,136.2	April 30, 2015	1,068.1
August 31, 2012	1,134.6	May 29, 2015	1,108.0
September 28, 2012	1,118.6	June 30, 2015	1,124.1
October 31, 2012	1,094.1	July 31, 2015	1,166.3
November 30, 2012	1,084.7	August 31, 2015	1,176.3
December 31, 2012	1,071.1	September 30, 2015	1,194.5
January 31, 2013	1,082.7	October 30, 2015	1,142.3
February 28, 2013	1,085.4	November 30, 2015	1,150.4
March 29, 2013	1,112.1	December 31, 2015	1,172.0
April 30, 2013	1,108.1	January 29, 2016	1,208.4
May 31, 2013	1,128.3	February 29, 2016	1,235.4
June 28, 2013	1,149.7	March 31, 2016	1,153.5
July 31, 2013	1,113.6	April 29, 2016	1,143.9
August 30, 2013	1,110.9	May 31, 2016	1,190.6
September, 30, 2013	1,075.6	June 30, 2016	1,164.7
		July 29, 2016	1,125.7

Prior to November 1997, the Government had permitted exchange rates to float within a daily range of 2.25%. In response to the substantial downward pressures on the Won caused by the Republic's economic difficulties in late 1997, in November 1997, the Government expanded the range of permitted daily exchange rate fluctuations to 10%. The Government eliminated the daily exchange rate band in December 1997, and the Won now floats according to market forces. The value of the Won relative to the U.S. dollar depreciated from ₩888.1 to US\$1.00 on June 30, 1997 to ₩1,964.8 to US\$1.00 on December 24, 1997. Due to improved economic conditions and increases in trade surplus, the Won has generally appreciated against the U.S. dollar, although the trend reversed in March 2008. During the period from January 2, 2008 through April 16, 2009, the value of the Won relative to the U.S. dollar declined by approximately 29.9%, due primarily to adverse economic conditions resulting from liquidity and credit concerns and volatility in the global credit and financial markets and repatriations by foreign investors of their investments in the Korean stock market. The market average exchange rate was ₩1,106.4 to US\$1.00 on August 19, 2016.

Balance of Payments and Foreign Trade

Balance of Payments

Balance of payments figures measure the relative flow of goods, services and capital into and out of the country as represented in the current balance and the capital balance. The current balance tracks a country's trade in goods and services and transfer payments and measures whether a country is living within its income from trading and investments. The capital balance covers all transactions involving the transfer of capital into and out of the country, including loans and investments. The overall balance represents the sum of the current and capital balances. An overall balance surplus indicates a net inflow of foreign currencies, thereby increasing demand for and strengthening the local currency. An overall balance deficit indicates a net outflow of foreign currencies, thereby decreasing demand for and weakening the local currency. The financial account mirrors the overall balance. If the overall balance is positive, the surplus, which represents the nation's savings, finances the overall deficit of the country's trading partners. Accordingly, the financial account will indicate cash outflows equal to the overall surplus. If, however, the overall balance is negative, the nation has an international deficit which must be financed. Accordingly, the financial account will indicate cash inflows equal to the overall deficit.

The following table sets out certain information with respect to the Republic's balance of payments:

Balance of Payments ⁽¹⁾

<u>Classification</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015 ⁽⁴⁾</u>
	(millions of dollars)				
Current Account	18,655.8	50,835.0	81,148.2	84,373.0	105,955.1
Goods	29,089.9	49,406.0	82,781.0	88,885.4	120,374.1
Exports ⁽²⁾	587,099.7	603,509.2	618,156.9	613,020.6	548,933.3
Imports ⁽²⁾	558,009.8	554,103.2	535,375.9	524,135.2	428,559.2
Services	(12,279.1)	(5,213.6)	(6,499.2)	(3,678.5)	(15,707.9)
Income	6,560.6	12,116.7	9,055.7	4,150.8	5,901.8
Current Transfers	(4,715.6)	(5,474.1)	(4,189.3)	(4,984.7)	(4,612.9)
Capital and Financial Account	(24,203.8)	51,540.7	80,077.6	89,325.1	109,562.1
Capital Account	(112.0)	(41.7)	(27.0)	(8.9)	(64.7)
Financial Account ⁽³⁾	24,315.8	51,582.4	80,104.6	89,334.0	109,626.8
Net Errors and Omissions	5,772.0	789.1	(1,016.6)	4,969.9	3,736.4

Notes:

- (1) Figures are prepared based on the sixth edition of Balance of Payment Manual, or BPM6, published by International Monetary Fund in December 2010 and implemented by the Government in December 2013.
- (2) These entries are derived from trade statistics and are valued on a free on board basis, meaning that the insurance and freight costs are not included.
- (3) Includes borrowings from the IMF, syndicated bank loans and short-term borrowings.
- (4) Preliminary.

Source: The Bank of Korea.

The Republic recorded a current account surplus of approximately US\$84.4 billion in 2014. The current account surplus in 2014 increased from the current account surplus of US\$81.1 billion in 2013, primarily due to an increase in surplus from the goods account.

Based on preliminary data, the Republic recorded a current account surplus of approximately US\$106.0 billion in 2015. The current account surplus in 2015 increased from the current account surplus of US\$84.4 billion in 2014, primarily due to an increase in surplus from the goods account which more than offset an increase in deficit from the services account. Based on preliminary data, the Republic recorded a current account surplus of approximately US\$24.1 billion in the first quarter of 2016. The current account surplus in the first quarter of 2016 increased from the current account surplus of US\$22.4 billion in the corresponding period of 2015, primarily due to an increase in surplus from the goods account.

Foreign Direct Investment

Since 1960, the Government has adopted a broad range of related laws, administrative rules and regulations, providing a framework for the conduct and regulation of foreign investment activities. In September 1998, the Government promulgated the Foreign Investment Promotion Act, or the FIPA, which replaced previous foreign direct investment related laws, rules and regulations, to promote inbound foreign investments by providing incentives to, and facilitating investment activities in the Republic by, foreign nationals. The FIPA prescribes, among others, procedural requirements for inbound foreign investments, incentives for foreign investments such as tax reductions, and requirements relating to designation and development of foreign investment target regions. The Government believes that providing a stable and receptive environment for foreign direct investment will accelerate the inflow of foreign capital, technology and management techniques.

The following table sets forth information regarding annual foreign direct investment in the Republic for the periods indicated.

	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>
	<u>(billions of dollars)</u>				
Contracted and Reported Investment					
Greenfield Investment ⁽¹⁾	11.7	12.5	9.6	11.0	14.1
Merger & Acquisition	2.0	3.8	5.0	8.0	6.8
Total	<u>13.7</u>	<u>16.3</u>	<u>14.5</u>	<u>19.0</u>	<u>20.9</u>
Actual Investment	6.6	10.7	9.8	12.1	16.3 ⁽²⁾

Notes:

(1) Includes building new factories and operational facilities.

(2) Preliminary.

Source: Ministry of Trade, Industry and Energy

In 2015, the contracted and reported amount of foreign direct investment in the Republic increased to US\$20.9 billion from US\$19.0 billion in 2014, primarily due to an increase in foreign investment in the service sector to US\$14.7 billion in 2015 from US\$11.2 billion in 2014 which more than offset a decrease in foreign investment in the manufacturing sector to US\$4.6 billion in 2015 from US\$7.6 billion in 2014.

The following table sets forth information regarding the source of foreign direct investment by region and country for the periods indicated:

Foreign Direct Investment by Region and Country

	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>
	(billions of dollars)				
North America					
U.S.A	2.4	3.7	3.5	3.6	5.5
Others	<u>1.3</u>	<u>0.7</u>	<u>1.1</u>	<u>1.4</u>	<u>2.9</u>
	3.7	4.4	4.6	5.0	8.4
Asia					
Japan	2.3	4.5	2.7	2.5	1.7
Hong Kong	0.6	1.7	1.0	1.1	1.5
Singapore	0.6	1.4	0.4	1.7	2.5
China	0.7	0.7	0.5	1.2	2.0
Others	<u>0.2</u>	<u>0.5</u>	<u>0.4</u>	<u>0.3</u>	<u>0.7</u>
	4.4	8.8	5.0	6.8	8.4
European Union					
England	0.9	0.4	0.1	0.4	0.3
Netherlands	1.0	0.6	0.6	2.4	0.5
Germany	1.5	0.4	0.4	0.2	0.5
France	0.2	0.2	0.5	0.2	0.1
Luxembourg	0.1	0.2	0.7	1.9	0.2
Others	<u>1.7</u>	<u>1.2</u>	<u>2.6</u>	<u>1.6</u>	<u>1.1</u>
	5.4	3.0	4.9	6.7	2.7
Others regions and countries	<u>0.2</u>	<u>0.1</u>	<u>0.0</u>	<u>0.5</u>	<u>1.4</u>
Total	<u><u>13.7</u></u>	<u><u>16.3</u></u>	<u><u>14.5</u></u>	<u><u>19.0</u></u>	<u><u>20.9</u></u>

Source: Ministry of Trade, Industry and Energy

Trade Balance

Trade balance figures measure the difference between a country's exports and imports. If exports exceed imports the country has a trade balance surplus while if imports exceed exports the country has a deficit. A deficit, indicating that a country's receipts from abroad fall short of its payments to foreigners, must be financed, rendering the country a debtor nation. A surplus, indicating that a country's receipts exceed its payments to foreigners, allows the country to finance its trading partners' net deficit to the extent of the surplus, rendering the country a creditor nation.

The following table summarizes the Republic's trade balance for the periods indicated:

	<u>Exports</u> ⁽¹⁾	<u>As % of GDP</u> ⁽²⁾	<u>Imports</u> ⁽³⁾	<u>As % of GDP</u> ⁽²⁾	<u>Balance of Trade</u>	<u>Exports as % of Imports</u>
	(billions of dollars, except percentages)					
2011	555.2	46.9%	524.4	44.3%	30.8	105.8
2012	547.9	46.0%	519.6	43.6%	28.3	105.4
2013	559.6	44.4%	515.6	40.9%	44.0	108.5
2014	572.7	44.1%	525.5	40.5%	47.2	109.0
2015 ⁽⁴⁾	526.9	42.2%	436.6	35.0%	90.3	120.7

Notes:

- (1) These entries are derived from customs clearance statistics on a C.I.F. basis, meaning that the price of goods include insurance and freight cost.
- (2) At chained 2010 year prices.
- (3) These entries are derived from customs clearance statistics on a C.I.F. basis, meaning that the price of goods include insurance and freight cost.
- (4) Preliminary.

Source: The Bank of Korea; Korea Customs Service.

The Republic, due to its lack of natural resources, relies on extensive trading activity for growth. The country meets virtually all domestic requirements for petroleum, wood and rubber with imports, as well as much of its coal and iron needs. Exports consistently represent a high percentage of GDP and, accordingly, the international economic environment is of crucial importance to the Republic's economy.

The following tables give information regarding the Republic's exports and imports by major commodity groups:

Exports by Major Commodity Groups (C.I.F.) ⁽¹⁾

	As % of 2011		As % of 2012		As % of 2013		As % of 2014		As % of 2015 ⁽²⁾	
	2011	Total	2012	Total	2013	Total	2014	Total	2015 ⁽²⁾	Total ⁽²⁾
(billions of dollars, except percentages)										
Foods & Consumer Goods	6.5	1.2	6.8	1.2	6.7	1.1	7.0	1.2	6.8	1.3
Raw Materials and Fuels	61.7	11.1	65.4	11.9	61.2	10.9	59.2	10.3	39.5	7.5
Petroleum & Derivatives	52.0	9.4	56.6	10.3	53.2	9.5	51.2	8.9	32.4	6.1
Others	9.7	1.7	8.8	1.6	8.0	1.4	8.0	1.4	7.1	1.3
Light Industrial Products	38.9	7.0	40.5	7.4	39.0	6.9	38.6	6.7	35.4	6.7
Heavy & Chemical Industrial Products . . .	448.0	80.7	435.2	79.3	452.8	77.8	467.9	81.7	445.1	84.5
Electronic & Electronic Products . . .	156.9	28.3	156.0	28.5	171.2	30.6	174.4	30.5	170.5	32.4
Chemicals & Chemical Products	59.1	10.6	59.6	10.9	64.4	11.5	65.6	11.5	55.9	10.6
Metal Goods	48.6	8.8	47.2	8.6	43.6	7.8	47.5	8.3	41.4	7.9
Machinery & Precision										
Equipment	54.5	9.8	55.7	10.2	55.3	9.9	57.9	10.1	57.4	10.9
Transport Equipment	124.7	22.5	112.1	20.5	113.1	20.2	116.5	20.3	112.8	21.4
Passenger Cars	40.9	7.4	42.4	7.7	44.3	7.9	44.8	7.8	41.8	7.9
Ship & Boat	54.6	9.8	38.2	7.0	36.2	6.5	38.7	6.8	38.8	7.4
Others	29.2	5.3	31.5	5.7	32.6	5.8	33.0	5.8	32.2	6.1
Others	4.2	0.8	4.6	0.8	5.2	0.9	6.0	1.0	7.1	1.3
Total	<u>555.2</u>	<u>100.0</u>	<u>547.9</u>	<u>100.0</u>	<u>559.6</u>	<u>100.0</u>	<u>572.7</u>	<u>100.0</u>	<u>526.9</u>	<u>100.0</u>

Notes:

(1) These entries are derived from customs clearance statistics. C.I.F. means that the price of goods includes insurance and freight costs.

(2) Preliminary

Source: The Bank of Korea; Korea Customs Service.

Imports by Major Commodity Groups (C.I.F.) ⁽¹⁾

	As % of 2011		As % of 2012		As % of 2013		As % of 2014		As % of 2015 ⁽²⁾	
	2011	Total	2012	Total	2013	Total	2014	Total	2015 ⁽²⁾	Total ⁽²⁾
(billions of dollars, except percentages)										
Industrial Materials and Fuels	324.8	61.9	325.1	62.6	313.8	60.9	311.2	59.2	219.1	50.2
Crude Petroleum	100.8	19.2	108.3	20.8	99.4	19.3	94.9	18.1	55.1	12.6
Mineral	31.1	5.9	28.3	5.4	24.7	4.8	24.6	4.7	17.6	4.0
Chemicals	44.2	8.4	43.8	8.4	43.2	8.4	43.9	8.4	39.6	9.1
Iron & Steel Products	30.4	5.8	26.4	5.1	24.6	4.8	27.0	5.1	21.2	4.9
Non-ferrous Metal	15.1	2.9	12.6	2.4	12.5	2.4	12.8	2.4	11.6	2.7
Others	103.2	19.7	105.7	20.3	109.4	21.2	108.0	20.5	74.0	16.9
Capital Goods	146.5	27.9	140.3	27.0	144.2	28.0	149.0	28.3	150.8	34.5
Machinery & Precision Equipment	50.5	9.6	49.8	9.6	50.1	9.7	50.8	9.7	49.1	11.2
Electric & Electronic Machines	80.1	15.3	76.3	14.7	80.9	15.7	84.5	16.1	87.5	20.0
Transport Equipment	13.9	2.7	12.1	2.3	11.3	2.2	11.6	2.2	12.4	2.8
Others	2.0	0.4	2.1	0.4	1.9	0.4	2.1	0.4	1.8	0.4
Consumer Goods	53.1	10.1	54.2	10.4	58.2	11.3	65.3	12.4	66.7	15.3
Cereals	7.5	1.4	7.9	1.5	8.5	1.6	7.9	1.5	6.9	1.6
Goods for Direct Consumption	15.0	2.9	14.3	2.8	14.5	2.8	16.7	3.2	17.1	3.9
Consumer Durable Goods	18.6	3.5	19.4	3.7	21.0	4.1	24.7	4.7	26.6	6.1
Consumer Nondurable Goods	12.1	2.3	12.6	2.4	14.3	2.8	16.0	3.0	16.1	3.7
Total	<u>524.4</u>	<u>100.0</u>	<u>519.6</u>	<u>100.0</u>	<u>515.6</u>	<u>100.0</u>	<u>525.5</u>	<u>100.0</u>	<u>436.6</u>	<u>100.0</u>

Notes:

(1) These entries are derived from customs clearance statistics. C.I.F. means that the price of goods includes insurance and freight costs.

(2) Preliminary.

Source: The Bank of Korea; Korea Customs Service.

In 2011, the Republic recorded a trade surplus of US\$30.8 billion. Exports increased by 19.0% to US\$555.2 billion in 2011 from US\$466.4 billion in 2010, primarily due to increased demand for mobile phones, consumer electronics products and automobiles from China and the emerging markets. Imports increased by 23.3% to US\$524.4 billion in 2011 from US\$425.2 billion in 2010, primarily due to an increase in oil and raw material prices.

In 2012, the Republic recorded a trade surplus of US\$28.3 billion. Exports decreased by 1.3% to US\$547.9 billion in 2012 from US\$555.2 billion in 2011, primarily due to adverse economic conditions in European countries. Imports decreased by 0.9% to US\$519.6 billion in 2012 from US\$524.4 billion in 2011, primarily due to decreased investment spending.

In 2013, the Republic recorded a trade surplus of US\$44.1 billion. Exports increased by 2.1% to US\$559.7 billion in 2013 from US\$547.9 billion in 2012, primarily due to increased demand for wireless communication devices, semiconductors and other information technology related products from the United States, China and the Southeast Asian nations. Imports decreased by 0.8% to US\$515.6 billion in 2013 from US\$519.6 billion in 2012, primarily due to decreased imports of oil, iron and steel.

Based on preliminary data, the Republic recorded a trade surplus of US\$47.2 billion in 2014. Exports increased by 2.3% to US\$572.7 billion in 2014 from US\$559.6 billion in 2013, primarily due to increased demand for semiconductors, wireless communication devices, iron and steel from the United States, the EU and the Southeast Asian nations. Imports increased by 1.9% to US\$525.5 billion in 2014 from US\$515.6 billion in 2013, primarily due to increased imports of cars, components for wireless communication devices and beef.

Based on preliminary data, the Republic recorded a trade surplus of US\$90.3 billion in 2015. Exports decreased by 8.7% to US\$526.9 billion in 2015 from US\$572.7 billion in 2014, primarily due to adverse global economic conditions. Imports decreased by 20.4% to US\$436.6 billion in 2015 from US\$525.5 billion of imports in 2014, primarily due to a decrease in oil prices, which also decreased unit prices of major raw materials. Based on preliminary data, the Republic recorded a trade surplus of US\$22.0 billion in the first quarter of 2016. Exports decreased by 13.3% to US\$115.6 billion and imports decreased by 16.3% to US\$93.6 billion from US\$133.4 billion of exports and US\$111.8 billion of imports, respectively, in the corresponding period of 2015.

The following table sets forth the Republic's exports trading partners:

Exports										
	2011	As % of 2011 Total	2012	As % of 2012 Total	2013	As % of 2013 Total	2014	As % of 2014 Total	2015 ⁽¹⁾	As % of 2015 Total ⁽¹⁾
(millions of dollars, except percentages)										
China	134,185.0	24.2	134,322.6	24.5	145,869.5	26.1	145,287.7	25.4	137,123.9	26.0
United States	56,207.7	10.1	58,524.6	10.7	62,052.5	11.1	70,284.9	12.3	69,832.1	13.3
Japan	39,679.7	7.1	38,796.1	7.1	34,662.3	6.2	32,183.8	5.6	25,576.5	4.9
Hong Kong	30,968.4	5.6	32,606.2	6.0	27,756.3	5.0	27,256.4	4.8	30,418.2	5.8
Singapore	20,839.0	3.8	22,887.9	4.2	22,289.0	4.0	23,749.9	4.1	15,011.2	2.8
Vietnam	13,464.9	2.4	15,946.0	2.9	21,087.6	3.8	22,351.7	3.9	27,770.8	5.3
Taiwan	18,206.0	3.3	14,814.9	2.7	15,699.1	2.8	15,077.4	2.6	12,004.3	2.3
India	12,654.1	2.3	11,922.0	2.2	11,375.8	2.0	12,782.5	2.2	12,029.6	2.3
Indonesia	13,564.5	2.4	13,955.0	2.5	11,568.2	2.1	11,360.7	2.0	7,872.4	1.5
Mexico	9,729.1	1.8	9,042.4	1.7	9,727.4	1.7	10,846.0	1.9	10,891.9	2.1
Australia	8,163.8	1.5	9,250.5	1.7	9,563.1	1.7	10,282.5	1.8	10,830.6	2.1
Russia	10,304.9	1.9	11,097.1	2.0	11,149.1	2.0	10,129.2	1.8	4,685.7	0.9
Germany	9,500.9	1.7	7,509.7	1.4	7,907.9	1.4	7,570.9	1.3	6,220.2	1.2
Others ⁽²⁾	177,745.7	32.0	167,194.8	30.5	168,924.6	30.2	173,501.0	30.3	156,489.1	29.7
Total	555,213.7	100.0	547,869.8	100.0	559,632.4	100.0	572,664.6	100.0	526,756.5	100.0

Notes:

(1) Preliminary

(2) Includes more than 200 countries and regions.

Source: The Bank of Korea; Korea Customs Service.

The following table sets forth the Republic's imports trading partners:

Imports										
	2011	As % of 2011 Total	2012	As % of 2012 Total	2013	As % of 2013 Total	2014	As % of 2014 Total	2015 ⁽¹⁾	As % of 2015 Total ⁽¹⁾
(millions of dollars, except percentages)										
China	86,432.2	16.5	80,784.6	15.5	83,052.9	16.1	90,082.2	17.1	90,250.3	20.7
Japan	68,320.2	13.0	64,363.1	12.4	60,029.4	11.6	53,768.3	10.2	45,853.8	10.5
United States	44,569.0	8.5	43,341.0	8.3	41,511.9	8.1	45,283.3	8.6	44,024.4	10.1
Saudi Arabia	36,972.6	7.1	39,707.1	7.6	37,665.2	7.3	36,694.5	7.0	19,561.5	4.5
Qatar	20,749.4	4.0	25,504.7	4.9	25,873.8	5.0	25,723.1	4.9	16,474.8	3.8
Australia	26,316.3	5.0	22,987.9	4.4	20,784.6	4.0	20,413.0	3.9	16,437.8	3.8
Germany	16,962.6	3.2	17,645.4	3.4	19,336.0	3.8	21,298.8	4.0	20,956.5	4.8
Kuwait	16,959.6	3.2	18,297.1	3.5	18,725.1	3.6	16,892.0	3.2	8,973.4	2.1
Taiwan	14,693.6	2.8	14,012.0	2.7	14,632.6	2.8	15,689.8	3.0	16,653.9	3.8
United Arab Emirates	14,759.4	2.8	15,115.3	2.9	18,122.9	3.5	16,194.3	3.1	8,614.7	2.0
Indonesia	17,216.4	3.3	15,676.3	3.0	13,190.0	2.6	12,266.3	2.3	8,850.4	2.0
Malaysia	10,467.8	2.0	9,796.4	1.9	11,095.8	2.2	11,097.9	2.1	8,609.4	2.0
Others ⁽²⁾	149,994.0	28.6	152,353.6	29.3	151,565.3	29.4	160,111.0	30.5	131,238.1	30.1
Total	524,413.1	100.0	519,584.5	100.0	515,585.5	100.0	525,514.5	100.0	436,499.0	100.0

Notes:

(1) Preliminary

(2) Includes more than 200 countries and regions.

Source: The Bank of Korea; Korea Customs Service.

In the past, the outbreak of severe health epidemics in Korea and various parts of the world increased uncertainty about prospects for international trade and economic growth for affected countries, as well as world economic prospects in general. In response to these outbreaks, the Government issued advisories on disease prevention and conducted special monitoring. In May 2015, an outbreak of Middle East Respiratory Syndrome, or MERS, resulted in the death of over 30 people and the quarantine of thousands. The Government continued to cooperate with regional and international efforts to develop and implement additional measures to contain and prevent MERS and other diseases. Another outbreak of MERS or similar incidents in the future may have an adverse effect on Korean and world economies and on international trade.

In recent years, the value of the Won relative to the U.S. dollar and Japanese Yen has fluctuated widely. An appreciation of the Won against the U.S. dollar and Japanese Yen increases the Won value of the Republic's export sales and diminishes the price-competitiveness of export goods in U.S. dollar and Japanese Yen terms, respectively. However, it also decreases the cost of imported raw materials in Won terms and the cost in Won of servicing the Republic's U.S. dollar and Japanese Yen denominated debt. In general, when the Won appreciates, export dependent sectors of the Korean economy, including automobiles, electronics and shipbuilding, suffer from the resulting pressure on the price-competitiveness of export goods, which may lead to reduced profit margins and loss in market share, more than offsetting a decrease in the cost of imported raw materials. If the Won continues to appreciate, the export dependent sectors of the Korean economy may suffer reduced profit margins or a net loss, which could result in a material adverse effect on the Korean economy.

Since the Government announced its plans to pursue free trade agreements, or FTAs, in 2003, the Republic has signed FTAs with key trading partners. The Republic has had bilateral FTAs in effect with Chile since 2004, Singapore since 2006, India since 2010, Peru since 2011, the United States since 2012, Turkey since 2013, Australia since 2014, Canada since January 2015 and China, New Zealand and Vietnam since December 2015. The Republic has also signed bilateral FTAs with Columbia and Turkey, which have yet to come into effect, and is currently in negotiations with a number of other key trading partners, including Indonesia and Japan. In addition, the Republic has had regional FTAs in effect with the European Free Trade Association since 2006, Association of Southeast Asian Nations since 2009 and the European Union since 2011.

Non-Commodities Trade Balance

The Republic had a non-commodities trade deficit of US\$10.4 billion in 2011, a non-commodities trade surplus of US\$1.4 billion in 2012, a non-commodities trade deficit of US\$1.6 billion in 2013 and a non-commodities trade deficit of US\$3.5 billion in 2014. Based on preliminary data, the Republic had a non-commodities trade deficit of US\$14.4 billion in 2015.

Foreign Currency Reserves

The foreign currency reserves are external assets that are readily available to and controlled by monetary authorities for meeting balance of payments financing needs and for other related purposes. The following table shows the Republic's total official foreign currency reserves:

Total Official Reserves

	December 31,				
	2011	2012	2013	2014	2015
	(millions of dollars)				
Gold ⁽¹⁾	\$ 2,166.6	\$ 3,761.4	\$ 4,794.5	\$ 4,794.7	\$ 4,794.7
Foreign Exchange ⁽²⁾	298,232.9	316,897.7	335,647.5	353,600.5	358,513.8
Total Gold and Foreign Exchange	300,399.5	320,659.1	340,442.0	358,395.2	363,308.5
Reserve Position at IMF	2,556.2	2,783.6	2,527.7	1,917.1	1,411.8
Special Drawing Rights	3,446.7	3,525.6	3,489.9	3,280.5	3,241.4
Total Official Reserves	<u>\$306,402.5</u>	<u>\$326,968.4</u>	<u>\$346,459.6</u>	<u>\$363,592.7</u>	<u>\$367,961.9</u>

Notes:

(1) For this purpose, domestically-owned gold is valued at US\$42.22 per troy ounce (31.1035 grams) and gold deposited overseas is calculated at cost of purchase.

(2) More than 95% of the Republic's foreign currency reserves are comprised of convertible foreign currencies.

Source: The Bank of Korea; International Monetary Fund

The Government's foreign currency reserves increased to US\$262.2 billion as of December 31, 2007 from US\$8.9 billion as of December 31, 1997, primarily due to continued balance of trade surpluses and capital inflows. In 2008, the Government's foreign currency reserves decreased, falling to US\$201.2 billion as of December 31, 2008, partially as a result of the Government's use of the foreign currency reserve to provide foreign currency liquidity to Korean financial institutions. The Government's foreign currency reserves increased to US\$306.4 billion as of December 31, 2011, US\$327.0 billion as of December 31, 2012, US\$346.5 billion as of December 31, 2013, US\$363.6 billion as of December 31, 2014 and US\$368.0 billion as of December 31, 2015, primarily due to continued trade surpluses and capital inflows. The amount of the Government's foreign currency reserve was US\$369.9 billion as of June 30, 2016.

Government Finance

The Ministry of Strategy and Finance prepares the Government budget and administers the Government's finances.

The Government's fiscal year commences on January 1. The Government must submit the budget, which is drafted by the Minister of Strategy and Finance and approved by the President of the Republic, to the National Assembly not later than 90 days prior to the start of the fiscal year and may submit supplementary budgets revising the original budget at any time during the fiscal year.

2014 budgeted revenues increased by 3.7% to ₩338.9 trillion from ₩326.9 trillion in 2013, led by an increase in budgeted tax revenues (including revenues from income tax and value added tax). 2014 budgeted expenditures and net lending increased by 3.3% to ₩325.4 trillion from ₩315.1 trillion in 2013, led by increases in budgeted expenditures on social security, public assistance, childcare and welfare services for senior citizens. The 2014 budget anticipated a ₩13.5 billion budget surplus.

2015 budgeted revenues increased by 3.6% to ₩351.1 trillion from ₩338.9 trillion in 2014, led by an increase in budgeted tax revenues (including revenues from income tax, value added tax and social security contributions). 2015 budgeted expenditures and net lending increased by 5.8% to ₩344.2 trillion from ₩325.4 trillion in 2014, led by increases in budgeted expenditures on economic growth, social security, public assistance, military services and welfare services for senior citizens, unemployed people and temporary workers. The 2015 budget anticipated a ₩6.9 billion budget surplus.

2016 budgeted revenues increased by 2.6% to ₩360.1 trillion from ₩351.1 trillion in 2015, led by an increase in budgeted tax revenues (including revenues from social security contributions and income tax). 2016 budgeted expenditures and net lending increased by 3.2% to ₩355.3 trillion from ₩344.2 trillion in 2015, led by increases in budgeted expenditures on economic growth (including research and development), welfare services for senior citizens, unemployed people and temporary workers, promotion of cultural industries, military services, public assistance, child care and education. The 2016 budget anticipated a ₩4.8 billion budget surplus.

The following table shows consolidated Government revenues and expenditures:

Consolidated Central Government Revenues and Expenditures

	Actual					Budget		
	2011	2012	2013	2014	2015	2014	2015	2016
	(billions of Won)							
Total Revenues	292,323	311,456	314,438	320,895	339,186	338,867	351,139	360,111
Current Revenues	289,797	307,754	311,136	318,185	335,911	334,653	346,636	355,980
Total Tax Revenues	231,273	246,918	248,046	255,313	270,974	268,415	276,583	283,467
Taxes on income, profits and capital gains	87,161	91,699	91,674	95,976	105,751	100,400	103,378	106,816
Social security contributions	38,892	43,904	46,140	49,793	53,089	51,962	55,441	60,530
Tax on property	8,713	8,832	8,591	9,054	11,113	9,754	10,134	10,303
Taxes on goods and services	71,519	77,811	77,642	79,055	79,442	80,924	83,272	84,196
Taxes on international trade and transaction	10,990	9,816	10,562	8,721	8,495	10,551	9,882	8,708
Other tax	13,998	14,857	13,438	12,715	13,084	14,824	14,477	12,915
Non-Tax Revenues	58,524	60,836	63,089	62,872	64,936	66,238	70,053	72,513
Operating surpluses of departmental enterprise sales and property income	24,675	25,242	24,591	23,112	22,129	23,999	23,816	25,920
Administration fees & charges and non-industrial sales	6,973	7,364	8,537	7,997	8,664	8,437	10,403	8,578
Fines and forfeits	17,180	17,488	18,164	19,556	20,777	20,769	21,962	23,484
Contributions to government employee pension fund	7,303	8,134	8,776	9,915	10,929	10,034	10,458	11,372
Current revenue of non-financial public enterprises	2,393	2,608	3,021	2,292	2,437	2,999	3,415	3,159
Capital Revenues	2,527	3,702	3,302	2,710	3,276	4,214	4,502	4,131
Total Expenditures and Net Lending	273,694	292,977	300,238	312,394	339,351	325,378	344,174	355,277
Total Expenditures	269,768	286,921	302,036	311,507	330,537	320,075	335,397	345,858
Current Expenditures	235,458	252,620	268,019	280,466	296,216	287,226	300,963	313,820
Expenditure on goods and service	52,989	55,384	57,769	59,616	63,160	64,470	68,865	69,715
Interest payment	14,566	14,239	13,386	14,057	14,056	14,439	14,293	14,434
Subsidies and other current transfers	165,233	179,433	193,451	203,649	216,189	204,638	214,125	226,011
Current expenditure of non-financial public enterprises	2,670	3,564	3,414	3,143	2,810	3,679	3,681	3,661
Capital Expenditures	34,310	34,301	34,017	31,041	34,322	32,850	34,433	32,038
Net Lending	3,926	6,056	(1,798)	888	8,814	5,303	8,778	9,419

Source: Ministry of Strategy and Finance; The Bank of Korea; Korea National Statistical Office

The consolidated Government account consists of a General Account, Special Accounts (including a non-financial public enterprise special account) and Public Funds. The Government segregates the accounts of certain functions of the Government into Special Accounts and Public Funds for more effective administration and fiscal control. The Special Accounts and Public Funds relate to business type activities, such as economic development, road and railway construction and maintenance, monopolies, and communications developments and the administration of loans received from official international financial organizations and foreign governments.

Revenues derive mainly from national taxes and non-tax revenues. Taxes in Korea can be roughly classified into the following types:

- income tax and capital gains tax,
- property tax,
- value-added tax,
- customs duty tax, and
- other taxes.

Income tax and capital gains tax are imposed on income derived from labor, business operation and ownership of assets and profits derived from capital appreciation. Income tax and capital gains tax, depending on the type of taxpayer, can be further classified into corporate income tax and individual income tax. Property tax is imposed on exchange or ownership of property and includes inheritance tax and gift tax. Value-added tax is imposed on value added to goods and services. Customs duty tax is imposed on imported goods. Other taxes include tax on certain securities transactions and a stamp tax for certain documents.

Expenditures include general administration, national defense, community service, education, health, social security, certain annuities and pensions and local finance, which involves the transfer of tax revenues to local governments.

For 2011, the Republic recorded total revenues of ₩292.3 trillion and total expenditures and net lending of ₩273.7 trillion. The Republic had a fiscal surplus of ₩18.6 trillion in 2011.

For 2012, the Republic recorded total revenues of ₩311.5 trillion and total expenditures and net lending of ₩293.0 trillion. The Republic had a fiscal surplus of ₩18.5 trillion in 2012.

For 2013, the Republic recorded total revenues of ₩314.4 trillion and total expenditures and net lending of ₩300.2 trillion. The Republic had a fiscal surplus of ₩14.2 trillion in 2013.

For 2014, the Republic recorded total revenues of ₩320.9 trillion and total expenditures and net lending of ₩312.4 trillion. The Republic had a fiscal surplus of ₩8.5 trillion in 2014.

Based on preliminary data, the Republic recorded total revenues of ₩339.2 trillion and total expenditures and net lending of ₩339.4 trillion in 2015. The Republic had a fiscal deficit of ₩0.2 trillion in 2015.

Debt

The Government estimates that the total outstanding debt of the Government (including guarantees by the Government) as of December 31, 2014 amounted to approximately ₩532.2 trillion, an increase of 7.1% over the previous year. The Government estimates that the total outstanding debt of the Government (including guarantees by the Government) as of December 31, 2015 amounted to approximately ₩582.9 trillion, an increase of 9.5% over the previous year. The Ministry of Strategy and Finance administers the national debt of the Republic.

External and Internal Debt of the Government

The following table sets out, by currency and the equivalent amount in U.S. Dollars, the estimated outstanding direct external debt of the Government as of December 31, 2015:

Direct External Debt of the Government

	Amount in Original Currency	Equivalent Amount in U.S. Dollars ⁽¹⁾
	(millions)	
US\$	US\$ 4,428.7	US\$ 4,428.7
Chinese Yuan (CNY)	CNY 3,000.0	462.2
Euro (EUR)	EUR 1,125.0	1,229.2
Total		<u>US\$ 6,120.1</u>

Note:

(1) Amounts expressed in currencies other than US\$ are converted to US\$ at the arbitrage rate announced by the Seoul Money Brokerage Services, Ltd. in effect on December 31, 2015.

The following table summarizes, as of December 31 of the years indicated, the outstanding direct internal debt of the Republic:

Direct Internal Debt of the Government

	(billions of Won)
2011	390,249.4
2012	414,213.5
2013	453,674.0
2014	493,584.9
2015	547,625.6

The following table sets out all guarantees by the Government of indebtedness of others:

Guarantees by the Government

	December 31,				
	2011	2012	2013	2014	2015
	(billions of Won)				
Domestic	33,799.1	32,783.6	32,978.5	29,158.4	26,393.8
External ⁽¹⁾	1,258.6	—	—	—	—
Total	<u>35,057.7</u>	<u>32,783.6</u>	<u>32,978.5</u>	<u>29,158.4</u>	<u>26,393.8</u>

Note:

(1) Converted to Won at foreign exchange banks' telegraphed transfer selling rates to customers or the market average exchange rates in effect on December 31 of each year.

External Liabilities

The following tables set out certain information regarding the Republic's external liabilities calculated under the criteria based on the sixth edition of Balance of Payment Manual, or BPM6, published by the International Monetary Fund in December 2010 and implemented by the Government in December 2013. Under BPM6, in particular, prepayments received in connection with the construction of ships are excluded from the external debt.

	December 31,				
	2011	2012	2013	2014	2015 ⁽¹⁾
	(billions of dollars)				
Long-term Debt	260.3	281.0	311.7	308.0	287.8
General Government	59.8	60.8	63.0	65.2	62.7
Monetary Authorities	14.2	21.2	29.2	25.9	19.4
Banks	93.4	97.8	102.2	104.0	102.4
Other Sectors	92.9	101.2	117.4	112.9	103.3
Short-term Debt	139.8	128.0	111.8	116.4	108.7
General Government	0.5	0.0	0.0	1.8	2.3
Monetary Authorities	8.9	14.9	10.8	12.2	14.9
Banks	102.9	85.4	77.9	79.9	73.0
Other Sectors	27.5	27.7	23.0	22.5	18.5
Total External Liabilities	400.0	408.9	423.5	424.4	396.6

Note:

(1) Preliminary

Debt Record

The Government has always paid when due the full amount of principal of, interest on, and amortization of sinking fund requirements of, all of its indebtedness.

TERMS AND CONDITIONS OF THE NOTES

The US\$500,000,000 2.125% Notes due 2026 (the “Notes,” which expression shall in these Conditions, unless the context otherwise requires, include any further notes issued pursuant to Condition 14 and forming a single series with the Notes) of Small and medium Business Corporation (“SBC”) are issued subject to and with the benefit of an agency agreement dated August 30, 2016 (such agreement as amended and/or supplemented and/or restated from time to time, the “Agency Agreement”) between SBC and Deutsche Bank AG, Hong Kong Branch, as fiscal agent (the “Fiscal Agent”), paying agent (the “Paying Agent”, and together with the Fiscal Agent, the “Paying Agents”), transfer agent (the “Transfer Agent”) and registrar (the “Registrar”). The statements in these Conditions include summaries of, and are subject to, the detailed provisions of and definitions in the Agency Agreement. Copies of the Agency Agreement are available for inspection during normal business hours at the specified office of each of the Paying Agents. The Noteholders are entitled to the benefit of, are bound by, and are deemed to have notice of, all the provisions of the Agency Agreement applicable to them.

The owners shown in the records of Euroclear and Clearstream, Luxembourg of book-entry interests in Notes are entitled to the benefit of, are bound by, and are deemed to have notice of, all the provisions of the Agency Agreement applicable to them.

1. FORM, DENOMINATION AND TITLE

1.1 Form and Denomination

The Notes are issued in registered form in the denomination of US\$200,000, and integral multiples of US\$1,000 in excess thereof (an “Authorized Holding”). A note certificate (each a “Certificate”) will be issued to each Noteholder in respect of its registered holding of Notes. Each Certificate will be numbered serially with an identifying number which will be recorded on the relevant Certificate and in the register of Noteholders (“Note Register”). SBC will procure that the Note Register is maintained by the Registrar at the registered office of the Registrar.

1.2 Title

Title to the Notes shall pass by transfer and registration of transfer in the Note Register in accordance with the provisions of the Agency Agreement.

1.3 Holder Absolute Owner

Except as ordered by a court of competent jurisdiction or as required by law, the registered holder of any Note will be treated as the absolute owner for all purposes (whether or not it is overdue and regardless of any notice of ownership, trust or any interest or any writing on, or the theft or loss of, the Certificate issued in respect of it), and none of SBC nor the Fiscal Agent, the Paying Agents, the Registrar, the Transfer Agents nor any agent thereof shall be affected by notice to the contrary.

2. TRANSFERS OF NOTES AND ISSUE OF CERTIFICATES

2.1 Transfers

Upon the terms and subject to the conditions set forth in the Agency Agreement, a Note may be transferred provided that after giving effect to the transfer both the transferor and the transferee must each hold an Authorized Holding of Notes. A Note may be transferred by depositing the Certificate issued in respect of that Note, with the form of transfer on the back duly completed and signed, at the specified office of the Registrar or any of the Agents.

2.2 Delivery of new Certificates

Each new Certificate to be issued upon transfer of Notes will, within five business days of receipt by the Registrar or the relevant Agent of the duly completed form of transfer endorsed on the relevant Certificate, be mailed by uninsured mail at the risk of the holder entitled to the Note to the address specified in the form of transfer. For the purposes of this Condition, business day shall mean a day on which Euroclear and Clearstream, Luxembourg are operating and a day on which commercial banks are open for business in the city in which the specified office of the Agent with whom a Certificate is deposited in connection with a transfer is located.

Except in the limited circumstances described herein as described in “The Global Certificate—Registration of Title,” owners of interests in the Notes will not be entitled to receive physical delivery of Certificates.

Where some but not all of the Notes in respect of which a Certificate is issued are to be transferred, a new Certificate in respect of the Notes not so transferred will, within five business days of receipt by the Registrar or the relevant Agent of the original Certificate, be mailed by uninsured mail at the risk of the holder of the Notes not so transferred to the address of such holder appearing on the Note Register or as specified in the form of transfer.

2.3 Formalities free of charge

Registration of transfer of Notes will be effected without charge by or on behalf of SBC or any Agent but upon (i) payment (or the giving of such indemnity as SBC or any Agent may reasonably require) in respect of any tax or other governmental charges which may be imposed in relation to such transfer, and (ii) SBC or the relevant Transfer Agent being reasonably satisfied that the regulations concerning transfer of Notes have been complied with.

2.4 Closed Periods

No Noteholder may require the transfer of a Note to be registered (i) during the period of 15 days ending on (and including) the due date for any payment of principal or interest on that Note or (ii) after any such Note has been called for redemption.

2.5 Regulations

All transfers of Notes and entries on the Note Register will be made subject to the detailed regulations concerning transfer of Notes scheduled to the Agency Agreement. The regulations may be changed by SBC upon prior written notification to the Registrar and the Fiscal Agent. A copy of the current regulations will be mailed (free of charge) by the Registrar to any Noteholder who requests one and is available at the office of the Transfer Agent.

3. STATUS

The Notes are direct, unconditional, unsubordinated and (subject to Condition 4) unsecured obligations of SBC and (subject as stated above) rank and will rank *pari passu*, without any preference among themselves, and at least *pari passu* with all other present and future outstanding unsecured and unsubordinated obligations of SBC (other than obligations preferred by mandatory provisions of applicable law).

4. NEGATIVE PLEDGE

4.1 Negative Pledge

So long as any of the Notes remains outstanding (as defined in the Agency Agreement), SBC will not create, purport to create, or permit to be outstanding any mortgage, charge, lien, pledge or other form of encumbrance or

security interest (each a “Security Interest”) upon the whole or part of its undertaking, property, assets or revenues, present or future, other than any lien or encumbrance arising by operation of law, to secure in respect of any International Investment Securities:

- (i) any payment of any sum due in respect of any such International Investment Securities; or
- (ii) any payment under any guarantee or other like obligation of any such International Investment Securities; or
- (iii) any payment under any indemnity or other like obligation relating to any such International Investment Securities,

without in any such case at the same time according to the Notes either the same Security Interest as is granted to or is outstanding in respect of such International Investment Securities, guarantee, indemnity or other like obligation or such other arrangement (whether or not comprising a Security Interest) as shall be approved by an Extraordinary Resolution. “Extraordinary Resolution” means (a) a resolution passed at a meeting of the Noteholders duly convened and held in accordance with the provisions contained in the Agency Agreement by a majority consisting of not less than three-fourths of the persons voting thereat upon a show of hands or if a poll shall be duly demanded then by a majority consisting of not less than three-fourths of the votes given on the poll or (b) a resolution in writing signed by or on behalf of the Noteholders holding not less than 90% in principal amount of the Notes for the time being outstanding.

4.2 Interpretation

For the purpose of these Conditions:

“International Investment Securities” means notes, debentures, bonds or investment securities of SBC or any other person which:

- (i) either are by their terms payable, or confer a right to receive payment, in any currency other than Won or are denominated in Won and more than 50% of the aggregate principal amount thereof is initially distributed outside Korea by or with the authorization of SBC; and
- (ii) are for the time being, or are intended to be, or are capable of being, quoted, listed, ordinarily dealt in or traded on any stock exchange or over-the-counter or other securities market outside Korea.

“Subsidiary” means, whether currently in existence or established in the future, any corporation or other business entity (i) of which SBC owns or controls (either directly or through another or other Subsidiaries) 50% or more of the issued share capital or other ownership interest having ordinary voting power to elect directors, managers or trustees of such corporation or other business entity (whether or not capital stock or other ownership interest in any other class or classes shall or might have voting power upon the occurrence of any contingency) or (ii) which at any time has its accounts consolidated with those of SBC or which, under Korean law, regulations or generally accepted accounting principles from time to time, should have its accounts consolidated with those of SBC.

5. INTEREST

5.1 Interest Rate and Interest Payment Dates

The Notes bear interest at the rate of 2.125% per annum from, and including, August 30, 2016 (the “Issue Date”) to, but excluding, the due date for redemption of the Notes. Interest will be paid semi-annually in arrears on February 28 (or February 29 in a leap year) and August 30 in each year (each an “Interest Payment Date”). The first Interest Payment Date will be February 28, 2017 in respect of the period from, and including, August 30, 2016 to, but excluding, February 28, 2017.

5.2 Interest Accrual

Each Note will cease to bear interest from and including its due date for redemption unless, upon due presentation or surrender, payment of the principal in respect of the Note is improperly withheld or refused or unless default is otherwise made in respect of payment. In such event, interest will continue to accrue until whichever is the earlier of:

- (a) the date on which all amounts due in respect of such Note have been paid; and
- (b) the date on which the full amount of the moneys payable in respect of such Notes has been received by the Fiscal Agent and notice to that effect has been given to the Noteholders in accordance with Condition 12.

5.3 Calculation of Broken Interest

If interest is to be calculated for a period of less than a full year, interest shall be calculated on the basis of the actual number of days elapsed and a 360-day year consisting of 12 months of 30 days each. For the avoidance of doubt, the last day of any month, including February (regardless of whether it is a leap year), constitutes the 30th day of that month, and the amount of interest payable on each Interest Payment Date shall be US\$10.625 per Note of US\$1,000 in nominal amount.

6. PAYMENTS

6.1 Payments in respect of Notes

Payment of principal and interest will be made by transfer to an account denominated in U.S. dollar maintained by the Noteholder with or, at the option of the Noteholder, by a check drawn on a bank in New York City mailed to the registered address of the Noteholder. Payments of principal and payments of interest due otherwise than on an Interest Payment Date will only be made against surrender of the relevant Certificate at the specified office of any of the Agents. Interest on Notes due on an Interest Payment Date will be paid to the holder shown on the Note Register at the close of business on the Record Date (as defined below) for the relevant Interest Payment Date; provided, however, that interest payable on the date of redemption shall be payable to the person to whom the principal of such Note shall be payable.

The "Record Date" for any Interest Payment Date will be, with respect to the Notes represented by the Global Certificate, the close of business on the Clearing System Business Day immediately prior to the Interest Payment Date, where "Clearing System Business Day" means Monday to Friday inclusive except December 25 and January 1 and, with respect to Notes represented by Certificates, the date 15 days immediately preceding such Interest Payment Date (in each case, whether or not a Business Day (as defined below)).

6.2 Payments subject to Applicable Laws

Payments in respect of principal and interest on Notes are subject in all cases to any fiscal or other laws and regulations applicable in the place of payment, but without prejudice to the provisions of Condition 8.

6.3 No commissions

No commissions or expenses shall be charged to the Noteholders in respect of any payments made in accordance with this Condition.

6.4 Payment on Business Days

Where payment is to be made by transfer to a U.S. dollar account maintained by the Noteholder, payment instructions (for value the due date or, if that is not a Business Day (as defined below), for value the first following day which is a Business Day) will be initiated and, where payment is to be made by check, the check will be mailed (uninsured and at the risk and, if mailed at the request of the holder otherwise than by ordinary mail, at the expense of the holder), on the due date for payment (or, if it is not a Business Day, the immediately

following Business Day) or, in the case of a payment of principal or a payment of interest due otherwise than on an Interest Payment Date, if later, on the Business Day on which the relevant Certificate is surrendered at the specified office of an Agent.

Noteholders will not be entitled to any interest or other payment for any delay after the due date in receiving the amount due if the due date is not a Business Day, if the Noteholder is late in surrendering its Certificate (if required to do so) or if a check mailed in accordance with this Condition arrives after the due date for payment or being lost in the mail.

If payment to a Noteholder is to be made by transfer to a U.S. dollar account maintained by the Noteholder, and it is not practicable to transfer the relevant amount to such account for value on the relevant date of payment as a result of differences in the time zones, none of the Paying Agents shall be obliged so to do, but shall be obliged to transfer the relevant amount to such account for value on the first practicable day after such relevant date of payment.

In this Condition, “Business Day” means a day (excluding Saturdays, Sundays and other public holidays) on which Euroclear and Clearstream, Luxembourg are operating and a day on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealing in foreign exchange and foreign currency deposits) in New York City, Seoul and London, and the place of the specified office of the Paying Agent at which the Certificate is presented for payment.

6.5 Partial Payments

If the amount of principal or interest which is due on the Notes is not paid in full, the Registrar will annotate the Note Register with a record of the amount of principal or interest in fact paid.

6.6 Agents

The names of the initial Agents and their initial specified offices are set out at the end of these Conditions. SBC reserves the right at any time to vary or terminate the appointment of any Agent and to appoint additional or other Agents provided that:

- (a) it will at all times maintain a Fiscal Agent;
- (b) it will at all times maintain a Paying Agent having its specified office in Hong Kong; and
- (c) it will at all times maintain a Registrar.

Notice of any termination or appointment and of any changes in specified offices will be given to the Noteholders promptly by SBC in accordance with Condition 12.

For so long as the Notes are listed on the Singapore Stock Exchange and the rules of the Singapore Stock Exchange so require, in the event that the Global Certificate is exchanged for Certificates, SBC will appoint and maintain a Paying Agent in Singapore, where the Certificates representing the Notes may be presented or surrendered for payment or redemption. In addition, in the event that the Global Certificate is exchanged for Certificates, an announcement of such exchange will be made by or on behalf of SBC through the Singapore Stock Exchange. Such announcement will include all material information with respect to the delivery of the Certificates, including details of the Paying Agent in Singapore.

7. REDEMPTION AND PURCHASE

7.1 Redemption at Maturity

Unless previously redeemed or purchased and cancelled as provided below, SBC will redeem the Notes at their principal amount on August 30, 2026.

7.2 Redemption for Taxation Reasons

If (a) as a result of any change in, or amendment to, the laws or regulations of a Relevant Jurisdiction (as defined in Condition 8), or any change in the official interpretation of the laws or regulations of a Relevant Jurisdiction, which change or amendment becomes effective after August 22, 2016, on the next Interest Payment Date SBC would be required to pay additional amounts as provided or referred to in Condition 8 and (b) the requirement cannot be avoided by SBC taking reasonable measures available to it, SBC may at its option, having given not less than 30 nor more than 60 days' notice to the Noteholders in accordance with Condition 12 (which notice shall be irrevocable), redeem all the Notes, but not some only, at any time at their principal amount together with interest accrued to but excluding the date of redemption. Prior to the publication of any notice of redemption pursuant to this paragraph, SBC shall deliver to the Fiscal Agent a certificate signed by two Directors of SBC stating that the requirement referred to in (a) above will apply on the next Interest Payment Date and cannot be avoided by SBC taking reasonable measures available to it and an opinion of independent legal or tax advisers of recognized standing to the effect that SBC has or will become obliged to pay such additional amounts as a result of the change or amendment.

7.3 Purchases

SBC or any of its Subsidiaries may at any time purchase Notes in any manner and at any price.

7.4 Cancellations

All Notes which are redeemed or purchased by or on behalf of SBC or any of its Subsidiaries will forthwith be cancelled (to the extent permitted by applicable law in the case of Subsidiaries), and accordingly may not be held, reissued or resold.

7.5 Notices Final

Upon the expiry of any notice as is referred to in Condition 7.2 above SBC shall be bound to redeem the Notes to which the notice refers in accordance with the terms of such paragraph.

8. TAXATION

8.1 Payment without Withholding

All payments in respect of the Notes by or on behalf of SBC shall be made without withholding or deduction for, or on account of, any present or future taxes, duties, assessments or governmental charges of whatever nature ("Taxes") imposed or levied by or on behalf of the Relevant Jurisdiction, unless the withholding or deduction of the Taxes is required by law. In that event, SBC will pay such additional amounts as may be necessary in order that the net amounts received by the Noteholders after the withholding or deduction shall equal the respective amounts which would have been receivable in respect of the Notes in the absence of the withholding or deduction; except that no additional amounts shall be payable in relation to any payment in respect of any Note:

- (a) to, or to a third party on behalf of, a holder who is liable to the Taxes in respect of the Note by reason of his having some connection with the Relevant Jurisdiction other than the mere holding of the Note; or
- (b) presented for payment by or on behalf of a Noteholder who would be able to avoid such withholding or deduction by presenting the relevant Note to another Paying Agent in a Member State of the European Union; or
- (c) presented for payment more than 30 days after the Relevant Date except to the extent that a holder would have been entitled to additional amounts on presenting the same for payment on the last day of the period of 30 days assuming that day to have been a Business Day; or

- (d) to, or to a third party on behalf of, a Noteholder who would not be liable or subject to the withholding or deduction by making a declaration of non-residence or other similar claim for exemption to the relevant tax authority.

8.2 Interpretation

In these Conditions:

- (a) “Relevant Date” means the date on which the payment first becomes due but, if the full amount of the money payable has not been received by the Fiscal Agent on or before the due date, it means the date on which, the full amount of the money having been so received, notice to that effect shall have been duly given to the Noteholders by SBC in accordance with Condition 12; and
- (b) “Relevant Jurisdiction” means The Republic of Korea or any political subdivision or any authority thereof or therein having power to tax or any other jurisdiction or any political subdivision or any authority thereof or therein having power to tax to which SBC becomes subject in respect of payments made by it of principal and interest on the Notes.

8.3 Additional Amounts

Any reference in these Conditions to any amounts in respect of the Notes shall be deemed also to refer to any additional amounts which may be payable under this Condition.

9. PRESCRIPTION

Claims in respect of principal and interest will become prescribed unless made within five years (in the case of principal) and two years (in the case of interest) from the Relevant Date, as defined in Condition 8.

10. EVENTS OF DEFAULT

If any one or more of the following events (each an “Event of Default”) shall occur and shall be continuing:

- (a) a default is made for more than seven days in the payment of any amount of principal due in respect of the Notes when and as the same ought to be paid in accordance with these Conditions; or
- (b) a default is made for more than 14 days in the payment of any amount other than principal in respect of the Notes when and as the same ought to be paid in accordance with these Conditions; or
- (c) any External Indebtedness (as defined below) of SBC in the aggregate principal amount of US\$10,000,000 or more either (i) becoming due and payable prior to the due date for payment thereof by reason of default by SBC or (ii) not being repaid at maturity as extended by the period of grace, if any, applicable thereto, or any guarantee given by SBC in respect of External Indebtedness of any other person in the aggregate principal amount of US\$10,000,000 or more not being honored when due and called, except in any such case where such External Indebtedness or guarantee is being contested in good faith by appropriate proceedings; or
- (d) SBC declaring a moratorium on the payment of any External Indebtedness (including obligations arising under guarantees) of SBC; or
- (e) the Government declaring a moratorium on the payment of any External Indebtedness (including obligations arising under guarantees) of the Government or the Government becoming liable to repay prematurely any sums in respect of such External Indebtedness (including obligations arising under guarantees) as a result of a default under, or breach of the terms applicable to, such External Indebtedness or such obligations, or the Government ceasing to be a member in good standing of the International Monetary Fund or the International Bank for Reconstruction and Development or the

international monetary reserves of the Government becoming subject to any lien, charge, mortgage, encumbrance or other security interest or any segregation or other preferential arrangement (whether or not constituting a security interest) for the benefit of any creditor or class of creditors; or

- (f) the Government ceasing to control (directly or indirectly) SBC or for any reason failing to provide the financial support to SBC stipulated as of the date of the Notes by Article 66-2 of the Small- and Medium-sized Enterprises Promotion Act, as amended; or
- (g) SBC being adjudicated or found bankrupt or insolvent or any order being made by a competent court or administrative agency or any resolution being passed by SBC to apply for the appointment of a receiver or trustee or other similar official in insolvency proceedings in relation to SBC or a substantial part of its assets or SBC being wound up or dissolved or SBC ceasing to carry on the whole or substantially the whole of its business;

the registered holder of the Notes may, at such holder's option, declare the principal of the Notes and the interest accrued hereon to be due and payable immediately by written notice to SBC and the Fiscal Agent at its corporate trust office, and unless all such defaults shall have been cured by SBC prior to receipt of such written notice, the principal of the Notes and the interest accrued thereon shall become and be immediately due and payable. Upon payment of such amount, all of SBC's obligations in respect of the payment of the principal of and interest, if any, on the Notes shall terminate.

As used herein, "**External Indebtedness**" means any obligation for the payment or repayment of money borrowed which is denominated in a currency other than the currency of Korea. No periodic evidence is required to be furnished by SBC as to the absence of defaults.

11. REPLACEMENT OF CERTIFICATES

If any Certificate is lost, stolen, mutilated, defaced or destroyed, it may be replaced at the specified office of the Registrar, upon payment by the claimant of the expenses incurred in connection with the replacement and on such terms as to evidence and indemnity as SBC may reasonably require. Mutilated or defaced Certificates must be surrendered before replacements will be issued.

12. NOTICES

All notices to the Noteholders will be valid if mailed to them at their respective addresses in the Note Register maintained by the Registrar. SBC shall also ensure that notices are duly given or published in a manner which complies with the rules and regulations of any stock exchange on which the Notes are for the time being listed. Any such notice will be deemed to have been given on the second day after being so mailed.

13. MEETINGS OF NOTEHOLDERS AND MODIFICATION

13.1 Provisions for Meetings

The Agency Agreement contains provisions for convening meetings of the Noteholders to consider any matter affecting their interests, including the modification by Extraordinary Resolution of any of these Conditions or the provisions of the Agency Agreement. The quorum at any meeting for passing an Extraordinary Resolution will be one or more persons present holding or representing more than 50% in principal amount of the Notes for the time being outstanding, or at any adjourned meeting one or more persons present whatever the principal amount of the Notes held or represented by him or them, except that at any meeting the business of which includes the modification of certain of these Conditions and certain of the provisions of the Agency Agreement, the necessary quorum for passing an Extraordinary Resolution will be one or more persons present holding or representing not less than two-thirds, or at any adjourned meeting not less than one-third, of the principal amount of the Notes for the time being outstanding. An Extraordinary Resolution passed at any meeting of the Noteholders will be binding on all Noteholders, whether or not they are present at the meeting. The

Agency Agreement contains provisions for the passing of an Extraordinary Resolution in the form of a written resolution signed by Noteholders holding not less than 90% in principal amount of the Notes for the time being outstanding.

13.2 Modification

The Fiscal Agent may agree, without the consent of the Noteholders, to any modification of any of these Conditions or any of the provisions of the Agency Agreement either (i) for the purpose of curing any ambiguity or of curing, correcting or supplementing any defective provision contained herein or therein or (ii) in any manner which is not materially prejudicial to the interests of the Noteholders. Any modification shall be binding on the Noteholders and, unless the Fiscal Agent agrees otherwise, any modification shall be notified by SBC to the Noteholders as soon as practicable thereafter in accordance with Condition 12.

14. FURTHER ISSUES

SBC may from time to time, without the consent of the Noteholders, create and issue further notes, having terms and conditions the same as those of the Notes, or the same except for the amount of the first payment of interest, which may be consolidated and form a single series with the outstanding Notes to the extent permitted under the applicable laws.

15. CURRENCY INDEMNITY

SBC's obligations under the Notes to make all payments in U.S. dollar will not be satisfied by any payment, recovery or any other realization of proceeds in any currency other than U.S. dollar. If, for the purpose of obtaining a judgment in any court with respect to any obligation of SBC under any Notes, it shall become necessary to convert into any other currency or currency unit any amount in the currency or currency unit due under any Notes, then such conversion shall be made by the Fiscal Agent at the market exchange rate (as determined by the Fiscal Agent) as in effect on the date of entry of the judgment (the "Judgment Date"); it being understood that the Fiscal Agent shall effect such conversion only after receipt of the relevant funds from SBC and that such conversion may require up to three Business Days to effect after the receipt of such funds. If pursuant to any such judgment, conversion shall be made on a date (the "Substitute Date") other than the Judgment Date and there shall occur a change between the market exchange rate for U.S. dollar as in effect on the Substitute Date and the market exchange rate as in effect on the Judgment Date, SBC agrees to pay such additional amounts (if any) in U.S. dollar as may be necessary to ensure that the amount paid is equal to the amount in such other currency or currency unit which, when converted at the market exchange rate as in effect on the Judgment Date, is the amount due under any Notes. To the extent permitted by applicable law, any amount due from SBC under this Condition shall be due as a separate debt and is not to be affected by or merged into any judgment being obtained for any other sums due in respect of any Notes. In no event, however, shall SBC be required to pay more in U.S. dollar due under the Notes at the market exchange rate as in effect on the Judgment Date than the amount of U.S. dollar stated to be due under the Notes so that in any event SBC's obligations under the Notes will be effectively maintained as obligations in U.S. dollar and SBC shall be entitled to withhold (or be reimbursed for, as the case may be) any excess of the amount actually realized upon any such conversion on the Substitute Date over the amount due and payable on the Judgment Date.

16. GOVERNING LAW AND SUBMISSION TO JURISDICTION

16.1 Governing Law

The Agency Agreement and the Notes are governed by, and will be construed in accordance with, the laws of the State of New York.

16.2 Jurisdiction of Courts

SBC agrees that any legal suit, action or proceeding arising out of or based upon the Agency Agreement or the Notes may be instituted in any state or U.S. federal court located in the Borough of Manhattan, The City of

New York, New York, United States of America. SBC (a) waives, to the extent it may effectively do so, any objection which it may have now or hereafter to the laying of the venue of any such suit, action or proceeding, and (b) irrevocably submits to the jurisdiction of any such court in any such suit, action or proceeding.

16.3 Appointment of Process Agent

SBC hereby designates Law Debenture Corporate Services Inc., as SBC's authorized agent to accept and acknowledge on its behalf service of any and all process which may be served in any such suit, action or proceeding in connection with the Agency Agreement, the Notes in any court specified in Condition 16.2 above, and agrees that service of process upon said agent at its office at 400 Madison Avenue, 4th Floor, New York, NY 10017, United States of America (or at such other address as such agent may designate by written notice to SBC and the Fiscal Agent) shall be deemed in every respect effective service of process upon SBC in any such suit, action or proceeding and shall be taken and held to be valid personal service upon SBC, whether or not SBC shall then be doing, or at any time shall have done, business within the State of New York, and that any such service of process shall be of the same force and validity as if service were made upon it according to the laws governing the validity and requirements of such service in such State.

16.4 Sovereign Immunity

SBC hereby irrevocably and unconditionally, to the extent permitted by applicable law, waives and agrees not to raise with respect to the Agency Agreement, the Notes any right to claim sovereign or other immunity from jurisdiction or execution and any similar defense, and irrevocably and unconditionally consents to the giving of any relief or the issue of any process, including, without limitation, the making, enforcement or execution against any property whatsoever (irrespective of its use or intended use) of any order or judgment made or given in connection with any suit, action or proceeding in connection with the Agency Agreement, the Notes.

THE GLOBAL CERTIFICATE

The Global Certificate contains the following provisions which apply to the Notes in respect of which they are issued whilst they are represented by the Global Certificate, some of which modify the effect of the Conditions. Terms defined in the Conditions have the same meaning in paragraphs 1 to 6 below.

1. ACCOUNTHOLDERS

For so long as all of the Notes are represented by the Global Certificate and the Global Certificate is held on behalf of a clearing system, each person (other than another clearing system) who is for the time being shown in the records of Euroclear or Clearstream, Luxembourg (as the case may be) as the holder of a particular aggregate principal amount of such Notes (each an “Accountholder”) (in which regard any certificate or other document issued by Euroclear or Clearstream, Luxembourg (as the case may be) as to the aggregate principal amount of such Notes standing to the account of any person shall, in the absence of manifest error, be conclusive and binding for all purposes) shall be treated as the holder of such aggregate principal amount of such Notes (and the expression “Noteholders” and references to “holding of Notes” and to “holder of Notes” shall be construed accordingly) for all purposes other than with respect to payments on such Notes, the right to which shall be vested, as against SBC and the Fiscal Agent, solely in the nominee for the relevant clearing system (the “Relevant Nominee”) in accordance with and subject to the terms of the Global Certificate. Each Accountholder must look solely to Euroclear or Clearstream, Luxembourg, as the case may be, for its share of each payment made to the Relevant Nominee.

2. CANCELLATION

Cancellation of any Note following its redemption or purchase by SBC will be effected by reduction in the aggregate principal amount of the Notes in the Note Register and by the annotation of the appropriate schedule to the Global Certificate.

3. PAYMENTS

Payments of principal and interest in respect of Notes represented by the Global Certificate will be made upon presentation or, if no further payment falls to be made in respect of the Notes, against presentation and surrender of the Global Certificate to or to the order of the Registrar or such other Transfer Agent as shall have been notified to the holder of the Global Certificate for such purpose.

Distributions of amounts with respect to book-entry interests in the Notes held through Euroclear or Clearstream, Luxembourg will be credited, to the extent received by the Registrar, to the cash accounts of Euroclear or Clearstream, Luxembourg participants in accordance with the relevant system’s rules and procedures.

A record of each payment made will be endorsed on the appropriate schedule to the Global Certificate by or on behalf of the Registrar and shall be *prima facie* evidence that payment has been made.

4. NOTICES

So long as all the Notes are represented by the Global Certificate and the Global Certificate is held on behalf of a clearing system, notices to Noteholders may be given by delivery of the relevant notice to that clearing system for communication by it to entitled Accountholders in substitution for notification as required by the Conditions. Any such notice shall be deemed validly given on the day after it has been delivered to the relevant clearing systems as aforesaid.

5. REGISTRATION OF TITLE

Registration of title to Notes in a name other than that of the Relevant Nominee will not be permitted unless Euroclear or Clearstream, Luxembourg, as appropriate, notifies SBC that it is unwilling or unable to continue as a clearing system in connection with the Global Certificate, and in each case a successor clearing system approved by the Fiscal Agent is not appointed by SBC within 90 days after receiving such notice from Euroclear or Clearstream, Luxembourg. In these circumstances, title to a Note may be transferred into the names of holders notified by the Relevant Nominee in accordance with the Conditions, except that Certificates in respect of Notes so transferred may not be available until 21 days after the request for transfer is duly made.

The Registrar will not register title to the Notes in a name other than that of the Relevant Nominee for a period of 15 calendar days preceding the due date for any payment of principal, premium (if any) or interest in respect of the Notes.

6. TRANSFERS

Transfers of book-entry interests in the Notes will be effected through the records of Euroclear and Clearstream, Luxembourg and their respective participants in accordance with the rules and procedures of Euroclear and Clearstream, Luxembourg and their respective direct and indirect participants.

TAXATION

Korean Taxation

The information provided below does not purport to be a complete summary of Korean tax law and practice currently applicable. Prospective investors who are in any doubt as to their tax position should consult with their own professional advisers.

The taxation of non-resident individuals and non-Korean corporation (“non-residents”) depends in whether they have a “permanent establishment” (as defined under Korean law and applicable tax treaty) in Korea to which the relevant income is attributable or with which such relevant income is effectively connected. Non-residents without permanent establishment in Korea are taxed in the manner described below. Non-residents with permanent establishment in Korea are taxed in accordance with different rules.

Tax on Interest

In principle, interest paid to a non-resident by a Korean company is subject to withholding of Korean income tax or corporation tax unless exempted by relevant laws or tax treaties.

The Special Tax Treatment Control Law (the “STTCL”) exempt interest on bonds denominated in a foreign currency (excluding payments to a Korean corporation or resident) from Korean income tax or corporation tax. The residence tax referred to below is also eliminated under the STTCL.

Interest paid on the Notes will be exempt under the STTCL unless paid to a Korean corporation or resident.

If not exempt under the STTCL, interest on the Notes will be subject to withholding of Korean income tax or corporation tax at the rate of 14% for a non-resident. In addition, local income tax will be imposed at the rate of 10% of the income tax or corporation tax (raising the total tax rate to 15.4%).

Tax is withheld by the payer (or its agents) of the interest.

Tax rates may be reduced or exempted by applicable tax treaties, conventions or agreements between Korea and the country of the recipient of the interest. The relevant tax treaties are summarized below.

Tax on Capital Gains

Korean tax laws currently exclude from Korea taxation gains made by a non-resident without a permanent establishment in Korea from the sale of the Notes to non-residents (unless the sale is to the non-resident’s permanent establishment in Korea). In addition, capital gains earned by non-residents from the transfer of the Notes taking place outside of Korea are currently exempt from taxation by virtue of the STTCL provided that the offering of the Notes is deemed to be an overseas issuance under the STTCL.

In the absence of an applicable treaty or any other special tax laws reducing or eliminating capital gains tax, the applicable rate of tax is the lower of 11% (including local income tax) of the gross realization proceeds (the “Gross Realization Proceeds”) or (subject to the production of satisfactory evidence of the acquisition cost of the relevant Korean securities) 22% (including local income tax) of the gain made. The gain is calculated as the Gross Realization Proceeds less the acquisition cost and transaction cost. There is no provision under relevant Korean tax law for offsetting gains and losses or otherwise aggregating transactions for the purpose of computing the net gain attributable to sales of Korean securities. Unless the seller can claim the benefit of an exemption or a reduced rate of tax under an applicable treaty or in the absence of the seller producing satisfactory evidence of its acquisition cost in relation to the Korean securities being sold, the purchaser or any other designated withholding agent must withhold an amount equal to 11% of the Gross Realization Proceeds. Any withheld tax must be paid

no later than the tenth day of the month following the month in which the payment for the purchase of the relevant Korean securities occurred. Failure to timely transmit the withheld tax to the Korean tax authorities technically subjects the purchaser or any other designated withholding agent to penalties under Korean tax law.

In order to obtain the benefit of a tax treaty exemption or non-taxation, a non-resident seller should submit to the purchaser prior to or at the time of payment, such evidence of tax residence of the seller as the Korean tax authorities may require in support of the claim for treaty protection. Furthermore, Korean tax law requires a non-resident seller to submit to the purchaser or any other designated withholding agent the application for the exemption or non-taxation pursuant to a treaty with a certificate of tax residence of the nonresident seller issued by a competent tax authority of the non-resident seller's country of residence prior to the ninth day of the month following the month in which the first payment occurs in order to obtain the benefit of a tax treaty exemption or non-taxation. No certification is required to claim an exemption under Korean tax law, including the exemption under STTCL discussed above.

Inheritance Tax and Gift Tax

Korean inheritance tax is imposed upon (1) all assets (wherever located) of the deceased if at the time of death the deceased was domiciled in Korea and (2) all property located in Korea which passes on death (irrespective of the domicile of the deceased). Gift tax is imposed similarly in case of a gift. The taxes are imposed if the value of the relevant property is above a certain limit and the tax rate varies from 10-50% according to the value of the relevant property and the identity of the persons involved. At present, Korea has not entered into any tax treaties regarding its inheritance or gift taxes. Under Korean inheritance and gift tax laws, notes issued by Korean corporations are deemed located in Korea irrespective of where they are physically located or by whom they are owned.

Stamp Duty

No stamp, issue or registration duties will be payable in Korea by the holders of the Notes in connection with the issue of the Notes except for a nominal amount of stamp duty on certain documents executed in Korea which will be paid by us. No securities transaction tax will be imposed on the transfer of the Notes.

Tax Treaties

At the date of this Offering Circular, Korea has tax treaties with over 80 countries, including Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Ireland, Italy, Japan, Luxembourg, the Netherlands, New Zealand, Norway, Singapore, Sweden, Switzerland, the United Kingdom and the United States of America under which the rate of withholding tax on interest is reduced, generally to between 5% and 15%, and the tax on capital gains is often eliminated.

Each holder of the Notes should inquire whether he or she is entitled to the benefit of a tax treaty with Korea with respect to any transaction involving the Notes. It is the responsibility of the party claiming the benefits of a tax treaty in respect of interest payments to file with us, the purchaser or the securities company, as applicable, a certificate as to his or her tax residence. In the absence of sufficient proof, we, the purchaser or the securities company, as applicable, must withhold taxes in accordance with the above discussion.

SUBSCRIPTION AND SALE

BNP Paribas, Citigroup Global Markets Limited, Credit Suisse Securities (Europe) Limited and Nomura International plc (together, the “Managers”) have, pursuant to a subscription agreement (the “Subscription Agreement”) dated August 22, 2016, severally and not jointly, agreed to subscribe or procure subscribers for the Notes. SBC has agreed to indemnify the Managers against certain liabilities, incurred in connection with the issue of the Notes. The Subscription Agreement may be terminated in certain circumstances prior to payment to SBC.

United States

The Notes have not been and will not be registered under the Securities Act and may not be offered or sold within the United States or to, or for the account or benefit of, U.S. persons except in certain transactions exempt from the registration requirements of the Securities Act.

The Notes are subject to U.S. tax law requirements and may not be offered, sold or delivered within the United States or its possessions or to a United States person, except in certain transactions permitted by U.S. tax regulations. Terms used in this paragraph have the meanings given to them by the U.S. Internal Revenue Code of 1986 and regulations thereunder.

Each Manager has agreed that, except as permitted by the Subscription Agreement, it will not offer, sell or deliver the Notes, (i) as part of their distribution at any time or (ii) otherwise until 40 days after the later of the commencement of the offering and the closing, within the United States or to, or for the account or benefit of, U.S. persons and that it will have sent to each dealer to which it sells any Notes during the distribution compliance period a confirmation or other notice setting forth the restrictions on offers and sales of the Notes within the United States or to, or for the account or benefit of, U.S. persons. Terms used in this paragraph have the meanings given to them by Regulation S under the Securities Act.

In addition, until 40 days after the commencement of the offering, an offer or sale of Notes within the United States by any dealer (whether or not participating in the offering) may violate the registration requirements of the Securities Act.

European Economic Area

In relation to each Member State of the European Economic Area which has implemented the Prospectus Directive (each, a “Relevant Member State”), each Manager has represented and agreed that with effect from and including the date on which the Prospectus Directive is implemented in that Relevant Member State (the “Relevant Implementation Date”) it has not made and will not make an offer of Notes which are the subject of the offering contemplated by this Offering Circular in relation thereto to the public in that Relevant Member State except that it may, with effect from and including the Relevant Implementation Date, make an offer of Notes to the public in that Relevant Member State:

- (a) at any time to any legal entity which is a qualified investor as defined in the Prospectus Directive;
- (b) at any time to fewer than 150 natural or legal persons (other than qualified investors as defined in the Prospectus Directive), subject to obtaining the prior consent of the relevant Dealer or Dealers nominated by the Issuer for any such offer; or
- (c) at any time in any other circumstances falling within Article 3(2) of the Prospectus Directive,

provided that no such offer of Notes shall require the Issuer or any Dealer to publish a prospectus pursuant to Article 3 of the Prospectus Directive or supplement a prospectus pursuant to Article 16 of the Prospectus Directive.

For the purposes of this provision, the expression an “offer of Notes to the public” in relation to any Notes in any Relevant Member State means the communication in any form and by any means of sufficient information

on the terms of the offer and the Notes to be offered so as to enable an investor to decide to purchase or subscribe the Notes, as the same may be varied in that Member State by any measure implementing the Prospectus Directive in that Member State and the expression “Prospectus Directive” means Directive 2003/71/EC (as amended, including by Directive 2010/73/EU), and includes any relevant implementing measure in the Relevant Member State.

The EEA selling restriction is in addition to any other selling restrictions set out below.

United Kingdom

Each Manager has represented and agreed that, except as permitted by the Subscription Agreement:

- (i) it has only communicated or caused to be communicated, and will only communicate or cause to be communicated, any invitation or inducement to engage in investment activity (within the meaning of Section 21 of the Financial Services and Markets Act 2000 (the “FSMA”)) received by it in connection with the issue or sale of any Notes in circumstances in which Section 21(1) of the FSMA does not apply to SBC; and
- (ii) it has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to the Notes in, from or otherwise involving the United Kingdom.

Korea

The Notes have not been and will not be registered under the Financial Investment Services and Capital Markets Act of Korea. Each Manager has represented and agreed that it will not, directly or indirectly, offer, sell or deliver any Notes in Korea or to, or for the account or benefit of, any resident (as defined under the Foreign Exchange Transactions Law of Korea and its Enforcement Decree) of Korea, or to others for reoffering or resale, directly or indirectly, in Korea or to, or for the account or benefit of, any resident of Korea, except as otherwise permitted by applicable Korean laws and regulations.

Hong Kong

Each Manager severally has represented and agreed that:

- (i) it has not offered or sold and will not offer or sell in the Hong Kong Special Administrative Region of the People’s Republic of China (“Hong Kong”), by means of any document, any Notes other than (i) to “professional investors” as defined in the Securities and Futures Ordinance (Cap. 571) of Hong Kong (the “SFO”) and any rules made under the SFO, or (ii) in other circumstances which do not result in the document being a “prospectus” as defined in the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32) of Hong Kong (“CO”) or which do not constitute an offer to the public within the meaning of the CO; and
- (ii) it has not issued or had in its possession for the purposes of issue, and will not issue or have in its possession for the purposes of issue, whether in Hong Kong or elsewhere, any advertisement, invitation or document relating to the Notes, which is directed at, or the contents of which are likely to be accessed or read by, the public in Hong Kong (except if permitted to do so under the securities laws of Hong Kong) other than with respect to the Notes which are or are intended to be disposed of (i) only to persons outside Hong Kong or (ii) only to “professional investors” as defined in the SFO and any rules made thereunder.

Singapore

Each Manager has acknowledged that this Offering Circular has not been and will not be registered as a prospectus with the Monetary Authority of Singapore under the Securities and Futures Act, Chapter 289 of

Singapore (the “SFA”). Accordingly, each of the Managers severally has represented and agreed that it has not offered or sold any Notes or caused the Notes to be made the subject of an invitation for subscription or purchase, will not offer or sell the Notes or cause the Notes to be made the subject of an invitation for subscription or purchase, and has not circulated or distributed, nor will it circulate or distribute, this Offering Circular or any other document or material in connection with the offer or sale, or invitation for subscription or purchase, of the Notes, whether directly or indirectly, to any person in Singapore other than (i) to an institutional investor under Section 274 of the SFA, (ii) to a relevant person pursuant to Section 275(1), or any person pursuant to Section 275(1A), and in accordance with the conditions specified in Section 275, of the SFA, or (iii) otherwise pursuant to, and in accordance with the conditions of, any other applicable provision of the SFA.

Where the Notes are subscribed or purchased under Section 275 of the SFA by a relevant person which is:

- (a) a corporation (which is not an accredited investor (as defined in Section 4A of the SFA)) the sole business of which is to hold investments and the entire share capital of which is owned by one or more individuals, each of whom is an accredited investor; or
- (b) a trust (where the trustee is not an accredited investor) whose sole purpose is to hold investments and each beneficiary of the trust is an individual who is an accredited investor,

securities (as defined in Section 239(1) of the SFA) of that corporation or the beneficiaries’ rights and interest (howsoever described) in that trust shall not be transferred within six months after that corporation or that trust has acquired the Notes pursuant to an offer made under Section 275 of the SFA except:

- (1) to an institutional investor or to a relevant person defined in Section 275(2) of the SFA, or to any person arising from an offer referred to in Section 275(1A) or Section 276(4)(i)(B) of the SFA;
- (2) where no consideration is or will be given for the transfer;
- (3) where the transfer is by operation of law;
- (4) as specified in Section 276(7) of the SFA; or
- (5) as specified in Regulation 32 of the Securities and Futures (Offers of Investments) (Shares and Debentures) Regulations 2005 of Singapore.

Italy

The offering of the Notes has not been registered pursuant to Italian securities legislation and, accordingly, no Notes may be offered, sold or delivered, nor may copies of this Offering Circular or of any other document relating to the Notes be distributed in the Republic of Italy, except:

- (i) to professional investors (*operatori qualificati*), as defined in Article 31, second paragraph, of CONSOB Regulation No. 11522 of July 1, 1998, as amended; and
- (ii) in circumstances which are exempt from the rules on solicitation of investments pursuant to Article 100 of Legislative Decree No. 58 of February 24, 1998, as amended (the “Financial Services Act”) and Article 33, first paragraph, of CONSOB Regulation No. 11971 of May 14, 1999, as amended.

Any offer, sale or delivery of the Notes or distribution of copies of this Offering Circular or any other document relating to the Notes in the Republic of Italy under (i) or (ii) above must be:

- (a) made by an investment firm, bank or financial intermediary permitted to conduct such activities in the Republic of Italy in accordance with the Financial Services Act and Legislative Decree No. 385 of September 1, 1993, as amended; and
- (b) in compliance with any other applicable laws and regulations.

General

No action has been taken by us or any of the Managers that would, or is intended to, permit a public offer of the Notes, or possession or distribution of this Offering Circular or any other offering material, in any country or jurisdiction where any such action for that purpose is required. Accordingly, each Manager has undertaken that it will comply with all applicable securities laws and regulations in each jurisdiction in which it purchases, offers, sells or delivers Notes or has in its possession or distributes this Offering Circular or any other offering material.

Other Relationships

In the ordinary course of business, some of the Managers and certain of their affiliates engage from time to time in various financing and investment banking transactions with SBC and its affiliates, for which they have received customary compensation.

LEGAL MATTERS

Certain legal matters in connection with the Notes will be passed upon for SBC by Lee & Ko, Korean counsel for SBC. Certain legal matters with respect to the Notes will be passed upon for the Managers by Cleary Gottlieb Steen & Hamilton LLP, United States counsel for the Managers. Lee & Ko may rely on Cleary Gottlieb Steen & Hamilton LLP as to all matters of New York law. Cleary Gottlieb Steen & Hamilton LLP may rely on Lee & Ko as to all matters of Korean law.

INDEPENDENT AUDITORS

The SME Fund's audited annual financial statements as of the years ended December 31, 2014 and 2015 included in this Offering Circular have been audited by Grant Thornton Daejoo, independent auditors, as stated in their report appearing herein.

INDEX TO FINANCIAL STATEMENTS OF THE SME FUND

	<u>Page</u>
Independent Auditors' Report	F-2
Statements of Financial Position as of December 31, 2015 and 2014	F-4
Statements of Income for the years ended December 31, 2015 and 2014	F-6
Statements of Changes in Equity for the years ended December 31, 2015 and 2014	F-7
Statements of Cash Flows for the years ended December 31, 2015 and 2014	F-8
Notes to the Financial Statements	F-10

Independent Auditors' Report

Based on a report originally issued in Korean

To the Board of Directors of
Small and Medium Business Corporation, manager of the Fund for Establishment and Promotion of SME

We have audited the accompanying financial statements of the Fund for Establishment and Promotion of SME (the "SME Fund"), managed by the Small and Medium Business Corporation, which comprise the statement of financial position as of December 31, 2015, and the related statement of comprehensive income, changes in equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the Republic of Korea, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibilities

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audit in accordance with auditing standards generally accepted in the Republic of Korea. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Group as of December 31, 2015, and its financial performance and its cash flows for the year then ended in accordance with accounting principles generally accepted in the Republic of Korea.

Other Matter

The accompanying statement of financial position of the Company as of December 31, 2014, and the related statement of operations, changes in equity and cash flows for the year then ended, were audited by other auditor, whose report thereon dated February 10, 2015, expressed an unqualified opinion.

The procedures and practices utilized in the Republic of Korea to audit financial statements may differ from those generally accepted and applied in other countries. Accordingly, this report is for use by those knowledgeable about Korean auditing standards and their application in practice

Grant Thornton Daejeon

Seoul, Korea

February 12, 2016

This audit report is effective as of February 12, 2016, the independent auditors' report date. Accordingly, certain material subsequent events or circumstances may have occurred during the period from the auditors' report date to the time this audit report is used. Such events and circumstances could significantly affect the accompanying financial statements and may result in modifications to this report.

FUND FOR ESTABLISHMENT AND PROMOTION OF SME
(managed by the Small and Medium Business Corporation)
Statements of Financial Position
AS OF DECEMBER 31, 2015 and 2014

<u>December 31,</u>	(In Korean won)	
	2015	2014
Assets		
Current assets:		
(1) Quick assets:		
Cash and cash equivalents	234,039,045,672	118,041,555,510
Current portion of held-to-maturity securities (Note 4)	—	5,806,489,307
Accounts and notes receivable—trade, less allowance for doubtful accounts of ₩2,733 million in 2015 and ₩1,689 million in 2014	5,802,861,168	159,349,300
Accounts and notes receivable—other, less allowance for doubtful accounts of ₩1,981 million in 2015 and ₩1,981 million in 2014	376,059,918	5,750,565,791
Short term loans, less allowance for doubtful accounts of ₩81,057 million in 2015 and ₩114,173 million in 2014 (Note 6)	2,944,715,258,496	2,711,398,127,391
Accrued revenues	15,771,901,679	18,748,997,729
Prepaid expenses	165,640,302	189,245,549
Prepaid income taxes (Note 21)	412,762,020	443,738,498
	3,201,283,529,255	2,860,538,069,075
(2) Inventories (Notes 2, 11):		
Land for building lot	5,149,143,713	5,149,143,713
	5,149,143,713	5,149,143,713
(3) Other currents assets:		
Derivative assets (Note 18)	94,943,182,984	—
	94,943,182,984	—
Total Current assets	3,301,375,855,952	2,865,687,212,788
Non-current assets:		
(1) Investments:		
Available-for-sale securities (Note 4)	159,569,555,052	139,897,741,173
Equity method accounted investments (Note 5, 7)	1,624,676,862,094	1,397,507,640,680
Long-term loans, less allowance for doubtful accounts of ₩566,093 million in 2015 and ₩403,352 million in 2014 (Note 6)	10,633,964,470,600	11,628,654,057,410
Long-term loans to employees	5,786,816,644	6,529,887,808
	12,423,997,704,390	13,172,589,327,071
(2) Tangible assets (Notes 2, 8, 9):		
Property and equipment, net	171,597,473,445	194,175,473,038
(3) Intangible assets (Note 10):		
Intangible assets	7,166,437,977	7,484,451,970
(4) Other non-currents assets (Notes 7, 18):		
Long-term guarantee deposits	49,102,900,211	44,244,956,593
Derivative assets	27,335,628,638	101,991,991,874
	255,202,440,271	347,896,873,475
Total Non-current assets	12,679,200,144,661	13,520,486,200,546
Total assets	15,980,576,000,613	16,386,173,413,334

<i>December 31,</i>	(In Korean won)	
	2015	2014
Liabilities and stockholder's equity		
Current liabilities:		
Accounts and notes payable—other	1,760,794,330	2,920,456,497
Accrued expenses	70,661,532,121	75,136,008,539
Advances from customers	3,743,912,976	3,443,627,104
Unearned revenue	289,635,334	492,078,944
Withholdings	6,348,463,507	4,129,301,735
Current portion of debt, less present value discount of ₩ 290 million in 2015 and ₩ 153 million in 2014 (Note 12, 13, 14, 16)	3,757,272,455,379	3,254,595,739,957
Derivative liabilities (Note 18)	—	3,336,104,097
	<u>3,840,076,793,647</u>	<u>3,344,053,316,873</u>
Non-current liabilities:		
Debentures, less present value discount ₩1,629 million in 2015 and ₩2,163 million in 2014 (Note 12, 13, 16)	10,361,791,885,848	11,534,413,339,363
Long-term borrowings (Note 12, 14)	3,868,800,000	8,407,200,000
Provision for retirement and severance benefits (Note 15)	24,113,993,834	21,421,256,011
Derivative liabilities (Note 18)	84,508,251,719	35,310,316,608
Deposits received (Note 17)	2,875,824,676	2,687,771,018
	<u>10,477,158,756,077</u>	<u>11,602,239,883,000</u>
Total liabilities	<u>14,317,235,549,724</u>	<u>14,946,293,199,873</u>
Fund's equity:		
Capital contributions	2,726,334,345,415	2,537,827,345,415
Capital surplus	5,376,404,959	5,376,404,959
Accumulated other comprehensive income	80,345,368,960	57,569,767,985
Accumulated deficit	(1,148,715,668,445)	(1,160,893,304,898)
Total Fund's equity	<u>1,663,340,450,889</u>	<u>1,439,880,213,461</u>
Total liabilities and stockholders' equity	<u>15,980,576,000,613</u>	<u>16,386,173,413,334</u>

See accompanying notes to the financial statements.

FUND FOR ESTABLISHMENT AND PROMOTION OF SME
(managed by the Small and Medium Business Corporation)
Statements of Income
FOR THE YEARS ENDED DECEMBER 31, 2015 and 2014

<i>Year Ended December 31,</i>	(In Korean won)	
	2015	2014
Operating revenues (Note 7)	906,810,280,952	961,995,164,423
Operating expenses (Notes 25)	969,345,828,108	973,251,672,983
Operating income (loss)	(62,535,547,156)	(11,256,508,560)
Other income		
Interest income	2,400,206,253	2,839,595,108
Reversal of allowance for doubtful accounts	55,169,087	—
Foreign currency translation gain, net (Note 16)	(29,109,222,961)	(17,544,656,511)
Equity in net gain of equity method accounted investments (Note 5)	10,625,806,236	17,151,326,688
Loss on valuation of debentures, net	53,048,267,457	(11,397,656,512)
Gain on valuation of derivative instruments, net (Note 18)	(23,939,044,424)	28,942,313,066
Gain on cancellation of derivative instruments, net (Note 18)	2,362,987,735	—
Compensation for the breach of contracts	749,638,192	209,566,060
Loss on disposal of equity method accounted investments, net	(3,429,329,025)	(3,738,472,006)
Gain on disposal of property and equipment, net	46,836,818,297	1,726,127,344
Others, net	8,687,999,307	5,478,785,908
	<u>68,289,296,154</u>	<u>23,666,929,145</u>
Income (Loss) before income taxes	5,753,748,998	12,410,420,585
Income taxes (Note 21)	(6,423,887,455)	(10,660,128,830)
Net income (Notes 20)	<u>12,177,636,453</u>	<u>23,070,549,415</u>

See accompanying notes to the financial statements.

FUND FOR ESTABLISHMENT AND PROMOTION OF SME
(managed by the Small and Medium Business Corporation)
Statements of Changes in Equity
FOR THE YEARS ENDED DECEMBER 31, 2015 and 2014

	(In Korean won)				Total fund's equity
	Capital contribution	Capital surplus	Accumulated other comprehensive income	Accumulated deficit	
Balance at 01-Jan-14	2,430,964,345,415	5,376,404,959	19,774,765,770	(1,183,963,854,313)	1,272,151,661,831
Government subsidies	106,863,000,000				106,863,000,000
Gain on valuation of available-for-sale securities, net			40,044,882,024		40,044,882,024
Change in equity of equity method investee			3,605,816,601		3,605,816,601
Gain on valuation of currency swap contracts			(5,855,696,410)		(5,855,696,410)
Net income (loss)				23,070,549,415	23,070,549,415
Balance at 31-Dec-14	<u>2,537,827,345,415</u>	<u>5,376,404,959</u>	<u>57,569,767,985</u>	<u>(1,160,893,304,898)</u>	<u>1,439,880,213,461</u>
Balance at 01-Jan-15	2,537,827,345,415	5,376,404,959	57,569,767,985	(1,160,893,304,898)	1,439,880,213,461
Government subsidies	188,507,000,000				188,507,000,000
Gain on valuation of available-for-sale securities, net			16,980,108,211		16,980,108,211
Change in equity of equity method investee			14,478,940,479		14,478,940,479
Gain on valuation of currency swap contracts			(8,683,447,715)		(8,683,447,715)
Net income (loss)				12,177,636,453	12,177,636,453
Balance at 31-Dec-15	<u>2,726,334,345,415</u>	<u>5,376,404,959</u>	<u>80,345,368,960</u>	<u>(1,148,715,668,445)</u>	<u>1,663,340,450,889</u>

See accompanying notes to the financial statements.

FUND FOR ESTABLISHMENT AND PROMOTION OF SME
(managed by the Small and Medium Business Corporation)
Statements of Cash Flows
FOR THE YEARS ENDED DECEMBER 31, 2015 and 2014

<i>Years Ended December 31,</i>	(In Korean won)	
	2015	2014
Cash flows from operating activities		
Net income	12,177,636,453	23,070,549,415
Addition of expenses not involving cash outflows & Deduction of revenues not involving cash inflows		
Accrual for retirement and severance benefits	6,450,070,224	5,496,533,819
Depreciation	8,456,593,693	7,643,584,844
Amortization	2,483,666,254	2,313,561,005
Bad debts expenses for accountable and note receivables—trade	1,044,809,556	54,915,834
Bad debts expenses for long-term and short-term loans	251,104,218,785	196,542,067,318
Reversal of allowance for doubtful accounts	(55,169,087)	—
Amortization of discount on current portion of debts	—	81,881,144
Amortization of discount on debentures	1,083,835,705	963,177,228
Loss on redemption of debentures	—	—
Foreign currency translation gain, net	29,109,222,961	17,544,656,511
Equity in net gain of equity method accounted investments	(10,625,806,235)	(17,151,326,688)
Loss on impairment of available-for-sale-securities, net of reversal	3,080,713,017	5,293,272,540
Loss on impairment of held-to-maturity securities, net of reversal	(4,205,238,442)	(4,067,553,802)
(Gain) loss on valuation of debentures, net	(53,048,267,457)	11,397,656,512
(Gain) loss on valuation of derivative instruments, net	23,939,044,424	(28,942,313,066)
Gain on cancellation of derivative instruments, net	(2,362,987,735)	
Gain on disposal of property and equipment, net	(46,836,818,297)	(1,726,127,344)
Gain on disposal of available-for-sale securities, net	(5,656,620,577)	(11,364,307,856)
Loss on disposal of equity method accounted investments, net	3,429,329,025	3,738,472,006
Others, net	(930,848,867)	(343,111,245)
Changes in assets and liabilities resulting from operating activities		
Accounts and notes receivable—trade	(6,687,503,837)	371,655,825
Accounts and notes receivable—other	5,477,291,756	(4,390,065,193)
Accrued revenues	2,977,096,050	1,699,163,111
Prepaid expenses	23,605,247	1,567,350
Prepaid income taxes	30,976,478	328,560,296
Accounts and notes payable—other	(1,159,662,167)	1,678,223,270
Accrued expenses	(4,474,476,418)	(5,859,487,576)
Deposits received	188,053,658	(2,083,790,532)
Unearned income	(202,443,610)	(59,021,456)
Withholdings	2,219,161,772	(84,541,538)
Advances from customers	300,285,872	2,727,097,153
Payment of retirement and severance benefits	(1,264,647,087)	(815,189,735)
Deposit for severance benefits	(2,092,496,484)	(2,054,413,599)
Others, net	(6,423,887,455)	(10,660,128,830)
Net cash provided by operating activities	<u>207,548,737,175</u>	<u>191,345,216,721</u>

<i>Years Ended December 31,</i>	(In Korean won)	
	2015	2014
Cash flows from investing activities		
Proceeds from disposal of available-for-sale securities	13,020,760,988	16,478,859,911
Proceeds from disposal of held-to-maturity securities	9,976,734,971	5,598,403,770
Proceeds from disposal of equity method accounted investments	590,000,000	900,000,000
Decrease in short-term loans, net	4,404,514,503,287	1,772,634,407,291
Increase in long-term loans, net	(3,902,068,086,574)	(1,702,987,334,047)
Increase in long-term loans to employees, net	743,071,164	(6,083,190)
Proceeds from disposal of property and equipment	66,561,422,275	3,467,936,602
Decrease in guarantee deposits	10,180,734,800	22,322,443,338
Acquisition of equity method accounted investments	(202,000,000,000)	(100,000,000,000)
Acquisition of property and equipment	(5,603,198,078)	(30,092,152,291)
Acquisition of intangible assets	(2,173,911,428)	(2,579,285,625)
Increase in guarantee deposits	(15,038,678,418)	(26,947,758,296)
Net cash provided by(used in) investing activities	<u>378,703,352,987</u>	<u>(41,210,562,537)</u>
Cash flows from financing activities		
Increase in government contributions	188,507,000,000	106,863,000,000
Proceeds from issuance of debentures	2,600,000,000,000	5,690,000,000,000
Repayment of current portion of long-term borrowings . . .	(3,258,761,600,000)	(6,064,496,000,000)
Net cash used in financing activities	<u>(470,254,600,000)</u>	<u>(267,633,000,000)</u>
Net increase in cash and cash equivalents	115,997,490,162	(117,498,345,816)
Cash and cash equivalents at beginning of year	<u>118,041,555,510</u>	<u>235,539,901,326</u>
Cash and cash equivalents at end of year	<u>234,039,045,672</u>	<u>118,041,555,510</u>

See accompanying notes to the financial statements.

FUND FOR ESTABLISHMENT AND PROMOTION OF SME
(managed by the Small and medium Business Corporation)
Notes to the Financial Statements
December 31, 2015 and 2014

1. General / The Company

The Government established the Fund for the Establishment and Promotion of Small and Medium Enterprises (the “SME Fund”) under Article 63 of the Small and Medium Enterprises Promotion Act (the “SME Promotion Act”) with an aim of securing financial resources necessary for facilitating the start of new small and medium enterprises, balanced development of industries, establishment of industrial infrastructure, expansion of business sphere and structural advancement. The Fund is operated and managed under the SME Promotion Act, National Finance Act and National Accounting Act.

The SME Fund was launched as the Fund for Promotion of Small and Medium Enterprises under Article 12 of the Promotion of Small and Medium Enterprises Act which was enacted in December 1978. The SME Fund was renamed as the Fund for Establishment and Promotion of Small and Medium Enterprises due to the amendment of the Promotion of Small and Medium Enterprises and Encouragement of Purchase of their Products Act in November 1995. In January 1996, the SME Fund absorbed the Support Fund for Establishment of Small and Medium Enterprise, the Upbringing Fund for Local Small and Medium Enterprises and the Support Fund for Small and Medium Enterprises Moved into Agro-Industrial Complex. The SME Fund was converted to a Public Fund due to the amendment of the Framework Act on Fund Management in December 1999. The SME Fund absorbed the Industrial Foundation Fund which had been under the jurisdiction of the Ministry of Knowledge Economy and the Fund for Promotion of Agro-Industrial Complex in December 2001 and January 2009, respectively, the SME Fund was renamed as the Fund for the Establishment and Promotion of Small and Medium Enterprises (the “SME Fund”).

The SME Fund is used to support the small and medium enterprises under Article 67 of the SME Promotion Act. Detailed purposes of the SME fund are as follows:

- (1) Support for establishment and business conversion
- (2) Support to small and medium enterprises for the development of technology
- (3) Support to small and medium enterprises for export and finding markets
- (4) Support policies for small and medium enterprises
- (5) Support to small and medium enterprises for structural advancement in human resources
- (6) Establishment and venture investment
- (7) Support to conventional market, small traders and enterprisers
- (8) Support to small and medium enterprises for business stability
- (9) Support to small and medium enterprises for new growth

2. Basis of Preparation

- (1) Statement of Compliance

The SME Fund prepared the financial statements in accordance with Accounting Standards for Non-Public Entities in the Republic of Korea (“K-GAAP for Non-Public Entities”) which have been effective since January 1, 2011.

(2) Basis of Measurement

The financial statements have been prepared on the historical cost basis, except for the following items in the statement of financial position:

- derivative instruments and hedged borrowings are measured at fair value
- available-for-sale financial assets measured at fair value

(3) Use of Estimates and Judgments

The preparation of the financial statements in conformity with K-GAAP for Non-Public Entities requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Information about critical judgments in applying accounting policies that have the most significant effect on the amounts recognized in the financial statements is included in the following note:

Note 6—Short-term and Long-term Loans

Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment within the next financial year are included in the following note:

Note 17—Commitments and Contingencies

3. Significant Accounting Policies

The significant accounting policies applied by the SME Fund in preparation of its financial statements are included below.

(1) Cash and cash equivalents

Cash and cash equivalents comprise cash on hand, demand deposits, and short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. The SME Fund considers investments with maturities of three months or less on acquisition date to be cash and cash equivalents.

(2) Inventories

The acquisition costs of inventories include costs of purchase or production and other direct costs. Unit cost of inventories is determined by the specific identification method. Inventories are valued at the lower of acquisition cost and net realizable value. Inventory obsolescence losses occurred in the normal course of business are charged to operating expenses.

(3) Financial instruments

① General

The SME Fund recognizes financial assets or financial liabilities in the statements of financial position when the SME Fund becomes the counterparty of the contract. Upon initial recognition, non-derivative financial instruments (other than financial instruments at fair value through profit or loss) are measured at their fair value plus (less) transaction costs that are directly attributable to the acquisition of the financial asset or issuance of the financial instrument.

Subsequently, financial assets or financial liabilities, except for equity instruments, derivatives and financial instruments at fair value through profit or loss, are measured at amortized cost.

A financial asset measured at amortized cost is assessed at each reporting date to determine whether there is objective evidence that the carrying amount of the investment may not be recoverable. If there is such objective evidence, the SME Fund accounts for recognition and measurement of impairment of the financial instruments according to policies as further described in the debt and equity securities section below.

The allowance for doubtful accounts is estimated based on an analysis of individual accounts and past experience of collection and presented as a deduction from financial assets. The SME Fund classifies corporate loans based on the borrowers' credit rating by considering the borrowers' business operations, financial position and estimated future cash flows (Forward Looking Criteria). An allowance is then calculated based on the classification of the loans by using the prescribed percentages of 0.85~0.90% for 'normal', 7.0% for 'precautionary', 20.0% for 'substandard', 50.0% for 'doubtful' and 100% for 'estimated loss'.

When the SME Fund transfers financial assets, except for investments in securities, the SME Fund derecognizes the assets when the following conditions are met:

- The SME Fund does not have rights to ownership of the transferred assets;
- The SME Fund does not have effective control over the transferred assets; and
- The transferee has the right to sell the assets.

If the transfer does not meet the above conditions, it is accounted for as a secured borrowing transaction.

② Securities

Upon acquisition, the SME Fund classifies debt and equity securities (excluding investments in subsidiaries, associates and joint ventures) into the following categories: held-to-maturity, available-for-sale, and trading securities. The SME Fund reviews their classification at the end of each reporting period. Investments in debt securities on which the SME Fund has the positive intent and ability to hold to maturity are classified as held-to-maturity. Securities that are acquired principally for the purpose of selling in the short term are classified as trading securities. Investments not classified as either held-to-maturity or trading securities are classified as available-for-sale securities.

Subsequently, held-to-maturity investments are carried at amortized cost and interest income is recognized in profit or loss using the effective interest method. Trading securities and available-for-sale securities are subsequently carried at fair value. Available-for-sale equity securities that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are recognized at cost. For equity securities that have a quoted market price, their market price is considered to be fair value and the market price is the closing price on the reporting date.

For debt securities which do not have a quoted market price in an active market, fair value is measured at discounted estimated future cash flows. The discount rate used is the corresponding rates reflecting the debt securities' credit rating as quoted by a credit rating agency, if any.

For investment funds that do not have a quoted market price in an active market, their fair value is the standard selling price as reported by the fund management agent.

Gains and losses arising from changes in the fair value of trading securities are included in the statement of income in the period in which they arise. Gains and losses arising from changes in the fair value of available-for-sale securities (net of tax) are recognized as other comprehensive income directly in equity. Accumulated other comprehensive income is recognized as profit or loss when the investments are impaired or sold.

At each reporting date, the SME Fund reviews whether events or changes in circumstances indicate that the carrying amount of the investments may not be recoverable. Impairment losses are recognized when the reliably estimated recoverable amounts are less than the carrying amount and it is not obvious that the investment is other than impaired.

An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss is recorded and the reversal of an impairment loss does not exceed the carrying amount that would have been determined without having recognized an impairment loss in prior years. The reversal is recognized in profit or loss.

Trading securities are presented as current assets. Available-for-sale securities that mature within one year from the end of the reporting period or where the likelihood of disposal within one year from the end of the reporting period is probable, are presented as current assets. Held-to-maturity securities, which mature within one year from the end of the reporting period, are presented as current assets. The other available-for-sale securities and held-to-maturity securities are presented separately in non-current assets.

③ Derivatives

The SME Fund holds foreign exchange forwards, interest rate swaps and foreign currency swaps to hedge its foreign currency and interest rate risk exposures. Derivatives are initially recognized at fair value on the date a derivative contract is entered into and are subsequently re-measured at their fair value. Attributable transaction costs are recognized in profit or loss when incurred. Embedded derivatives are separated from the host contract and accounted for separately if the economic characteristics and risks of the host contract and the embedded derivative are not closely related, and a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative. Changes in the fair value of separable embedded derivatives are recognized immediately in the statement of net loss.

The SME Fund has the following hedging relationships:

- fair value hedge—to avoid the exposure to changes in fair value of a recognized asset or liability or an unrecognized firm commitment, or an identified portion of such an asset, liability or firm commitment, that is attributable to a particular risk and could affect profit or loss;
- cash flow hedge—to avoid the exposure to variability in cash flows that is attributable to a particular risk associated with a recognized asset or liability or a highly probable forecasted transaction and could affect profit or loss;

The SME Fund documents, at the inception of the transaction, the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. The SME Fund also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting the changes in fair values or cash flows of hedged items.

1) Fair value hedge

Profit or loss on the valuation of a hedging instrument and profit or loss in the valuation of a hedged item that is attributable to a particular risk are recognized as profit or loss in the statement of income.

The SME Fund discontinues hedge accounting for fair value hedges prospectively if:

- the hedging instrument expires or is sold, terminated or exercised; or
- the hedge no longer meets the criteria for hedge accounting.

Adjustments to a hedged item are amortized and recognized as profit or loss from the date hedge accounting is discontinued.

2) Cash flow hedge

The portion of the gain or loss on the hedging instrument that is determined to be an effective hedge to reduce the risk of future cash flow variability is recognized in other comprehensive income.

Subsequently other comprehensive income is reclassified

- from equity to profit or loss in the same periods during which the hedged forecasted cash flows affect profit or loss; or
- from equity to the associated asset or liability based on the nature of the forecasted transaction.

If the hedging instrument no longer meets the criteria for hedge accounting, expires or is sold, terminated, exercised, or the designation is revoked, then hedge accounting is discontinued prospectively. However, if the forecasted transaction is expected to occur, the cumulative gain or loss on the hedging instrument that has been recognized in other comprehensive income is reclassified to profit or loss in the periods during which the forecasted transaction occurs. If the forecasted transaction is no longer expected to occur, the balance in other comprehensive income is recognized immediately in profit or loss.

Investments in associates on which the SME Fund has the ability to significantly influence the financial and operating policies are accounted for using the equity method and are initially recognized at cost.

The SME Fund's share of its post-acquisition profits or losses in investments in associates is recognized in the statement of income, and its share of post-acquisition movements in equity is recognized in equity. The cumulative post-acquisition movements are adjusted against the carrying amount of each investment.

When the SME Fund's share of losses in an associate equals or exceeds its interest in the associate, including preferred stock or other long term loans and receivables issued by the associate, the SME Fund does not recognize further losses, unless it has incurred obligations or made payments on behalf of the associate.

The SME Fund's investments in associates include goodwill identified on the acquisition date (net of any accumulated impairment loss). Goodwill is calculated as the excess of the acquisition cost of an investment in an associate over the SME Fund's share of the fair value of the identifiable net assets acquired. Goodwill is amortized using the straight-line method over its estimated useful life. Amortization of goodwill is recorded together with equity income (losses).

(4) Investments in associates and subsidiaries

The SME Fund recognizes bargain purchases (where there is negative goodwill) as profit or loss upon acquisition of the investment.

Unrealized gains on transactions between the SME Fund and its associates are eliminated to the extent of the SME Fund's interest in each associate.

If an associate uses accounting policies or estimates other than those of the SME Fund for like transactions and events in similar circumstances, the SME Fund makes appropriate adjustments to conform the associate's or accounting policies to those of the SME Fund when they are accounted for by the SME Fund using the equity method. However, in the event that accounting policies and estimates differ due to the application of Article 31 of Exceptions to Accounting for Small and Medium-Sized Entities or K-IFRS, no adjustments are made.

(5) Property and equipment

Property and equipment are initially measured at cost. The cost of property and equipment includes the expenditures arising directly from the construction or acquisition of the asset, any costs directly attributable to

bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management and the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located.

Assets acquired through investment in kind or donation are recorded at their fair value upon acquisition. For assets acquired in exchange for a non-monetary asset, the fair value of the asset given up is used to measure the cost of the asset received unless the fair value of the asset received is more clearly evident.

Significant expenditures or improvements extending the useful life of assets are capitalized. Normal maintenance and repairs are charged to expense as incurred.

Depreciation is computed by the declining-balance method and the straight-line method over the estimated useful lives of the assets using rates based on the useful lives of the respective assets as follows:

	<u>Useful lives (years)</u>	<u>Depreciation method</u>
Buildings	40	straight-line
Structures	40	straight-line
Vehicles	5	declining-balance
Furniture and equipment	5	declining-balance
Tools	5	declining-balance
Laboratory equipments	5	declining-balance
Other tangible assets	40	straight-line

Gains and losses on disposal of an item of property and equipment are determined by comparing the proceeds from disposal with the carrying amount of property and equipment and are recognized in profit or loss.

(6) Intangible assets

Costs of intangible assets includes expenditures arising directly from the construction or acquisition of the asset and any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management.

The acquisition costs of intangible assets are amortized on a straight-line basis over estimated useful lives of the assets of five years.

① Research and development costs

The costs in development phase that meets certain criteria are recognized as intangible assets (development costs). Other costs phase are recognized as costs of goods or selling and administrative expenses (development expenses) and the costs in research phase are recognized as selling and administrative expenses (research expenses).

② Subsequent expenditures

The expenditures that occur subsequent to acquisition of intangible assets are capitalized when it is probable the expenditures will generate future economic benefits and the amount can be measured reliably. If those criteria are not met, the expenditures are recognized in profit or loss.

(7) Impairment of assets

The carrying amounts of the SME Fund's non-financial assets, other than assets arising from inventories, deferred tax assets and assets constituting a discontinued operation, are reviewed at the end of the reporting

period to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. Intangible assets that are not yet available for use, irrespective of whether there is any indication of impairment, are tested for impairment annually by comparing their recoverable amount to their carrying amount.

The SME Fund estimates the recoverable amount of an individual asset. If it is impossible to measure the individual recoverable amount of an asset, then the SME Fund estimates the recoverable amount of each cash-generating unit ("CGU"). A CGU is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets. An impairment loss is recognized if the carrying amount of an asset or a CGU exceeds its recoverable amount. Impairment losses are recognized in profit or loss.

Except for impairment losses in respect of goodwill which are never reversed, an impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized.

(8) Retirement and severance benefits

Employees who have been with the SME Fund for more than one year are entitled to lump-sum payments based on salary rates and length of service at the time they leave the SME Fund. The SME Fund's estimated liability under the plan, which would be payable if all employees left at the end of the reporting period, is accrued in the accompanying statements of financial position.

A portion of the liability is covered by an employees' severance benefits trust where the employees have a vested interest in the deposit with the insurance company (or the bank) in trust. The deposit for severance benefits held in trust is, therefore, reflected in the accompanying statements of financial position as a reduction of the liability for retirement and severance benefits.

The SME Fund introduced a pension plan from 2012. Under the Retirement Benefits Regulation, consideration of service requirements under the plan begins from the date when the plan is effective; the period of service prior to the effective date of the plan will continue to be covered by the previous retirement benefits plan.

The SME Fund has both defined benefit pension plan and defined contribution pension plan. For defined contribution plan, each eligible employee receives a fixed amount of pension after retirement. Until the employees retire, the SME Fund accrues, as a liability for retirement and severance benefits, lump-sum payments payable to employees under the assumption that they left the SME Fund as of the end of the reporting period. All employees with a minimum of one year of service are eligible to participate and must elect to participate in the plan. If an employee selected the pension plan upon retirement, the SME Fund accrues estimated benefits based on actuarial assumptions measured at the end of the reporting period at the discounted present value. The SME Fund recognizes all actuarial gains or losses arising from actuarial assumption changes and experiential adjustments in profit or loss as incurred.

The amount of benefit payments depends on the performance of the plan assets and is not guaranteed. The SME Fund recognizes the contribution payable to a defined contribution plan in exchange for that service as an expense.

The combined provision for retirement and severances benefits under the pension plan and those under the existing retirement benefit plan are recorded as the liability for retirement and severance benefits. Pension plan assets, together with the existing retirement and severance benefit deposit and the deposit previously made to the National Pension Fund under the old National Pension Law, as referred to above, are reflected in the accompanying statements of financial position as a reduction of the liability for retirement and severance benefits.

(9) Provisions

Provisions are recognized when all of the following are met:

- an entity has a present obligation as a result of a past event;
- it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and
- a reliable estimate can be made of the amount of the obligation.

Where the effect of the time value of money is material, a provision is recorded at the present value of the expenditures expected to be required to settle the obligation.

Where the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement is recognized as a separate asset when, and only when, it is virtually certain that reimbursement will be received and the expense generated by the provision is presented net of the amount of expected reimbursement.

(10) Income taxes

Income tax on the income or loss for the year comprises current and deferred tax. Current tax is the expected tax payable on the taxable income for the year, using enacted tax rates.

Deferred tax is provided using the asset and liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for tax purposes. The amount of deferred tax provided is based on the expected manner of realization or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the end of the reporting period.

Deferred tax assets and liabilities are classified as current or non-current based on the classification of the related asset or liability for financial reporting or the expected reversal date of the temporary difference for those with no related asset or liability such as loss carryforwards and tax credit carryforwards. The deferred tax amounts are presented as a net current asset or liability and a net non-current asset or liability.

Changes in deferred taxes due to a change in the tax rate, except for those related to items initially recognized outside profit or loss either in other comprehensive income or directly in other equity, are recognized as profit or loss in the current year.

(11) Foreign currency transactions

① Functional and presentation currency

These financial statements are presented in Korean won, which is the SME Fund's functional currency and the currency of the primary economic environment in which the SME Fund operates.

② Foreign currency transactions

Transactions in foreign currencies are translated to the respective functional currencies of the SME Fund at exchange rates at the dates of the transactions. Non-monetary items that are measured in terms of historical cost in foreign currency are retranslated to the exchange rate at the date of the transaction. Non-monetary items that are measured at fair value in foreign currency are retranslated to the functional currency at the exchange rate at the date that the fair value was determined.

When a gain or loss on a non-monetary item is recognized in other comprehensive income, any exchange component of that gain or loss is recognized in other comprehensive income. Conversely, when a gain or loss on a non-monetary item is recognized in profit or loss, any exchange component of that gain or loss is recognized in profit or loss.

(12) Prior period adjustments

Prior period adjustments resulting from other than fundamental errors are charged or credited to net income in the current period.

Fundamental errors are defined as errors with such a significant effect on the financial statements for one or more prior periods that those financial statements can no longer be considered to have been reliable at the date of their issue. Prior period adjustments resulting from fundamental errors are charged or credited to the beginning balance of retained earnings, and the financial statements of the prior year are restated.

(13) Accounting for capital contributions

Contributions received from government are generally recorded in the statement of financial position as capital contributions in the SME Fund's equity. However, both government contributions received specifically for the purpose of compensating the difference between the SME Fund's lending interest rate and market interest rate paid on borrowings, and contributions received specifically to fund other local government projects are recognized as revenues in accordance with Small & Medium Business Administration's accounting standard on capital contributions.

4. Investments in Securities

Current and non-current investments as of December 31, 2015 and 2014 are summarized as follows:

(In millions of won)

		2015		2014	
		Available-for-sale securities	Held-to-maturity securities	Available-for-sale securities	Held-to-maturity securities
Current	Debt securities	₩ —	—	—	5,806
Non-current	Equity securities	159,570	—	139,898	—
	Debt securities	—	—	—	—
		<u>159,570</u>	<u>—</u>	<u>139,898</u>	<u>—</u>
		<u>₩159,570</u>	<u>—</u>	<u>139,898</u>	<u>5,806</u>

(1) Available-for-sale Securities

① Equity securities as of December 31, 2015 and 2014 are summarized as follows:

(In millions of won)

	2015	2014
Marketable securities	₩ 24,947	443
Non-marketable securities	124,560	121,278
Investments in mutual benefit funds	10,063	18,177
	<u>₩159,570</u>	<u>139,898</u>

i) Marketable securities recorded at fair value as of December 31, 2015 and 2014 are summarized as follows:

(In millions of won)

<u>Company</u>	<u>Ownership</u>	<u>2015</u>		<u>2014</u>
		<u>Acquisition cost</u>	<u>Fair value</u>	<u>Book value</u>
Hanchang Paper Co.,Ltd.	0.11%	₩ 31	83	42
Woorio Optical Telecom Co., Ltd.	1.18%	491	813	401
Pharma Research Products Co., Ltd.	3.32%	869	22,206	—
AJIN Industrial Co., Ltd.	1.46%	917	1,254	—
HANJUNGNCS Co., Ltd.	4.78%	1,031	591	—
		<u>₩3,339</u>	<u>24,947</u>	<u>443</u>

ii) Non-marketable securities as of December 31, 2015 and 2014 are summarized as follows:

(In millions of won)

<u>Company</u>	<u>Ownership</u>	<u>Acquisition cost</u>	<u>Net asset</u>	<u>Book value</u>	
				<u>2015</u>	<u>2014</u>
Korea Exchange	3.03%	₩31,370	86,543	86,543	86,461
Korea Enterprise Data Co., Ltd.	4.62%	3,200	4,229	3,200	3,200
HYTC CO.,LTD.	5.88%	1,968	1,675	1,968	—
Wooshin Development Finance Corp.	16.67%	1,667	2,411	1,667	1,667
Kumkangkikun Co., Ltd.	6.02%	1,600	1,369	1,600	1,600
Others (*)		55,405	59,053	29,582	28,350
		<u>₩95,210</u>	<u>155,280</u>	<u>124,560</u>	<u>121,278</u>

(*) The SME Fund recognized the acquisition costs as an impairment loss for non-marketable securities which the business has actually ceased operations. For securities of which net assets value has fallen below 10% of the acquisition costs, the SME Fund considered the recoverability of net assets value is low and recognized the difference between the net assets value and the carrying amount of the securities an impairment loss. In connection with this, The SME Fund recognized expenses for start-up business grants of ₩349 million as operating expenses for the year ended December 31, 2015.

Non-marketable securities are recorded at acquisition costs as the securities are non-marketable and the difference between fair value and acquisition costs is not significant.

iii) Investments in mutual benefit funds as of December 31, 2015 and 2014 are summarized as follows:

(In millions of won)

<u>Company</u>	<u>Ownership</u>	<u>Acquisition cost</u>	<u>Net asset</u>	<u>Book value</u>	
				<u>2015</u>	<u>2014</u>
K&C-Gyeongnam Youth Job Creation	25.51%	₩ 3,350	494	3,350	3,350
Global Star Korea Fund	0.45%	336	3	3	6
Venture Plus Multimedia Investment Association	40.00%	3,000	324	200	200
BTIC Investment Fund I	30.00%	3,000	531	3,000	3,000
Centurion Visual-media Knowledge-based Service Industry Investment Association	35.00%	2,882	158	158	3,500
Centurion Visual-media Investment Association	30.00%	2,286	208	208	214
Asia Pacific Venture Investment Fund	40.00%	3,144	480	3,144	7,907
		<u>₩17,998</u>	<u>2,198</u>	<u>10,063</u>	<u>18,177</u>

(*) The SME Fund recognized the acquisition costs as an impairment loss for investments in mutual benefit funds which the business has actually ceased operations. For securities of which net assets value has fallen below 10% of the acquisition costs, the SME Fund considered the recoverability of net assets value is low and recognized the difference between the net assets value and the carrying amount of the securities as an impairment loss. In connection with this, the SME Fund recognized expenses for start-up business grants of ₩2,730 million as operating expenses for the year ended December 31, 2015.

Venture capital partnership, corporate restructuring partnership and parts and material specialized investment partnership (“Partnership”) has a limited length of duration. As the purpose of the establishment of Partnership is to expand supports for small-to-medium size ventures, to restructure and recover insolvent small-to-medium size firms and to support for developing parts and material industry, the investment was not made for the control purpose. Also, as the investment decisions are made by members of Partnership, the SME Fund accounted the investment at cost rather than apply equity method. However, the SME Fund accounted investment using the equity method for the Partnership of which Korea Venture Investment Corporation, wholly owned by the SME Fund, serves as a member of the Partnership, and the SME Fund owns 20% or more.

Assuming direct investment, net assets value of Partnership is assessed considering the following factors:

(1) the difference between (a) net assets value of Partnership and investment costs for investee and (b) net assets value of investee, and (2) provision for guarantee of loss. The net asset value of investments is determined based on the most recent audited or reviewed financial statements and stock valuation report.

(2) Held-to-maturity securities

① Held-to-maturity securities as of December 31, 2015 and 2014 are summarized as follows:

(In millions of won)

<u>Company</u>	<u>Maturity</u>	<u>2015</u>		<u>2014</u>	
		<u>Acquisition cost</u>	<u>Fair value</u>	<u>Book value</u>	<u>Book value</u>
Current					
SMI XX ABS Securitization Specialty Co. (*1)		5,306	4,684	0	4,684
SMI XXI ABS Securitization Specialty Co. (*1) . . .		<u>5,042</u>	<u>1,122</u>	<u>0</u>	<u>1,122</u>
		<u>10,348</u>	<u>5,806</u>	<u>0</u>	<u>5,806</u>
Non-current					
Government bonds	More than 1 year	—	—	—	—
		<u>₩10,348</u>	<u>5,806</u>	<u>—</u>	<u>5,806</u>

(*1) The SME Fund recognized the recoverable amount as the fair value and the computed difference between the fair value and the acquisition cost is an impairment gain of ₩1,546 million and it is an operating expense for the year ended December 31, 2015.

5. Investments in Associates and Subsidiaries

(1) year ended December 31, 2015

① Investments in companies accounted for using the equity method as of December 31, 2015 are summarized as follows:

(In millions of won, except percentage of ownership)

<u>Company</u>	<u>Percentage of ownership</u>	<u>Cost</u>	<u>Net assets</u>	<u>Balance at December 31, 2015</u>
Small Business Distribution Center Co., Ltd.	100.00%	₩ 175,303	91,663	91,663
Small Business Corporation Registrar.	100.00%	1,925	2,514	2,514
Korea Venture Investment Corp.	100.00%	50,000	76,833	76,833
Korea Fund of Funds	59.14%	<u>1,319,000</u>	<u>1,453,667</u>	<u>1,453,667</u>
		<u>₩1,546,228</u>	<u>1,624,677</u>	<u>1,624,677</u>

② Changes in the opening and closing balances of investments in companies accounted for using the equity method for the year ended December 31, 2015 are as follows:

(In millions of won)

<u>Company</u>	<u>Beginning Balance</u>	<u>Acquisitions</u>	<u>Gains from Equity method</u>	<u>Changes from equity method</u>	<u>Other increase (decrease)</u>	<u>Year-end balance</u>
Small Business Distribution Center Co., Ltd.	₩ 102,627	—	(10,964)	—	—	91,663
Small Business Corporation Registrar	2,355	—	159	—	—	2,514
Korea Venture Investment Corp. (*1)	75,678	—	1,738	7	(590)	76,833
Korea Fund of Funds (*2)	1,216,848	202,000	19,693	18,555	(198,571)	1,453,667
Total	1,397,508	202,000	10,626	18,562	(4,019)	1,624,677

(*1) Other decrease of Korea Venture Investment Corp. is due to dividends received from investments.

(*2) ₩ 3,429 million losses from the change in equity of equity method is recognized in the other gains.

③ Condensed financial statements of investee companies are summarized as follows

(In millions of won)

<u>Company</u>	<u>Total Asset</u>	<u>Total Liability</u>	<u>Total Net Assets</u>	<u>Total Sales</u>	<u>Net Income(Loss)</u>
Small Business Distribution Center Co., Ltd.	₩ 219,289	127,626	91,663	67,964	(10,964)
Small Business Corporation Registrar. (*1)	3,536	1,022	2,514	5,622	159
Korea Venture Investment Corp. (*1)	80,761	3,928	76,833	13,617	1,738
Korea Fund of Funds (*2)	2,463,453	5,581	2,457,872	110,013	32,137

(*1) The SME Fund accounted for its investment by using the equity method of accounting based on the unaudited financial statements as it was unable to obtain the audited financial statements and performed procedures to verify the unaudited financial statements.

(*2) Financial statements reviewed as of June 30, 2015 and for the six-month period ended have been used and major changes that occurred after June 30, 2015 were reflected when accounting for the equity method.

(2) year ended December 31, 2014

① Investments in companies accounted for using the equity method as of December 31, 2014 are summarized as follows:

(In millions of won, except percentage of ownership)

<u>Company</u>	<u>Percentage of ownership</u>	<u>Cost</u>	<u>Net assets</u>	<u>Balance at December 31, 2014</u>
Small Business Distribution Center Co., Ltd.	100.00%	₩ 175,303	102,627	102,627
Small Business Corporation Registrar.	100.00%	1,824	2,355	2,355
Korea Venture Investment Corp.	100.00%	60,000	75,678	75,678
Korea Fund of Funds	60.90%	1,117,000	1,998,109	1,216,848
		₩1,354,127	2,178,769	1,397,508

② Changes in the opening and closing balances of investments in companies accounted for using the equity method for the year ended December 31, 2014 are as follows:

(In millions of won)

<u>Company</u>	<u>Beginning Balance</u>	<u>Gains from Equity method</u>	<u>Changes from equity method</u>	<u>Other increase (decrease)</u>	<u>Year-end balance</u>
Small Business Distribution Center					
Co., Ltd	₩ 101,712	915	—	—	102,627
Small Business Corporation Registrar	2,232	123	—	—	2,355
Korea Venture Investment Corp. (*1)	73,916	2,672	(10)	(900)	75,678
Korea Fund of Funds (*2)	<u>1,102,502</u>	<u>13,442</u>	<u>4,632</u>	<u>96,262</u>	<u>1,216,848</u>
Total	<u>1,280,372</u>	<u>17,152</u>	<u>4,622</u>	<u>95,362</u>	<u>1,397,508</u>

③ Changes in the opening and closing balances of investments in companies accounted for using the equity method for the year ended December 31, 2014 are as follows:

<u>Company</u>	<u>Total Asset</u>	<u>Total Liability</u>	<u>Total Net Assets</u>	<u>Total Sales</u>	<u>Net Income (Loss)</u>
Small Business Distribution Center					
Co., Ltd	₩ 194,732	92,105	102,627	75,708	892
Small Business Corporation					
Registrar. (*1)	3,426	1,071	2,355	5,156	128
Korea Venture Investment Corp. (*1)	80,018	4,340	75,678	11,394	2,907
Korea Fund of Funds (*2)	<u>2,002,650</u>	<u>4,541</u>	<u>1,998,109</u>	<u>54,489</u>	<u>29,135</u>

(*1) The SME Fund accounted for its investment by using the equity method of accounting based on the unaudited financial statements as it was unable to obtain the audited financial statements and performed procedures to verify the unaudited financial statements.

(*2) Financial statements reviewed as of June 30, 2014 and for the six-month period ended have been used and major changes that occurred after June 30, 2014 were reflected when accounting for the equity method.

6. Short-term and Long-term Loans

(1) Short-term and long-term loans as of December 31, 2015 are as follows:

(In millions of won)

		<u>Short-term loans</u>	<u>Long-term loans</u>	<u>Total</u>
Direct loans	General loans	₩1,842,892	5,748,984	7,591,876
	Loans to venture capitals	620	4,997	5,617
	Sub-total	<u>1,843,512</u>	<u>5,753,981</u>	<u>7,597,493</u>
Indirect loans		<u>1,182,260</u>	<u>5,446,077</u>	<u>6,628,337</u>
	Sub-total	<u>3,025,772</u>	<u>11,200,058</u>	<u>14,225,830</u>
Doubtful accounts		<u>(81,057)</u>	<u>(566,093)</u>	<u>(647,150)</u>
Total		<u>2,944,715</u>	<u>10,633,965</u>	<u>13,578,680</u>

Short-term and long-term loans as of December 31, 2014 are as follows:

(In millions of won)

		<u>Short-term loans</u>	<u>Long-term loans</u>	<u>Total</u>
Direct loans	General loans	₩1,389,013	5,066,076	6,455,089
	Loans to venture capitals	620	4,997	5,617
	Sub-total	<u>1,389,633</u>	<u>5,071,073</u>	<u>6,460,706</u>
Indirect loans		<u>1,435,939</u>	<u>6,960,933</u>	<u>8,396,872</u>
	Sub-total	<u>2,825,572</u>	<u>12,032,006</u>	<u>14,857,578</u>
Doubtful accounts		<u>(114,173)</u>	<u>(403,352)</u>	<u>(517,525)</u>
Total		<u><u>2,711,399</u></u>	<u><u>11,628,654</u></u>	<u><u>14,340,053</u></u>

(2) The asset quality classification for direct loans and allowance for direct loan losses as of December 31, 2015 and 2014 are as follows:

(In millions of won)

	<u>2015</u>		<u>2014</u>	
	<u>Loans</u>	<u>Allowance for doubtful accounts</u>	<u>Loans</u>	<u>Allowance for doubtful accounts</u>
Normal	₩6,489,150	55,644	5,659,072	48,695
Precautionary	289,797	20,286	219,992	15,399
Substandard	157,456	31,491	75,874	15,175
Doubtful	242,721	121,360	72,870	33,172
Estimated loss	418,369	418,369	432,898	405,085
	<u><u>₩7,597,493</u></u>	<u><u>647,150</u></u>	<u><u>6,460,706</u></u>	<u><u>517,526</u></u>

7. Related Party Transactions

(1) Details of subsidiaries as of December 31, 2015 are as follows:

<u>Controlled subsidiary</u>	<u>Ownership</u>
Small Business Distribution Center Co., Ltd.	100.00%
Small Business Corporation Registrar.	100.00%
Korea Venture Investment Corp.	100.00%
Korea Fund of Funds.	59.14%

(2) Significant transactions which occurred in the normal course of business with related companies for the years ended December 31, 2015 and 2014 are as follows:

(In millions of won)

<u>Relationship</u>	<u>Name</u>	<u>Transaction</u>	<u>2015</u>	<u>2014</u>
Subsidiary	Small Business Distribution			
	Center Co., Ltd.	Operation revenues	₩ 706	725
		Operating expenses	360	315
		Management expenses ...	131	104
	Small Business Corporation			
	Registrar.	Operating revenues	4	6
		Operating expenses	3,415	2,926
	Korea Venture Investment			
	Corp.	Operating revenues	6	—
		Management expenses ...	49	65
	Total	Operation revenues	716	731
		Operating expenses	3,775	3,241
		Management expenses ...	180	169

(3) Security deposit and deposit received balances with related companies are summarized as follows:

① Details of security deposit and deposit received for the year ended December 31, 2015

<u>Relationship</u>	<u>Company</u>	<u>Security Deposit</u>	<u>Deposit Received</u>
Subsidiary	Small Business Distribution		
	Center Co., Ltd.	₩—	495
	Korea Venture Investment Corp.	670	—

② Details of security deposit and deposit received for the year ended December 31, 2014

<u>Relationship</u>	<u>Company</u>	<u>Security Deposit</u>	<u>Deposit Received</u>
Subsidiary	Small Business Distribution		
	Center Co., Ltd.	₩—	495
	Korea Venture Investment Corp.	670	—

(4) Invested capital stocks with related companies as of December 31, 2015 are as follows:

(In millions of won, except percentage of ownership and number of shares)

<u>Relationship</u>	<u>Related Companies</u>	<u>Percentage of ownership</u>	<u>Number of shares</u>	<u>Net asset value</u>	<u>Book value</u>
Subsidiary	Small Business Distribution				
	Center Co., Ltd.	100.00%	21,728,644	₩91,663	₩91,663
	Small Business Corporation				
	Registrar.	100.00%	385,000	2,514	2,514
	Korea Venture Investment				
	Corp.	100.00%	10,000,000	76,833	76,833
	Korea Fund of Funds	59.14%	1,319,000	1,453,667	1,453,667

Invested capital stocks with related companies as of December 31, 2014 are as follows:

(In millions of won, except percentage of ownership and number of shares)

<u>Relationship</u>	<u>Related Companies</u>	<u>Percentage of ownership</u>	<u>Number of shares</u>	<u>Net asset value</u>	<u>Book value</u>
Subsidiary	Small Business Distribution Center Co., Ltd.	100%	21,728,644	₩102,627	₩102,627
	Small Business Corporation Registrar.	100%	385,000	2,355	2,355
	Korea Venture Investment Corp.	100%	10,000,000	75,678	75,678
	Korea Fund of Funds	60.90%	1,117,000	1,998,109	1,216,848

8. Property and Equipment

(1) Changes in property and equipment for the year ended December 31, 2015 are as follows:

(In millions of won)

	<u>Book value as of Jan. 1, 2015</u>	<u>Acquisitions</u>	<u>Disposals</u>	<u>Depreciation</u>	<u>Other Appreciation</u>	<u>Book value as of Dec. 31, 2015</u>
Land	₩ 32,783	—	(11,406)	—	—	21,377
Buildings	133,880	2,143	(6,291)	(4,208)	—	125,524
Structures	1,504	962	—	(52)	—	2,414
Vehicles	90	—	—	(41)	—	49
Furniture and equipment	2,937	1,711	(4)	(1,737)	—	2,907
Tools	41	9	—	(23)	—	27
Laboratory equipments	2,797	778	—	(1,680)	—	1,895
Other tangible assets	20,143	—	(2,023)	(716)	—	17,404
	<u>₩194,175</u>	<u>5,603</u>	<u>(19,724)</u>	<u>(8,457)</u>	<u>—</u>	<u>171,597</u>

(2) Changes in property and equipment for the year ended December 31, 2014 are as follows:

(In millions of won)

	<u>Book value as of Jan. 1, 2014</u>	<u>Acquisitions</u>	<u>Disposals</u>	<u>Depreciation</u>	<u>Other Appreciation</u>	<u>Book value as of Dec. 31, 2014</u>
Land	₩ 23,876	—	—	—	8,907	32,783
Buildings	68,350	23,832	(589)	(3,269)	45,556	133,880
Structures	1,551	4	—	(51)	—	1,504
Vehicles	56	66	—	(32)	—	90
Furniture and equipment	1,494	2,835	(1)	(1,391)	—	2,937
Tools	75	—	—	(34)	—	41
Laboratory equipments	4,277	583	—	(2,063)	—	2,797
Other tangible assets	22,099	—	(1,152)	(804)	—	20,143
Construction-in-progress	51,691	2,772	—	—	(54,463)	—
	<u>₩173,469</u>	<u>30,092</u>	<u>(1,742)</u>	<u>(7,644)</u>	<u>—</u>	<u>194,175</u>

(3) The officially declared values of land at December 31, 2015 and 2014 as announced by Ministry of Land, Infrastructure and Transport, are as follows:

(In millions of won)

	2015		2014	
	Book value	Declared value	Book value	Declared value
Inventories	₩ 2,824	3,551	2,824	3,519
Property and equipment, net	21,377	94,324	32,783	100,090
	<u>₩24,201</u>	<u>97,875</u>	<u>35,607</u>	<u>103,609</u>

(4) The SME Fund-owned real estate for purposes of selling in lots at December 31, 2015 and 2014 are summarized as follows:

(In millions of won)

	2015		2014	
	Acquisition	Book value	Acquisition	Book value
Land	₩ 8,083	2,824	8,083	2,824
Buildings	2,438	2,325	2,438	2,325
	<u>₩10,521</u>	<u>5,149</u>	<u>10,521</u>	<u>5,149</u>

9. Insurance

As of December 31, 2015, buildings, furniture and equipment are insured against fire damage as follows:

Types of Insurance	Asset	Book Value	Insured Value	Name of Insurance Company
Fire and Property Insurance	Buildings, Equipment etc.	114,881	181,399	Meritz Fire Insurance

10. Intangible Assets

Changes in other intangible assets for the years ended December 31, 2015 and 2014 are as follows:

(In millions of won)

	2015	2014
Net balance at beginning of year	₩ 7,484	7,219
Additions	2,166	2,579
Amortization	(2,484)	(2,314)
Net balance at end of year	<u>₩ 7,166</u>	<u>7,484</u>

11. Government Grants

The SME Fund received ₩2,400 million in 2001 from Pocheon City for the construction of the Pocheon-Yangmoon Industrial Complex. The subsidies received for these constructions were used for the acquisition of inventories and the balances are shown as a deduction from inventories at the end of the reporting period.

12. Financial Risk Management and Maturity Analysis for Financial Liabilities

(1) Liquidity risk management

Liquidity risk is the risk that the SME Fund will encounter difficulty in meeting the obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. The SME Fund's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the SME Fund's reputation.

The SME Fund ensures that it has sufficient cash on demand to meet expected operational expenses including the servicing of financial obligations; this excludes the potential impact of extreme circumstances that cannot reasonably be predicted, such as natural disasters. In addition, the SME Fund maintains the following lines of credit:

- A total credit limit of ₩2,500 billion with Woori Bank Co., LTD

(2) The following are the contractual maturities of financial liabilities as of December 31, 2015, including estimated interest payments and excluding the impact of netting agreements.

(In millions of won)

	Carrying amount	6 months or less	6-12 months	1-2 years	2-5 years	More than 5 years
Current portion of long-term debt	₩ 3,753,338	1,442,269	2,311,069	—	—	—
Long-term borrowing	3,869	—	—	2,679	1,190	—
Debentures	10,410,000	—	—	3,830,000	5,010,000	1,570,000
Total	₩14,167,207	1,442,269	2,311,069	3,832,679	5,011,190	1,570,000

It is not expected that the cash flows included in the maturity analysis could occur significantly earlier, or at significantly different amounts.

13. Debentures

(1) Debentures issued in local currency as of December 31, 2015 and, 2014 are summarized as follows:

(In millions of won)

	Annual interest rate	Repayment term	2015	2014
SME promotion bonds (private placement)	—	5 year installment repayment with 3 year grace period	₩ —	140,000
SME promotion bonds (public placed bonds) (*)	1.69~7.17	Full repayment on maturity	13,643,421	14,198,172
Sub-total			₩13,643,421	14,338,172
Less discount (long-term portion)			(1,746)	(1,931)
			₩ 3,280,000	14,336,241
Less: current portion of debentures (including current portion of discount of ₩117 million in 2015 and ₩153 million in 2014)			(3,279,883)	(3,246,511)
			₩10,361,792	11,089,730

(*) The valuation of interest rate swap contracts amounting to ₩(46,579) million in 2015 and ₩(1,828) million in 2014 are adjusted to the carrying amount of the debentures.

(2) Debentures issued in foreign currency as of December 31, 2015 and 2014 are summarized as follows:

(In millions of won)

	<u>Annual interest rate</u>	<u>Repayment term</u>	<u>2015</u>	<u>2014</u>
SME promotion bonds				
(private placement) (*)	5.75%	Full repayment on maturity	₩ 473,024	445,068
Less: discount (long-term portion) . .			(173)	(384)
			<u>₩ 472,851</u>	<u>444,684</u>
Less: current portion of debentures (including current portion of discount of ₩173 million in 2015 and ₩0 million in 2014)			(472,851)	(0)
			<u>₩ 0</u>	<u>444,684</u>

(*) The valuation of currency swap contracts amounting to ₩4,224 million in 2015 and ₩5,388 million in 2014 are adjusted to the carrying amount of the debentures.

(3) Aggregate maturities of the SME Fund's long-term bonds payable as of December 31, 2015 are summarized as follows:

(In millions of won)

<u>December 31</u>	<u>Bonds payable in won</u>	<u>Bonds payable in foreign currency</u>	<u>Total</u>
2016	₩ 3,280,000	468,800	3,748,800
2017	3,830,000	—	3,830,000
2018	2,810,000	—	2,810,000
2019	1,400,000	—	1,400,000
2020 and thereafter	2,370,000	—	2,370,000
	<u>₩13,690,000</u>	<u>468,800</u>	<u>14,158,800</u>

14. Long-term Borrowings

(1) Long-term borrowings as of December 31, 2015 and 2014 are summarized as follows:

(In millions of won)

<u>Lender</u>	<u>Annual interest rate</u>	<u>2015</u>	<u>2014</u>
Local currency borrowings			
Ministry of Finance and Economy	1.17~1.48%	₩ 8,408	16,492
		8,408	16,492
Less: current portion of long-term debt		(4,539)	(8,084)
		<u>₩ 3,869</u>	<u>8,408</u>

Repayment terms for the long term borrowing is 5 years following the 3 year grace period without any related guaranteed security

(2) Aggregate maturities of the SME Fund's long-term debt as of December 31, 2015 are summarized as follows:

<u>December 31,</u>	<u>Local currency borrowing</u>
2016	4,539
2017	2,679
2018	1,190
	<u>₩8,408</u>

15. Retirement and Severance Benefits

(1) Changes in retirement and severance benefits for the years ended December 31, 2015 and 2014 are as follows:

(In millions of won)

	<u>2015</u>	<u>2014</u>
Provision for retirement and severance benefits at beginning of year	₩36,627	31,945
Accrual for retirement and severance benefits	(1,265)	5,497
Payments	6,450	(815)
Provision for retirement and severance benefits at end of year	<u>₩41,812</u>	<u>36,627</u>

The SME Fund adopted a defined benefit pension plan and defined contribution plan on July 30, 2012. Under the New Retirement Benefits Regulation, the SME Fund applied the regulations for the service period after July 30, 2012, prospectively.

The SME Fund maintained an employees' retirement trust before July 30, 2012. Subsequent to that, the SME Fund entered into a retirement pension arrangement. The retirement trust paid and retirement pension paid are presented as a deduction of provision for severance benefits.

(2) The SME Fund does not have an obligation to pay the retirement benefits after an employee leaves the SME Fund. However, it requires employees to purchase a single premium annuity when employees receive lump-sum payment upon their retirement. Accordingly, the SME Fund does not recognize any obligation relating to the single premium annuity.

(3) Pension plan assets as of December 31, 2015 and 2014 are summarized as follows:

(In millions of won)

	<u>2015</u>	<u>2014</u>
Time deposits	₩ 7,477	6,045
Others	10,124	9,061
	<u>₩17,601</u>	<u>15,106</u>

(4) Changes in retirement pension payable for the years ended December 31, 2015 and 2014 are as follows:

(In millions of won)

	<u>2015</u>	<u>2014</u>
Beginning balance	₩15,106	12,716
Increase	3,731	3,208
Decrease	<u>(1,236)</u>	<u>(818)</u>
Ending balance	<u>₩17,601</u>	<u>15,106</u>

(5) Other assets related to provision for retirement and severance benefits as of December 31, 2015 and 2014 are summarized as follows:

(In millions of won)

	<u>2015</u>	<u>2014</u>
Deposits for Severance Benefits	₩75	74
Contribution to National Pension Plan	<u>22</u>	<u>25</u>
	<u>₩97</u>	<u>99</u>

(6) The expenses related to defined contribution plan are ₩1,027 million in 2015 and ₩458 million in 2014.

16. Assets and Liabilities Denominated in Foreign Currencies

(1) Assets and liabilities denominated in foreign currency as of December 31, 2015 are summarized as follows:

(In millions of won, in thousands of USD)

		<u>2015</u>		
		<u>Foreign currency</u>	<u>Exchange rate</u>	<u>Translation into won</u>
Debentures	USD	<u>399,852</u>	<u>1,172.00</u>	<u>₩468,627</u>
Total foreign currency denominated liabilities				<u>₩468,627</u>

(2) Assets and liabilities denominated in foreign currency as of December 31, 2014 are summarized as follows:

(In millions of won, in thousands of USD)

		<u>2014</u>		
		<u>Foreign currency</u>	<u>Exchange rate</u>	<u>Translation into won</u>
Debentures	USD	<u>399,650</u>	<u>1099.20</u>	<u>₩439,296</u>
Total foreign currency denominated liabilities				<u>₩439,296</u>

17. Commitments and Contingencies

The SME Fund's significant pending litigations as of December 31, 2015 are as follows:

(In millions of won)

<u>Court</u>	<u>Plaintiff</u>	<u>Defendant</u>	<u>Descriptions</u>	<u>Amount of damage claim</u>
Seoul Southern District Court	SBC	Miracle Co.	Unfair profit objection	749
Seoul High Court	SBC	Yu, Haekyung	Revoking of fraudulent act	307
Seoul Central District Court	SBC	Seo, HyunSook	Revoking of fraudulent act	12
Chuncheon District Court	SBC	Willtronics Co. LTD.	Revoking of fraudulent act	69
Seoul Southern District Court	SBC	Park, Junghoon	Revoking of fraudulent act	160
Gwangju District Court	SBC	Jin, Sucheol and others	Revoking of fraudulent act	424
Gwangju District Court	SBC	Republic of Korea	Dividend objection	190
Daejeon High Court	SBC	Korea Technology Finance Corp.	Surety Obligation	2,373
Seoul Central District Court	SBC	Shin, Kyungsook	Cancellation of registration of ownership	21
Daejeon District Court	SBC	Jejudol CEO Kim, Heesang and others	Loan	21
Mokpo Branch Court	SBC	Kang, Byungsup	Revoking of fraudulent act	2
Changwon District Court	SBC	Uhm, Sunhee	Revoking of fraudulent act	289
Suwon District Court	SBC	Bae, Youngju	Revoking of fraudulent act	41
Mokpo Branch Court	SBC	Maru industrial LLC and others	Revoking of fraudulent act	377
Hongseong Branch Courts	SBC	Koo, Jaryong and other	Revoking of fraudulent act	4
Gwangju District Court	SBC	Choi, Jinho	Revoking of fraudulent act	20
Jeju District Court	SBC	Lee, Jaeyoung and other	Revoking of fraudulent act	142

<u>Court</u>	<u>Plaintiff</u>	<u>Defendant</u>	<u>Descriptions</u>	<u>Amount of damage claim</u>
Changwon District Court . . .	SBC	Jeil Metal Co. LTD.	Revoking of fraudulent act	125
Daegu Western Branch Court (District)	SBC	Lee, Jungjae	Revoking of fraudulent act	125
Daegu District Court	SBC	Jang, Hoyoun	Revoking of fraudulent act	71
Jinju Branch Court	SBC	Choi, Byungwook and other	Revoking of fraudulent act	116
Daejeon District Court	SBC	Mun, Jumsun	Revoking of fraudulent act	7
Seoul Southern District Court	SBC	Kim, Kyungae	Revoking of fraudulent act	100
Daejeon District Court	SBC	Gwal.Hyungryul	Revoking of fraudulent act	24
Nonsan Branch Courts	SBC	Sul, Junsuk	Revoking of fraudulent act	47
Seoul Central District Court	SBC	National Agricultural Cooperative Federation.	Revoking of fraudulent act	82
Yeoju Branch Court	SBC	Federation.	Revoking of fraudulent act	240
Gwangju District Court	SBC	Bankruptcy trustee Kim, Sungchul of Bankrupt 'DaehanEdu Co. LTD.'	Dividend objection	241
Gwangju District Court	SBC	Kim, Jaeil	Revoking of fraudulent act	50
Andong Branch Courts	SBC	Sim, Wansik	Revoking of fraudulent act	16
Daegu District Court	SBC	Korearict CourtCourtn.	Loan	103
Seosan Branch Courts	SBC	Park, Yesul	Revoking of fraudulent act	10
Daegu Western Branch Court (District)	SBC	Daekwang Chemis	Revoking of fraudulent act	345
Daegu District Court	SBC	Stark Co. LTD.	Loan	234
Gunsan Branch Court	SBC	UKthehridot Courtnt acttrict)riectD.'rupt 'Dae	Dividend objection	49
Seoul Southern District Court	SBC	Monoray Co. LTD. And other	Loan	110
Daegu District Court	SBC	Ahn, Jihoo and other	Loan	192
Seoul Southern District Court	SBC	Wiltech Co. LTD.	Loan	370

<u>Court</u>	<u>Plaintiff</u>	<u>Defendant</u>	<u>Descriptions</u>	<u>Amount of damage claim</u>
Seoul Southern District Court	SBC	SJ Heat treatment Co. LTD.	Loan	174
Jeonju District Court	SBC	Kangdong Concrete Co. LTD	Revoking of fraudulent act	307
Seoul Southern District Court	SBC	Dongkwang IND Co. LTD.	Dividend objection	237
Daegu District Court	SBC	Park, Daehwa	Loan	82
Pohang Branch Courts	SBC	Jangsan Construction Co. LTD	Revoking of fraudulent act	495
Mokpo Branch Courts	SBC	Samin Industrial Co. LTD	Revoking of fraudulent act	350
Seoul Southern District Court	SBC	Geosung Construction Co. LTD	Loan	72
Seoul Southern District Court	SBC	Galaxy Co. LTD and other	Loan	86
Seoul Southern District Court	SBC	Kinetic Energy Co. LTD. And other	Loan	451
Gyeongju Branch Courts	SBC	KJS&P Co. LTD and other	Revoking of fraudulent act	46
Jinju Branch Court	SBC	Dodo Fisheries Co. LTD and others	Loan	407
Seoul Eastern District Court	SBC	Im, Younghwan and others	Revoking of fraudulent act	324
Haenam Branch Courts	SBC	Lee, Aekyung	Revoking of fraudulent act	140
Bucheon Branch Court	SBC	Jo, Taeje	Revoking of fraudulent act	36
Ulsan District Court	SBC	Park, Sunghye	Revoking of fraudulent act	45
Daegu District Court	SBC	Lee, Bongjung	Loan	1,009
Seoul Southern District Court	SBC	Xiworld Co. LTD	Loan	1,079
Wonju Branch Court	SBC	a corporation aggregate 'Hope worldwide Korea'	Revoking of fraudulent act	21
Seoul Southern District Court	SBC	Kim, Youngbin	Loan	1,079
Chungju Branch Court	SBC	Kim, Jungsoo	Revoking of fraudulent act	52
Daejeon District Court	SBC	Jeonbook-Jungeup Supermarket Co-Op and others	Loan	63

<u>Court</u>	<u>Plaintiff</u>	<u>Defendant</u>	<u>Descriptions</u>	<u>Amount of damage claim</u>
Jinju Branch Court	SBC	Cho Wonseok	Surety Obligation	44
Seoul Southern District Court	SBC	Kim Sung-joo	Surety Obligation	204
Seoul Southern District Court	SBC	Sekyu Choi Electronics Co. Ltd. and other	Loan	9
Incheon District Court	SBC	Yang Sungeum and others	Third party objection	44
Daegu District Court	SBC	Park Yeongju and other	Loan	100
Jinju Branch Court	SBC	Shin Dongrim	Surety Obligation	208
Daejeon District Court	SBC	Seol Junseok	Revoking of fraudulent act	47
Cheongju District Court	SBC	Youngjin drainboard Co. Ltd.	Revoking of fraudulent act	121
Masan Branch Court	SBC	Future Steel Co. Ltd.	Revoking of fraudulent act	125
Daegu District Court	SBC	Choi Geotae	Loan	150
Jinju Branch Court	SBC	Kim Youngsoon	Surety Obligation	81
Jeonju District Court	SBC	Choi Gwangseong	Revoking of fraudulent act	100
Seoul Southern District Court	SBC	Myoung Kwangsik	Loan	96
Seoul Southern District Court	SBC	Naru Technology Co. Ltd. and other	Loan	206
Jinju Branch Court	SBC	Nine Media Group Co. Ltd.	Loan	203
Jinju Branch Court	SBC	Keyitu Crane Co. Ltd.	Loan	334
Jeonju District Court	SBC	Threetree L.L.C.	corporeal property transfer	120
Jeonju District Court	SBC	Kwon Jeongtaek and other	Revoking of fraudulent act	109
Seoul Southern District Court	SBC	Seil Co. Ltd. and other	Loan	102
Seoul Southern District Court	SBC	Creative Imaging Technology Co. Ltd. and other	Loan	205
Jinju Branch Court	SBC	Lee Sunwoo	Surety Obligation	51
Jinju Branch Court	SBC	Green Zone Co. Ltd.	Loan	101
Jinju Branch Court	SBC	Choi Jintae	Surety Obligation	101
Jinju Branch Court	SBC	Kim Hwanchul	Surety Obligation	215
Jinju Branch Court	SBC	SOLAMAX Co. Ltd.	Loan	10

<u>Court</u>	<u>Plaintiff</u>	<u>Defendant</u>	<u>Descriptions</u>	<u>Amount of damage claim</u>
Seoul Southern District Court	SBC	Green Korea Co. Ltd. and other	Loan	134
Seoul Southern District Court	SBC	SD International Co. Ltd. and other	Loan	250
Seoul Southern District Court	SBC	J.Y.C. School Co. Ltd.	Loan	2,129
Jinju Branch Court	SBC	Sangjin Distribution Co. Ltd.	Loan	52
Jinju Branch Court	SBC	Oh Hankyun	Surety Obligation	52
Masan Branch Court	SBC	Best Metal Co. Ltd.	Dividend objection	99
Jeonju District Court	SBC	General Manager Yoo Donggi of ASA jeonju Co. Ltd.	Dividend objection	177
Gunsan Branch Court	SBC	Kim Yeonhee and other	Revoking of fraudulent act	53
Daejeon District Court	SBC	S.M. Air Technology Co. Ltd and othrts	Loan	206
Daegu District Court	SBC	Kim Jinkyu	Loan	59
Ulsan District Court	SBC	Ryu Nakhyun	Third party objection	70
Daejeon District Court	SBC	Green Food Co. Ltd.	Dividend objection	9
Busan Eastern Branch Court	SBC	Kang Doochul	Revoking of fraudulent act	547
Busan District Court	SBC	Kim Seohyun	Revoking of fraudulent act	125
Miryang Branch Court	SBC	Han Changsoo	Revoking of fraudulent act	6
Jinju Branch Court	SBC	Bang Changnam and other	Loan	23
Daejeon District Court	SBC	Lee Taekyu	Loan	509
Daejeon District Court	SBC	Kim Donghwa	Surety Obligation	116
Daejeon District Court	SBC	Haewon Food Co. Ltd. and other	Loan	204
Jinju Branch Court	SBC	Namkyoung Fisheries Co. Ltd. and otrers	Loan	60
Jinju Branch Court	SBC	Starttwenty-one Co. Ltd.	Loan	246
Jinju Branch Court	SBC	Bang Jinchul	Surety Obligation	246
Seoul Southern District Court	SBC	Daewoong Metal Co. Ltd. and other	Loan	34

<u>Court</u>	<u>Plaintiff</u>	<u>Defendant</u>	<u>Descriptions</u>	<u>Amount of damage claim</u>
Daejeon District Court	SBC	J.E E&T Co. Ltd and others	Loan	114
Daejeon District Court	SBC	Bak, JongJu	Loan	278
Jinju Branch Court	SBC	Park, InCheol who Bankruptcy trustee of Bankrupt Company Dongwoo hightec Co. Ltd	Loan	14
Seongnam Branch Court . . .	SBC	Go GiYoung and others	Third party objection	66
Jinju Branch Court	SBC	Lee MunJu	Loan	91
Jinju Branch Court	SBC	Hwang GwangSu	Surety Obligation	91
Jinju Branch Court	SBC	Maxqueen tronic Co. Ltd and others	Loan	65
Jinju Branch Court	SBC	Heo SunJa	Surety Obligation	129
Jinju Branch Court	SBC	Go RakJong	Loan	129
Jinju Branch Court	SBC	Narae Distribution Co. Ltd	Surety Obligation	129
Jinju Branch Court	SBC	Lee SeoYeon and others	Revoking of fraudulent act	121
Changwon District Court . . .	SBC	Leem SeongIl	Revoking of fraudulent act	31
Bucheon Branch Court	SBC	YoungJin International Co. Ltd and others	corporeal property transfer	85
Daejeon District Court	SBC	Paju Agricultural Co. Ltd and others	Loan	52
Daejeon District Court	SBC	G-12 Co. Ltd and others	Loan	103
Seoul Southern District Court	SBC	Kim MunSeop	Loan	52
Seoul Southern District Court	SBC	Encore Development Co. Ltd and others	Loan	25
Seoul Southern District Court	SBC	Min ByeongGwan	Loan	200
Seoul Southern District Court	SBC	Dongwon Electric Machinery Co. Ltd and others	Loan	305
Jinju Branch Court	SBC	The one Distribution Co. Ltd and others	Loan	83
Seoul Southern District Court	SBC	C&B Co. Ltd	Revoking of fraudulent act	50
Daejeon District Court	SBC	Myungseong Engineering Co. Ltd	Loan	94
Gimcheon Branch Courts . . .	SBC	Shinhwa Steel Co. Ltd	Dividend objection	143

<u>Court</u>	<u>Plaintiff</u>	<u>Defendant</u>	<u>Descriptions</u>	<u>Amount of damage claim</u>
Cheongju District Court	SBC	Song ChanHo and others	Revoking of fraudulent act	91
Jeonju District Court	SBC	Kim BumSoo	Revoking of fraudulent act	50
Pyeongtaek Branch Court . . .	SBC	Korea Technology Finance Corp. and others	Revoking of fraudulent act	84
Seoul Southern District Court	SBC	Dongsan Fine Chemicals Co. Ltd	Loan	55
Seoul Southern District Court	SBC	Go UiDeuk	Surety Obligation	194
Seoul Southern District Court	SBC	Brown Innovation Co. Ltd and others	Loan	188
Jinju Branch Court	SBC	Gahyo F&B Co. Ltd and others	Loan	30
Jinju Branch Court	SBC	Ravielle Co. Ltd	Loan	104
Jinju Branch Court	SBC	Kim HongRae	Surety Obligation	104
Jinju Branch Court	SBC	G.L Co. Ltd	Loan	58
Jinju Branch Court	SBC	Kim SangJun	Surety Obligation	160
Jinju Branch Court	SBC	WonIl. Co. Ltd	Loan	38
Jinju Branch Court	SBC	Lee KangHo	Loan	200
Jinju Branch Court	SBC	Lee GapSu	Surety Obligation	222
Jinju Branch Court	SBC	J-nongminsarang Co. Ltd	Loan	14
Seoul Southern District Court	SBC	D-Tech E&G Co. Ltd and other	Loan	73
Seoul Southern District Court	SBC	Hwang YoungOk	Loan	79
Seoul Southern District Court	SBC	Huneco Co. Ltd	Loan	207
Seoul Southern District Court	SBC	Choi SeongEun	Loan	1
Bucheon Branch Court	SBC	Ji YoungSeon	Revoking of fraudulent act	44
Seoul High Court	SBC	Sawnics Co. Ltd	Corporate rehabilitation	—
SUPREME COURT	SBC	Sawnics Co. Ltd	Corporate rehabilitation	—
Sub Total				<u>27,351</u>

<u>Court</u>	<u>Plaintiff</u>	<u>Defendant</u>	<u>Descriptions</u>	<u>Amount of damage claim</u>
Seoul High Court	KEB Hana Bank Co.	SBC	Collection of original receivable balance	454
Suwon District Court	Yun Byeongheun	SBC	Dividend objection	145
Ulsan District Court	Within Co.	SBC	Confirmation of right of claim for payment	349
Busan High Court	Strategy Human Resource Development	SBC	Revocation of Disposition of Restriction on Participation	50
Sub Total				<u>948</u>

18. Derivative Instruments and Hedge Accounting

(1) Derivatives for fair value hedge accounting

① Interest swap

The SME Fund entered into interest swap contracts to hedge the interest fluctuation risk or variability of fair value from the local bonds. Details of derivative instruments as of December 31, 2015 are as follows:

(In millions of won)

<u>Counterparty</u>	<u>Related liabilities</u>	<u>Unsettled amount</u>	<u>Settlement date</u>
UBS	290th Public placed bonds	₩140,000	2008.11.14~2018.10.15
Credit Suisse	354th Public placed bonds	150,000	2010.10.15~2018.10.15
Credit Suisse	352th Public placed bonds	120,000	2010.09.30~2018.10.15
Credit Suisse	290th Public placed bonds	140,000	2010.10.15~2018.10.15
Credit Suisse	374th Public placed bonds	130,000	2011.09.02~2021.06.02
Credit Suisse	375th Public placed bonds	70,000	2011.09.17~2021.06.17
Credit Suisse	511th Public placed bonds	140,000	2015.06.16~2030.06.16
Credit Suisse	514th Public placed bonds	150,000	2015.08.07~2030.08.07

The SME Fund entered into interest swap contracts to hedge the interest fluctuation risk or variability of fair value from the local bonds. Details of derivative instruments as of December 31, 2014 are as follows:

(In millions of won)

<u>Counterparty</u>	<u>Related liabilities</u>	<u>Unsettled amount</u>	<u>Settlement date</u>
Merrill Lynch	281th Public placed bonds	₩ 70,000	2008.08.27~2015.08.08
UBS	290th Public placed bonds	140,000	2008.11.14~2018.10.15
Credit Suisse	354th Public placed bonds	150,000	2010.09.17~2018.10.15
Credit Suisse	352th Public placed bonds	120,000	2010.09.17~2018.10.15
Credit Suisse	290th Public placed bonds	140,000	2010.09.17~2018.10.15
Credit Suisse	374th Public placed bonds	130,000	2011.09.02~2021.06.02
Credit Suisse	375th Public placed bonds	70,000	2011.06.17~2021.06.17
Credit Suisse	469th Public placed bonds	70,000	2014.02.06~2024.02.08
Credit Suisse	470th Public placed bonds	100,000	2014.02.21~2024.02.21
Credit Suisse	474th Public placed bonds	100,000	2014.03.07~2024.03.07

② Currency swap

The SME Fund entered into a currency swap contract to hedge the foreign currency exchange rate fluctuation risk or variability of fair value from bonds in foreign currency. Details of derivative instruments as of December 31, 2015 are as follows:

(In thousands of USD)

<u>Counterparty</u>	<u>Related liabilities</u>	<u>Unsettled amount</u>	<u>Settlement date</u>
UBS	1st Overseas bonds	\$ 80,000	2006.09.14
Credit Suisse		60,000	~2016.09.14
Merrill Lynch		40,000	

The SME Fund entered into a currency swap contract to hedge the foreign currency exchange rate fluctuation risk or variability of fair value from bonds in foreign currency. Details of derivative instruments as of December 31, 2014 are as follows:

(In thousands of USD)

<u>Counterparty</u>	<u>Related liabilities</u>	<u>Unsettled amount</u>	<u>Settlement date</u>
UBS	1st Overseas bonds	\$ 80,000	2006.09.14
Credit Suisse		60,000	~2016.09.14
Merrill Lynch		40,000	

(2) Derivatives for cash flow hedge accounting

① Interest swap

The SME Fund entered into interest swap contracts to hedge the interest fluctuation risk or variability of fair value from the local bonds. Details of derivative instruments as of December 31, 2015 are as follows:

(In millions of won)

<u>Counterparty</u>	<u>Related liabilities</u>	<u>Unsettled amount</u>	<u>Settlement date</u>
JP morgan	462th Public placed bonds	70,000	2013.11.11~2024.02.12
Nomura	382th Public placed bonds	30,000	2011.09.06~2021.09.06
JP morgan	487th Public placed bonds	50,000	2014.06.20~2024.09.20

The SME Fund entered into interest swap contracts to hedge the interest fluctuation risk or variability of fair value from the local bonds. Details of derivative instruments as of December 31, 2014 are as follows:

(In millions of won)

<u>Counterparty</u>	<u>Related liabilities</u>	<u>Unsettled amount</u>	<u>Settlement date</u>
JP morgan	462th Public placed bonds	70,000	2013.11.11~2024.02.12
Nomura	382th Public placed bonds	30,000	2011.09.06~2021.09.06
JP morgan	487th Public placed bonds	50,000	2014.06.20~2024.09.20

② Currency swap

The SME Fund entered into a currency swap contract to hedge the foreign currency exchange rate fluctuation risk of variability of future cash flows from bonds in foreign currency. Details of derivative instruments as of December 31, 2015 are as follows:

(In thousands of USD)

<u>Counterparty</u>	<u>Related liabilities</u>	<u>Unsettled amount</u>	<u>Settlement date</u>
UBS	1st Overseas bonds	\$85,000	2006.09.14
Credit Suisse		50,000	~2016.09.14
Merrill Lynch		85,000	

The SME Fund entered into a currency swap contract to hedge the foreign currency exchange rate fluctuation risk of variability of future cash flows from bonds in foreign currency. Details of derivative instruments as of December 31, 2014 are as follows:

(In thousands of USD)

<u>Counterparty</u>	<u>Related liabilities</u>	<u>Unsettled amount</u>	<u>Settlement date</u>
UBS	1st Overseas bonds	\$85,000	2006.09.14
Credit Suisse		50,000	~2016.09.14
Merrill Lynch		85,000	

(3) Valuation of derivatives as of December 31, 2015 is as follows:

(In millions of won)

	<u>Fair Value</u>	<u>Gain (loss) on valuation</u>	<u>Accumulated other comprehensive income</u>
Interest swap	₩(57,173)	(51,885)	(9,149)
Currency swap	94,943	27,946	(1,983)
	<u>₩ 37,770</u>	<u>(23,939)</u>	<u>(11,132)</u>

Valuation of derivatives as of December 31, 2014 is as follows:

(In millions of won)

	<u>Fair Value</u>	<u>Gain (loss) on valuation</u>	<u>Accumulated other comprehensive income</u>
Interest swap	₩(5,635)	16,456	(1,444)
Currency swap	68,981	12,487	(6,063)
	<u>₩63,346</u>	<u>28,943</u>	<u>(7,508)</u>

19. Funds' Equity

Transactions in funds' equity for the year ended December 31, 2015 are as follows:

(In millions of won)

	<u>Government subsidiaries</u>	<u>Private subsidiaries</u>	<u>Public institution subsidiaries</u>	<u>Total</u>
Balance at January 1, 2015	₩2,326,666	34,054	177,107	2,537,827
Increase	188,507	—	—	188,507
Balance at December 31, 2015	<u>₩2,515,173</u>	<u>34,054</u>	<u>177,107</u>	<u>2,726,334</u>

Transactions in funds' equity for the year ended December 31, 2014 are as follows:

(In millions of won)

	<u>Government subsidiaries</u>	<u>Private subsidiaries</u>	<u>Public institution subsidiaries</u>	<u>Total</u>
Balance at January 1, 2014	₩2,219,803	34,054	177,107	2,430,964
Increase	106,863	—	—	106,863
Balance at December 31, 2014	<u>₩2,326,666</u>	<u>34,054</u>	<u>177,107</u>	<u>2,537,827</u>

20. Accumulated Deficit

Statements of disposition of accumulated deficit for the years ended December 31, 2015 and 2014 were as follow:

Date of appropriation for 2015: February 19, 2016

Date of appropriation for 2014: February 13, 2015

(In millions of won)

	<u>2015</u>	<u>2014</u>
Undisposed accumulated deficit		
Balance at beginning of year	₩(1,160,893)	(1,183,964)
Net loss	12,823	23,071
Balance at end of year before appropriation	(1,148,070)	(1,160,893)
Disposition of accumulated deficit		—
Undisposed accumulated deficit to be carried over to subsequent year	<u>₩(1,148,070)</u>	<u>(1,160,893)</u>

21. Income Taxes

The components of income tax expense for the years ended December 31, 2015 and 2014 are summarized as follows:

(In millions won)

	<u>2015</u>	<u>2014</u>
Charged directly to capital adjustments	₩(6,424)	(10,660)

The SME Fund did not recognize deferred income tax assets for the year ended December 31, 2015, as it is not probable that the SME Fund will be able to realize some or all of the net deferred income tax assets in future periods.

As of December 31, 2015, details of gross deferred assets and liabilities, current income tax payable, and current income tax receivable are as follows:

(In millions won)

	<u>2015</u>	<u>2014</u>
Prepaid income taxes	₩413	444

22. Comprehensive Loss

Comprehensive loss for the years ended December 31, 2015 and 2014 is as follows:

(In millions of won)

	<u>2015</u>	<u>2014</u>
Net income	₩12,823	23,071
Gain on valuation of available-for-sale securities, net	16,980	40,045
Change in equity of equity method investee	14,479	(3,606)
Gain (loss) on valuation of currency swap contracts	(8,683)	(5,856)
Comprehensive income	<u>₩35,599</u>	<u>60,866</u>

23. Non-cash Investing and Financing Activities

Significant non-cash investing and financing activities for the years ended December 31, 2015 and 2014 were summarized as follows:

(In millions of won)

	<u>2015</u>	<u>2014</u>
Write off loan	₩120,816	100,738
Loan transferred to available-for-sale securities	8,396	10,922
Gain on valuation of available-for-sale securities	22,210	51,171
Loss on valuation of available-for-sale securities	441	168
Capital adjustment debit arising from equity method investments	18,563	4,623
Capital adjustment credit arising from equity method investments	—	—
Gain on valuation of currency swap contracts	1,983	6,063
Gain on valuation of interest swap contracts	—	1,818
Loss on valuation of interest swap contracts	9,150	3,263
Borrowings increased due to the cancellation of interest rate swaps	7,134	1,722
Income tax expense credited directly to equity	6,424	10,660

24. Date of Authorization for Issue

The 2015 financial statements were authorized for issue on February 15, 2016, at the Board of Directors meeting, which will be submitted for approval to the Management committee to be held on February 19, 2016.

25. Value Added Information

Details of accounts included in the computation of value added for the years ended December 31, 2015 and 2014 are as follows:

(In millions of won)

	<u>2015</u>	<u>2014</u>
Salaries and wages	₩64,807	60,076
Accrual for retirement and severance benefits	7,400	5,955
Other employee benefits	5,461	5,258
Rent	5,314	2,675
Depreciation	8,458	7,644
Taxes and dues	1,565	1,544

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