

Construction Market

1. Domestic

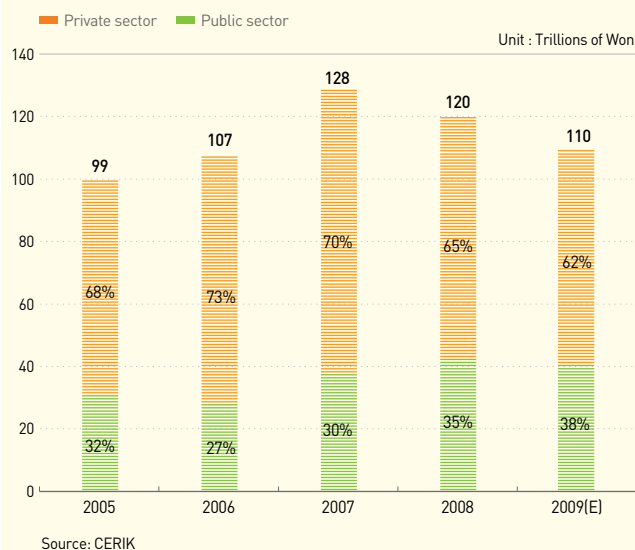
The Construction & Economy Research Institute of Korea (CERIK) reported that the value of new contracts in Korea totaled ₩120 trillion in 2008, which was 6 percent lower than the figure for the year before. This decline was fueled by the slumping the private sector housing market. The general downturn in the construction market persisted throughout the second half due to the drop in new orders and the mounting number of unsold apartments, rising costs for construction materials and lower profitability for privately-funded infrastructure projects. The value of new contacts in the public sector actually rose 18.1 percent in 2008 with the second round of "new city" and "new town" projects being supported by the Korean government. On the other hand, new orders in the private sector fell 10.7 percent with the decline in residential construction.

The slowdown came towards the end of the year; therefore, industry watchers do not expect an upsurge in domestic construction orders in 2009. The contraction in housing supply is likely to continue, and the lackluster domestic economy will dampen demand for nonresidential construction and public private partnership projects. As a result, new construction orders as a whole are forecasted to fall 8.3 percent year on year to ₩110 trillion.

By sector, CERIK predicts the growth in government contracts, which were up 8.2 percent year on year in 2008, to rise another 4.1 percent in 2009. This projection is based on the government's increased budget for infrastructure investment, ongoing work at the government's Multipurpose Administrative City in the Chungcheong area, and higher supply volumes for the second-phase "new city" projects. By contrast, new orders are forecasted to drop in the private sector. Demand for new housing will most likely continue to fall through the first half at least. For the time being, construction companies will have trouble in moving more than 140,000 unsold apartments outside the Greater Seoul Area. Thus, the slowdown in new housing construction that began in the private sector in 2008 is expected to continue in 2009.

Considering all these factors together, the volume of new construction orders in Korea will undoubtedly be lower in 2009 than it was during the year before.

New Construction Orders



2. Housing Market

Global economic activity has been in a free fall since September 2008, and the Korean real estate market has also changed quickly. The plummeting stock market has led to a sharp decline in real estate transactions and the number of unsold apartments has surged. Construction companies have been hit by a severe liquidity shortage as a result. Concern has mounted over the possibility that the real estate market slowdown will spread to the real economy, and the sale of distressed properties has begun to occur. The initial construction of large apartment complexes and reconstruction of old apartment complexes have fallen sharply in southern Seoul.

Recognizing the urgency of the situation, the Korean government implemented policies to stabilize the real estate market seven times during the second half of 2008 alone. On November 3, the government announced a broad set of market stimulation measures, including the relaxation of anti-speculation regulations. The move appeared to safeguard the market from the worst case scenario, but attention has

remained riveted on when a full-scale recovery can begin. In 2008, the government approved the construction of some 370,000 new apartment units, and an additional 300,000 units are expected to be granted the go-ahead in 2009. This means the construction companies that are heavily dependent on residential projects will experience difficulty in securing the cash flow they need through regular marketing activities for the short term. On the other hand, the government will provide tax benefits for buyers of unsold apartments outside the Greater Seoul Area and will relax stringent requirements imposed upon the reconstruction of apartment buildings. These moves should boost apartment prices and stimulate purchase transactions, leading to a gradual recovery in the second half.

3. Overseas Construction Orders

The first overseas project for a Korean builder was in 1965, and it was not until February 2006 that the aggregate total reached the US\$200 billion mark. However, that figure had topped US\$300 billion within just the next three years. Overseas construction activities slowed after the onset of the foreign exchange crisis at the end of 1997, but a full recovery began from 2004. The Ministry of Land, Transport and Maritime Affairs announced that Korean construction companies won a record US\$47.6 billion in overseas projects during 2008.

The overseas project portfolio for the Korean construction industry is most heavily weighted in the Middle East, where projects amounted to US\$27.2 billion (57 percent of the total). Asia, led by Singapore and China, represents the second largest portion (31 percent), with US\$14.7 billion worth of orders received from all the other regions, Latin America and Africa in particular, came to US\$5.7 billion, a relatively small part of the total. However, the total value of new orders from these regions keeps growing every year. Many Korean construction companies won most of their new orders in Saudi Arabia, Libya, Kuwait and Singapore over the years.

Many Korean contractors have begun to provide engineering services overseas starting in 2003, and in 2008 they won 240 engineering-related contracts, worth US\$900 million. That

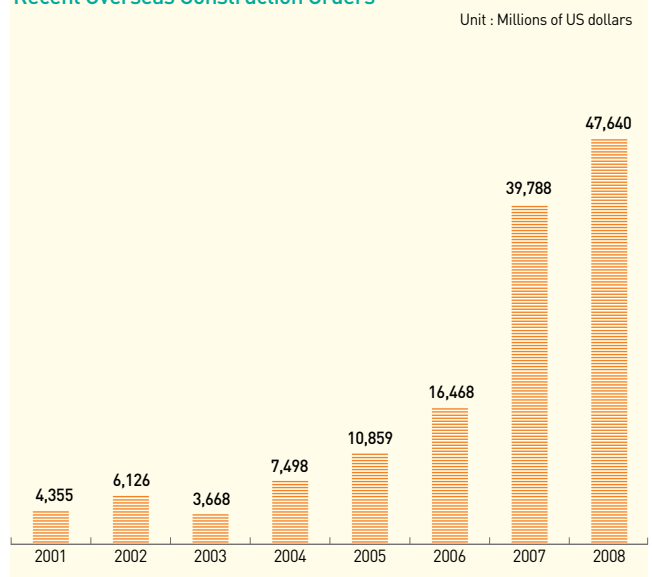
figure is more than twice the US\$380 million in engineering awards received in 2007.

Overseas project particulars have changed greatly over time in other ways as well. Korean construction companies are no longer confined to simple subcontracting roles but have become involved in the investment development business, which entails a complete range of capabilities, from project planning and project discovery, feasibility analysis, and project financing to the operation of completed facilities.

The so-called "ubiquitous city" (U-City) projects in Korea have incorporated advanced information technologies into the urban development projects known as "new towns." Korean contractors are now starting to export these "U-City" concepts and to offer package deals overseas that link natural resource development with infrastructure construction.

The overseas construction market will be influenced by conflicting factors in 2009: the risk from the ongoing global economic downturn and the opportunities represented by government stimulus packages. The Korean construction industry expects to win US\$40 billion in new orders outside the country during 2009. To this end, private sector companies will also advance into new markets and establish overseas construction funds in cooperation with government-run entities.

Recent Overseas Construction Orders



Management's Discussion and Analysis

Recent Overseas Construction Orders

	2006	2007	2008
Total	16,468	39,788	47,640
Middle East	9,530 (57.9%)	22,801(57.3%)	27,204(57.0%)
Asia	4,046 (24.5%)	12,849(32.3%)	14,689(31.0%)
Other	2,892 (17.6%)	4,138(10.4%)	5,747(12.0%)

Unit : Millions of US dollars

Summary of Operations

New Orders

The Korean government began imposing anti-speculation restrictions on real estate in 2007, causing domestic construction activities to slow. This was followed by the global financial crisis of 2008, which adversely affected construction activity worldwide. Despite these circumstances, GS E&C saw new orders rise 15 percent year on year in 2008 to surpass ₩12.23 trillion. Robust order taking in both the overseas project and domestic housing sectors enabled the company to continue posting the highest growth in new business among all Korean builders.

The order backlog at year's end, to include ₩15.7 trillion in provisional new orders, totaled an estimated ₩42.3 trillion, enough work to keep the company working at full capacity for the next six years. The value of new overseas civil engineering projects was 33 percent higher than the figure for 2007. New overseas projects won in 2008 exceeded ₩4.96 trillion, which was far better than the figures for 2006 (just under ₩1.79 trillion) and 2007 (over ₩3.08 trillion). Such growth is mainly due to the excellent track record that GS E&C has amassed in the construction of oil refineries, gas processing plants and petrochemical plants outside Korea. At the same time, the company has managed to make significant inroads into new national markets such as the UAE and Saudi Arabia. The global downturn will mean a reduction in new overseas orders will be forthcoming in 2009. Therefore, the company's expected target for the year has been set conservatively at ₩10.2 trillion.

Sales Revenue

Sales rose 14.2 percent from the ₩6.01 trillion posted in 2007 to more than ₩6.87 trillion in 2008, exceeding the original goal of ₩6.65 trillion. This strong showing amid an overall slump in construction activity is attributable to a balanced portfolio that spans six sectors-civil engineering, plants, environmental facilities, office buildings, housing and power plants.

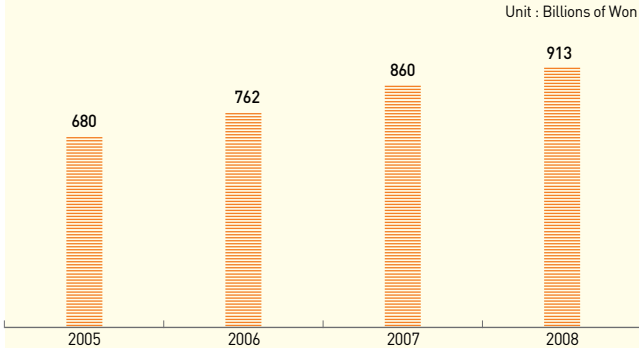
Breaking down the sales total by business division, the Civil Engineering Business Division recorded ₩657 billion, down 16 percent from the previous year as the Seoul Beltway Project was completed in 2007 and infrastructure project sales were generally slower in 2008. The Plant Business Division saw sales rise 6 percent year on year to ₩2.1 trillion, as the domestic HOU project and overseas plant projects proceeded on schedule. The Housing Business Division performed exceptionally well considering the instability in the housing market as a whole. Sales rose 25 percent, from more than ₩1.95 trillion in 2007 to over ₩2.44 trillion in 2008, thanks to large-scale apartment redevelopment projects as well as housing projects on company-owned land. The company has set its 2009 sales target at ₩6.94 trillion, about the same as the total achieved in the previous year.

Profits

Gross Profit

Gross profit rose 6 percent, from ₩860 billion in 2007 to ₩913 billion in 2008, but the gross margin fell one percentage point, from 14.3 percent to 13.3 percent, over the same period. The decline in profitability was due to higher prices for raw materials, and a fall in the gross margin for the Civil Engineering Business Division after the completion of the Seoul Outer Beltway Project. On the other hand, the Plant Business Division enjoyed a gross margin was a 3.8%p improvement over 2007 and 6.7%p better than in 2006. Higher profitability will be difficult to achieve in 2009 because of higher raw material price, increased marketing costs and more low-margin projects in the sales mix. Therefore, the gross margin for the year is expected to be 12.7 percent, down 0.6%p from 2008.

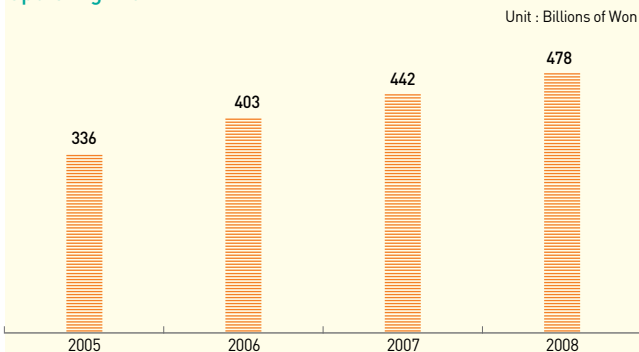
Gross Profit



Operating Profit

Operating profit reached ₩478 billion in 2008, a solid 8.1 percent gain from 2007 despite the overall difficulties in the construction industry. However, the company was unable to achieve its ₩500 billion target because ₩48 billion in bad debt expense was included in sales & administrative expenses to reflect the increased risk from unsold apartments. In spite of this, the selling & administrative expenses fell due to decreased salary expenses and advertising cost. Operating profit for 2009 has been conservatively set at ₩506 billion to reflect the increased risk from some unsold apartments, while operating costs and other expenses are projected to be lower than in 2008 and the company's overall financial status is expected to be sound.

Operating Profit



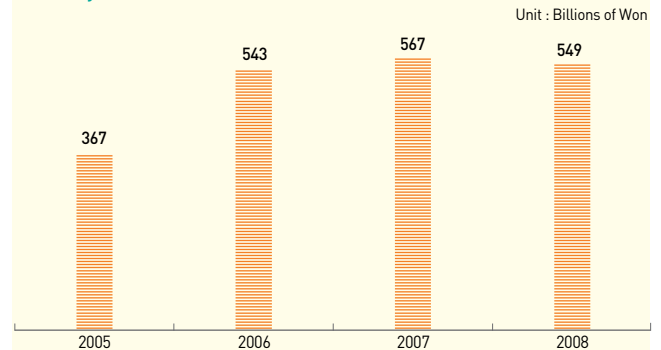
Ordinary Profit

The company already maintains a ₩70 billion allowance for bad debt to cover project financing loan guarantee of non-profitable housing project. An additional ₩70 billion reserve was established to cover the risk of loans defaults by some

cooperative members of apartment reconstruction projects. After those funds were set aside, pre-tax net income totaled ₩549 billion, which was 3 percent lower than the ₩567 billion figure posted in 2007.

As for non-operating income, ₩31 billion was earned in interest revenue. The company also maintains a hedge against foreign exchange risk through exchange rate fluctuation insurance and forward exchanges, and these activities generated ₩165 billion in non-operating income during 2008. With a conservative target for non-operating income in 2009, pre-tax net income is expected to reach ₩526 billion.

Ordinary Profit



Financial Position

Cash Flow

Cash & cash equivalents rose from ₩371 billion in 2007 to ₩809 billion in 2008. The changes in cash flow are detailed by activity type as follows:

First, operating cash flow totaled ₩619 billion. Contributing factors included ₩382 billion in net profit, ₩250 billion in non-cash income and expenses, and ₩11.8 billion in cash inflow resulting from changes in operating assets and liabilities.

Second, cash flow from investment activities generated a cash outflow of ₩301 billion. These activities included investments for future development projects and land purchases for in-house projects.

Management's Discussion and Analysis

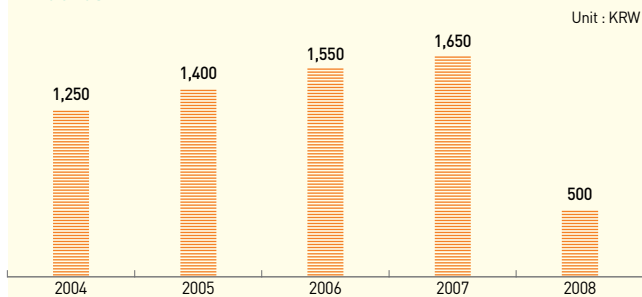
Third, cash flow from financing activities increased by ₩62 billion during the year, and ₩82 billion was paid out in dividends.

Dividends & Investments

The dividend per share, which was ₩1,650 for 2007, was set at ₩500 for 2008, decreasing the total dividend payout from ₩82 billion to ₩25 billion.

After distributing some profits in the form of dividends, the company invests most of the retained earnings to elevate shareholders' future value.

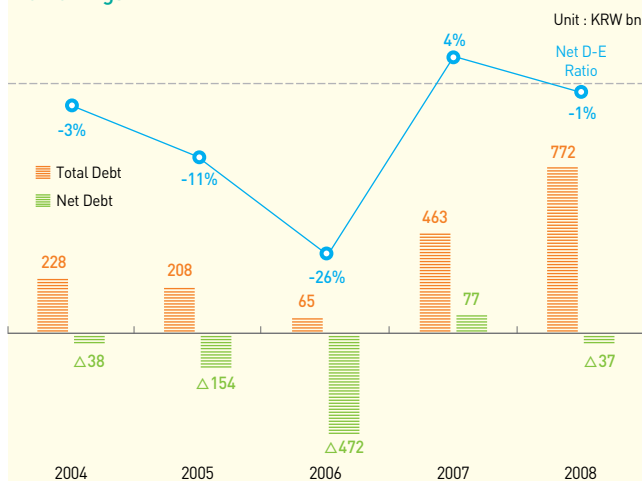
Dividends



Borrowings

Borrowings at the end of 2008 totaled ₩772 billion, up sharply from the ₩463 billion figure posted a year earlier. The funds were raised in a US\$310 million issuance of foreign currency denominated corporate bonds in early 2008.

Borrowings



Equity

As of December 31, 2008, the company had 51 million outstanding shares of common stock; no preferred stocks, convertible bonds or bonds with warrant have been issued. Chairman Chang-Soo Huh and other members of the Huh family are the major shareholders, with 30.48% of the total shares issued. An additional 2.98% are in the form of treasury stock or part of the employee stock sharing program. At year's end, foreign investors owned 33.10% of the total shares issued.