Management's Discussion and Analysis

Construction Market

1. Domestic Construction Market

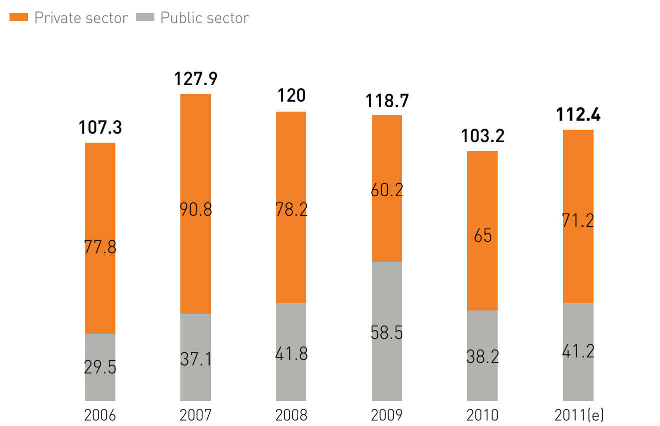
The Construction and Economy Research Institute of Korea (CERIK) reported that the volume of new orders dropped 13 percent year on year to ₩103.2 trillion in 2010. Orders in the private sector rose 7.9 percent to reach ₩65 trillion, while new government contracts fell 34.7 percent from the previous year to ₩38.2 trillion.

In 2009, the Korean government increased its budget for infrastructure investment to stimulate economic activity and front-loaded implementation, causing the financial effect to dry up in 2010. For this reason, along with the corresponding base effect, the order volume in the government sector decreased from a year earlier.

Here is a breakdown of the figures:
New government orders for civil engineering projects in 2010 were 39.8 percent lower than in 2009 because the contracts for major projects championed by the administration, notably the Four Major Rivers Restoration Plan, had already been issued. The order volume for building construction was also down 20.5 percent on the declining fiscal health of government-run corporations and local government bodies.

By contrast, the private sector was buoyed by redevelopment and reconstruction projects, enabling new orders for construction to rise 1 percent. New contracts in the civil engineering segment also surged 37.5 percent year on year with strong demand for power plants, power transmission lines and machinery installation. However, the monetary value of the new private sector projects did not reach pre-2009 levels, and the complete recovery of the new order volume in Korea's private sector is unlikely in 2011.

New Construction Orders | Unit : Trillions of Won |



*source: CERIK

New domestic orders for construction projects are forecasted to total ₩112.4 trillion in 2011, up 8.9 percent from the previous year.

The public sector will have less leeway for investing in new civil engineering projects, given the reduction in infrastructure budgets (down 3.2% YoY) as well a financial position weakened by the burdens and liabilities accompanying the spate of new orders by local governments and state-run enterprises. On the other hand, construction contracts should rise with greater demand for offices to accommodate government ministries and agencies relocating to the so-called "ubiquitous cities" and multi-functional administrative city (Sejoing City) outside the capital region. On balance, the volume of orders from the Korean government is projected to be 7.8 percent higher in 2011 than it was in 2010.

Moreover, new private sector contracts are expected to increase 9.5 percent year on year. This growth is attributed to a rising volume of new home presales, spurred by improved economic conditions, and large-scale corporate investments in new facilities.
Importantly, the actual volume of new construction orders in Korea in 2011 could differ significantly from the forecasted figures. Many of the large development projects currently under consideration are being reviewed and delayed because local governments and state-run enterprises have weakened financially. Some of these projects are likely to be downsized or cancelled altogether.

2. Housing Market

The rise in domestic housing prices began to slow in the second half of 2009, and in 2010 they actually fell in most areas of the country, except for in Busan and some other major cities. However, the rate of housing price drop showed signs of decline in the second half of 2010, and the movement in prices neared a standstill, indicating that the market had bottomed out. At the same time, the chonsei (lump sum deposit) requirements when renting a home have begun to rise in Korea, which means the potential for volatility in housing prices is unavoidable.

Housing prices in 2010 showed an overall pattern of fluctuation regardless of home type, but differences in this pattern were seen depending on home size. Prices for small and medium-sized units varied widely, while changes in home purchase or rental demand could be felt. The average purchase price index for small homes rose 2 percent over the course of the year, while that for medium-sized homes went up 1.7 percent. By contrast, the average price index for large homes actually fell 0.7 percent during the same period, indicating a major curtailment in demand. Chonsei requirements also changed the least for large-sized homes, which means that purchase as well as rental of large homes was down significantly. This trend indicates a strong preference for small and medium-sized homes despite the steady macroeconomic recovery.

The domestic housing market was sluggish, meaning that the transaction volume remained lower than normal. However, in the second half, the number of residential purchases and rentals started to increase. The housing market recovery has recently begun to be seen in all parts of the country. This fact, coupled with expectations that the housing prices have bottomed out, are interpreted as factors that will lead to a housing market turnaround, and the outlook for Korea's housing market has gradually improved. A survey (Real Estate 114) on consumer attitudes toward home transactions reveals that the number of people looking to conclude a presale contract on a new residence rose slightly during the third quarter of 2010.

Market factors influencing housing prices are mixed, although those driving prices up seem to outweigh those bringing prices down. A temporary shock will be felt in the market if interest rates rise faster than originally expected because of inflationary pressure or the outbreak of another financial crisis in Europe. In this event, however, real business cycle indicators and the global economic situation should remain on track for recovery, which should affect the domestic housing market positively.

Factors also exist within the housing market that put upward pressure on prices. A supply shortage is driving up chonsei requirements, and favorable conditions exist for the resumption of development projects in areas outside Korea's capital region. The public also expects local government officials to keep their election promises to increase the accessibility of affordable housing in their respective jurisdictions.

Meanwhile, factors that tend to lower housing prices include a persistent backlog of unsold presale units. Another such factor is the government's growing resolve to implement a broad-based exit strategy from the recent global financial crisis.

Conflicting opinions are voiced with regard to housing supply and demand in Korea. Private sector builders are now more restricted in their capability to supply new housing units. Financing for real estate development projects has dried up because the financial institutions have become more risk averse in the wake of the global financial crisis. From February 2009 debate has raged in Korea's National Assembly over abolishing a government-imposed ceiling on presale prices for new residential units. The resolution of this matter remains unclear. As a result, construction companies are increasingly delaying or cancelling projects to build new high-rise, high-density residential complexes. Market watchers say that the housing supply shortage, brought on by systemic and business factors, will continue for the time being.

Meanwhile, increased housing demand, driven by higher income levels, is also limited right now. Although economic activity is recovering, the unemployment rate in Korea is going up, too. Household income is falling, while household debt is climbing. Structural factors such as higher chonsei rates and concerns over an inadequate housing supply are prompting analysts to

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predict growing demand among prospective presale home buyers, who anticipate that prices will soon rise.

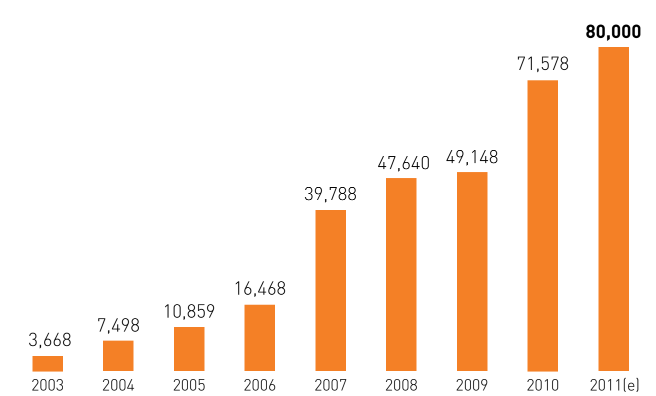
The already-mentioned rise in chonsei rates will spur housing purchases. Supply shortages caused by systemic and business factors are also expected to drive up housing prices in certain localities in Korea's provincial areas. However, private sector construction companies lack the incentives to build new housing on a large scale. Therefore they are expected to participate selectively in new projects, focusing on public housing with outstanding site conditions as well as residential redevelopment (apartment complexes built on old private home sites), and apartment reconstruction projects in downtown areas. In sum, a rapid return to business as usual in the housing sector is unlikely.

3. Overseas Construction Market

A total of 419 Korean construction companies won overseas orders for 588 different projects, worth a total of US$71.57 billion, in 91 countries. This all-time record was set even while the effects of the recent global financial crisis lingered on. The total was nearly 50 percent higher than the US$49.1 billion in new orders received outside Korea during 2009. The year 2010 was significant for Korean builders for various reasons besides the record total in monetary value.

Korea's first builder to win an overseas contract did so in September 1965. The aggregate value of overseas orders from that time reach the US$400 billion market in 2010, after 45 years.

Recent Overseas Construction Orders I Unit : Millions of US dollars I



*source: ICAK

High oil prices since the mid-2000s and an infrastructure development boom in Asia's emerging economies have boosted the overseas market prospects for Korean builders. Most countries around the world cut back on their new investments in the wake of the 2008 global financial crisis, but Korean companies have managed to continue winning new contracts in major countries in the Middle East, a region of focus. The total value of overseas orders received has climbed steadily as a result.

Importantly, the order value increased in numerous Asian countries, to include Singapore, India, Vietnam, Australia, Myanmar, and Turkmenistan in 2010. The total for new orders in Asia neared US20 billion for the year, and this region promises strong growth opportunities going forward.

Korea's engagement in construction projects outside the country contributed greatly to the domestic economy as well as to the advancement of the domestic construction industry. The economy faced difficulties during the two oil shocks of the 1970s (one in 1973 and the other in 1979), but income from overseas construction helped to soften the effects and provided a platform for rapid economic advancement. Korean companies worked alongside those from the most advanced nations, and they came home with advanced technology and management systems.

Overseas construction remains critically important today as a driver of economic growth in Korea. Record new order volumes have been achieved since the end of 2008, despite the onset of a global financial crisis. This business provided much of the strength that enabled Korea to recover from the crisis ahead of all other OECD member nations. Annual revenue from overseas construction has surpassed that earned outside the country from shipbuilding, automobiles or semiconductors.

However, problems with portfolio imbalance remain. New orders received broke the record in 2010, but involvement in the Latin American and African markets is still very weak. In addition, some 80 percent of all orders are for plant projects. Industry experts repeatedly mention the need to improve the project financing system, which lags behind the world's best, and to increase support to small and medium-sized builders

that want to expand into overseas markets.
New overseas orders received climbed to US$71.57 billion in 2010, up 46 percent from the year before, and the Middle East represented US$47.25 billion of this total. Large-scale plant projects such as the US$18.6 billion nuclear power complex and the US$3.4 billion Rabigh 6 power plant project in Saudi Arabia made up some two-thirds of the total in 2010, as they did the previous year. This underscores the importance of the main market segment for Korean construction companies. In terms of regional distribution, the UAE led the list at US$25.6 billion in new orders received, followed by Saudi Arabia, with US$10.5 billion.

New orders showed robust growth in Asia as well, and the future outlook here is bright. The totals from Vietnam, Australia and India were all over US$3 billion in 2010, and the regional figure reached US$18.1 billion, up 66 percent from the year before. The brisk pace of economic growth in the emerging Asian economies is expected to result in rapid expansion of the construction markets here and steady growth in orders for Korean builders.

New orders from Latin America amounted to US$2.1 billion in 2010, three times the total reached in 2009 as the region grappled with the economic crisis. An oil sand processing facility in Canada and a semiconductor factory in the US also raised the regional total for North America significantly year on year.

The amount of overseas orders received has seen robust growth since the mid-2000s and the trend is forecasted to continue in 2011. High oil prices will continue through the year, which means a steady stream of new orders for gas processing plants, power plants and other industrial facilities in oil-producing nations. Solid economic recovery is seen for Asia and Latin America as well. Therefore, new orders from overseas are likely to break the US$80 billion mark for the first time.

The Middle East represents Korea's primary overseas construction market, so the performance of new orders received outside Korea is closely tied to the movement in international oil prices. When oil prices are high, revenue rises for Middle Eastern oil producing nations, which then issue more orders for plants and various kinds of infrastructure. Korean builders then are recipients of more work in the region.

Currently the international oil price is over US$90 per barrel and the price is most likely to remain high throughout 2011. This means than many orders for new plants and infrastructure are forthcoming form countries like the UAE and Saudi Arabia.
In addition, construction activity is expected to recover fully in Asia, and new orders are forecasted to be strong. Korean builders are also busy marketing their services in Latin America and Africa, which could translate into higher totals for the year.

Summary of Operations

New Orders

The value of new orders received by GS E&C in 2010 reached ₩14.1 trillion, which was 9.6 percent higher than the figure posted a year earlier. The domestic real estate market began to slow from 2008 and global business activity remained sluggish because of the residual effects of the global financial crisis. However, GS E&C saw new orders continue to grow on the back of industrial plants and power generation plants overseas as well as buildings for GS group affiliates.

The order backlog at year's end, including ₩11.1 trillion in provisional contracts for housing projects, totaled ₩44.9 trillion, enough work to keep the company operating at full capacity for the next five years. Importantly the value of new power and environment plant orders in the Middle East rose 278 percent year on year, while new orders received for buildings on behalf of GS group affiliates were 71 percent higher in 2010 than they were a year earlier. New projects overseas totaled ₩6.4 trillion, slightly lower than the ₩6.5 trillion posted in 2009 but much higher than the average annual figure over the past five years. The total consists of the usual new orders for oil refineries and gas processing plants in the Middle East, as well as for orders in some new regions and project types: an oil sands processing plant in Canada, fertilizer plant in Australia, and a wastewater treatment plant in Bahrain.

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The confident showing in 2010 will help to provide momentum in the coming year. The company plans to receive new orders totaling ₩16.2 trillion by pursing a balanced approach to growth and profitability.

Sales Revenue

Sales rose 7 percent to more than ₩7.89 trillion in 2010, surpassing the target of ₩7.58 trillion set at the start of the year. This strong showing amid lackluster construction activity in general can be attributed to a balanced portfolio that spans six sectors: civil engineering, industrial plants, office buildings, housing, power plants and environmental facilities.

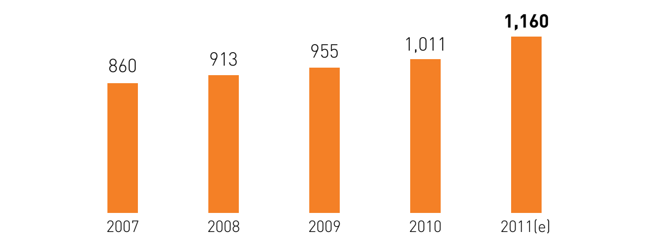
Breaking down the sales total by division, the Architecture Business Division recorded ₩1.44 trillion, up 22 percent from the previous year thanks to a surge in new orders received in 2009. The Plant Business Division saw sales rise 10 percent year on year to ₩2.56 trillion, as the domestic HOU project and overseas plant projects proceeded on schedule. New orders for the Civil Engineering Business Division were down in 2010, but sales rose 29 percent from the previous year to surpass ₩1.07 trillion as work on the government's Four Rivers Restoration Project and large-scale subcontracted work continued smoothly.

Profits

Gross Profit

Gross profit rose 6 percent, from ₩955 billion in 2009 to ₩1.01 trillion in 2010, but the gross margin dipped 0.1 percentage points, from 12.9 percent to 12.8 percent, over the same period. The decline in profitability is temporary as profit is conservatively calculated for plant projects that are in their early stages of execution. On the other hand the cost-to-sales ratio for completed projects by the Civil Engineering, Architecture and Power Divisions greatly improved their figures over 2009. Looking forward to 2011, improving profitability will not be easy, but it should remain about the same as it was in 2010.

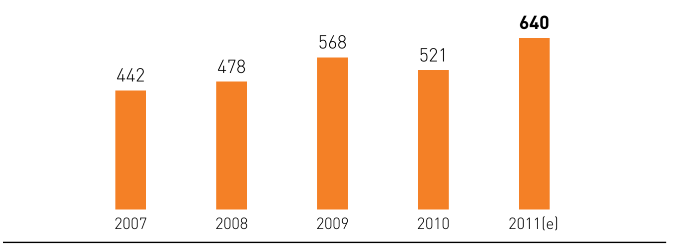
Gross Profit | Unit : Billions of Won |



Operating Profit

Operating profit reached ₩521 billion in 2010, down 8 percent from 2009. One reason for the lower figure is the increase in selling, general and administrative expenses (SG&A) resulting from bids lost amid excessive competition as the overall construction industry struggled. Another cause was that the allowance for bad debt was set to cover the risk related to unsold apartments. Finally, salaries and commissions paid were both higher in 2010 than they were a year earlier. The operating profit target for 2011 has been set at ₩640 billion, based on the new Korean International Financial Reporting Standards (K-IFRS), assuming that the constant emphasis on fiscal soundness will lead to cuts in operating costs and other expenses.

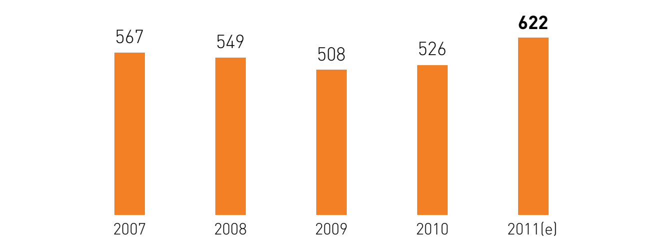
Operating Profit | Unit : Billions of Won |



Ordinary Profit

Ordinary profit rose 4 percent, from ₩508 billion in 2009 to ₩526 billion in 2010. In non-operating expenses, a much lower allowance was set in 2010 than in 2009 for bad debt related to project finance projects for which construction work has not started but land prices are expected to fall. In addition, the strong Korean Won generated some gains on foreign currency transactions. In addition gain on valuation using equity method of accounting and other income were higher in 2010 than they were the previous year. Ordinary profit in 2011 is expected to reach ₩622 billion, reflecting gains from the sales of equity shares as well as the allowance for bad debt to cover additional project finance projects that cannot start construction work.

Ordinary Profit | Unit : Billions of Won |

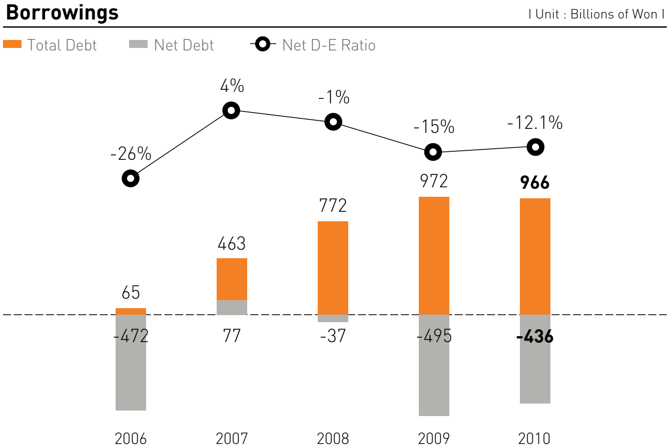


Financial Position

Borrowings

Borrowings at the end of 2010 totaled ₩966 billion, down slightly from the ₩972 billion figure posted a year earlier.

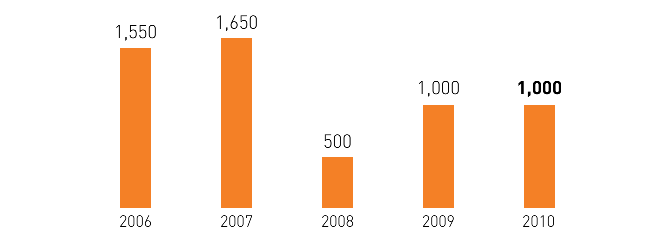
Borrowings | Unit : Billions of Won |



Dividends & Investments

The dividend per share was set at ₩1,000 in 2009 and remained ₩1,000 for 2010. Therefore, the total dividend payout also remained ₩49 billion. After distributing some profits in the form of dividends, the company will invest most of the retained earnings to elevate shareholders' future value.

Dividends & Investments | Unit : Won |



Cash flow

At the end of 2010, cash & cash equivalents stood at ₩1.4 trillion, down 4.7 percent from a year earlier. The changes in cash flow are detailed by activity type as follows:

First, cash flow from operations totaled ₩202 billion. Contributing factors included ₩407 billion in net profit, ₩298 billion in non-cash income and expenses, and minus ₩503 billion in cash inflow resulting from changes in operating assets and liabilities.

Second, cash flow from investment activities generated a cash outflow of ₩198 billion. These activities included investments for future development projects and land purchases for in-house projects.

Third, financing activities generated a cash outflow of ₩72 billion during the year. Specifically, inflow and outflow from short-term borrowings resulted in a ₩312 billion cash increase, while W49 billion was paid out in dividends.

Equity

As of December 31, 2009, 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 45.47% of the total shares issued.