

# MANAGEMENT'S DISCUSSION & ANALYSIS

## 2008 OVERVIEW

Founded in 1947, over the past six decades LG Chem has grown to become one of Korea's leading petrochemical companies. Today, it is dedicated to three core businesses: petrochemicals, information & electronic materials, and industrial materials. In laying the groundwork for future growth, it has steadily stepped up its strategic efforts and investments in areas that offer high growth potential, especially in its information & electronic materials division.

The fiscal 2008 year was not only a time of much uncertainty that posed tremendous challenges in the business environment, it was also marked by an economic slump in Korea as the global economy continued its downward spiral, with unstable financial markets and fluctuating oil prices in the wake of the subprime mortgage crisis in the United States. Still, LG Chem saw its sales rise by 42% over the previous year, to 12,645 billion won, and operating profits by 103% over the previous year, to 1,344 billion won. The rise in both sales and operating profits was due mainly to performance improvement in the petrochemicals division and strong business growth in the information & electronic materials division. Furthermore, net income jumped nearly 46%, to 1,003 billion won, record-highs for LG Chem in terms of both sales and profits.

On a consolidated basis, sales were up 28%, to 14,555 billion won, operating profits were up 24%, to 1,321 billion won, and net income was up 46%, to 1,003 billion won.

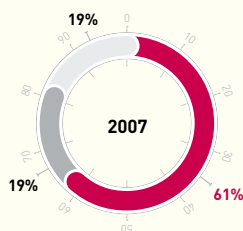
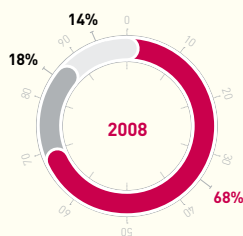
Looking at the performance of business divisions in 2008, the petrochemicals division posted strong profits despite market volatilities brought on by fluctuating oil prices. Although there were certain constraints on business activities over the last year, diversification of products resulted in a dramatic rise in profits, with sales growing 48%, to 10,025 billion won, and operating profits more than 77%, to 903 billion won.

In particular, oxo-alcohol enjoyed growing demand, as did the PVC and synthetic rubbers, whose demand continued to outpace supply due primarily to the industry's lack of facility expansion in recent years, while also contributing to robust profits for LG Chem. In addition, the company's super absorbent polymers (SAP), a downstream of its acrylates, was acquired in September 2008 as part of LG Chem's efforts to achieve vertical integration and to strengthen its downstream specialty businesses. Based on the strength of its integrated business structure, the division will bolster its production competitiveness through diversified exports along with strategic marketing.

The information & electronic materials division continued to record impressive returns. An increased customer base for batteries, coupled with strengthened cost leadership of polarizers and a rise in productivity, were key contributors to the increase in sales and operating profits, which grew 26%, to 2,700 billion won, and 198%, to 451 billion won, respectively.

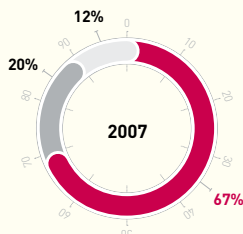
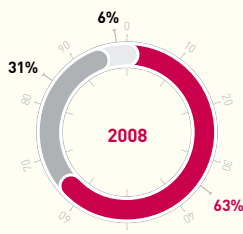
### DIVISIONAL SALES

- Petrochemicals
- Information & electronic materials
- Industrial materials



### DIVISIONAL OPERATING PROFIT

- Petrochemicals
- Information & electronic materials
- Industrial materials



In the battery business, despite the fire at the company's Ochang Complex in March 2008 (which affected the cylindrical and prismatic battery production line), LG Chem was able to minimize any potential damages to customer deliveries by recovering from the accident almost immediately. In fact, stable quality control and a reliable technology base, coupled with aggressive marketing, expanded the company's customer base, which substantially increased both sales and profits.

In the polarizer business, continuous cost reduction efforts across all of its operations, close customer relationship management, and the development of new products led to robust growth despite growing pressure to lower prices because of the slowdown in the LCD industry in the second half of the year. Although sagging IT demand looks inevitable at this stage because of the global slump, LG Chem will continue to outpace its competitors based on cost leadership and to maintain its position as a major global player in this field.

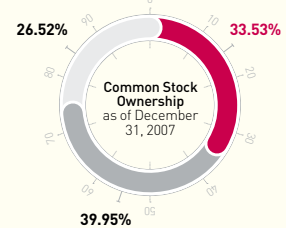
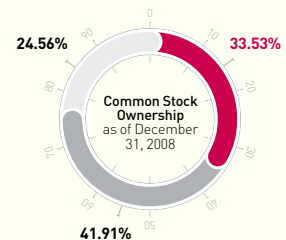
In the industrial materials division, business performance has slackened due mainly to the domestic recession. Sales growth remained flat at 2,091 billion won, and operating profits dropped by 9%, to 85 billion won. The prolonged weakness in the real estate market and the consequent slowdown in construction and rebuilding have also dampened growth in the housing solutions business, while the global downturn decreased sales in the living solutions business overseas. As such, the decision to demerge the industrial materials division was made in an effort to explore a new driving engine for the company. The launch of LG Hausys in April 2009 offers the division a great opportunity to distance itself from the recession and secure a new growth engine by enhancing operational capabilities through continuous restructuring and streamlining.

At LG Chem, research and development efforts have been made to strengthen competitiveness through research in the petrochemicals division, including high polymer compounds, processes, and catalysts. The information & electronic materials division has focused its resources on displays and clean energy products, with a strong synergy effect as a potential driving engine for future growth and profits. Such efforts started to come to fruition when LG Chem was chosen as the exclusive battery supplier for the Chevy Volt, a next-generation electric car. In order to deal with the rapidly changing nature of technologies in growth potential areas, LG Chem has made further global partnerships and pursued joint research activities from the early stages of many R&D projects.

Finally, LG Chem allocated 805 billion won to its investment budget early on in the 2008 fiscal year. However, only 713 billion won was invested, as some projects underwent alterations in response to sudden changes in market conditions. By division, 302 billion won went to the petrochemicals division, 266 billion won went to the information & electronic materials division, 73 billion won went to the industrial materials division, and 72 billion won went to the corporate common division. In 2009, LG Chem plans to invest slightly more in the information & electronic materials division, mostly for mid- to large-sized batteries.

#### SHAREHOLDER COMPOSITION

- LG Corp.
- Korean Individuals & Institutions
- Foreign Shareholders



# MANAGEMENT'S DISCUSSION & ANALYSIS

## FINANCIAL INFORMATION

### FINANCIAL STRUCTURE

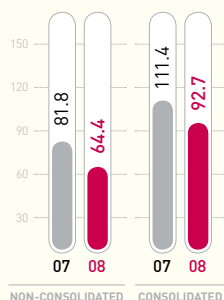
As a result of substantial improvement in business and an increase in cash flow from the previous year, LG Chem's total liability to equity ratio fell over 27.4%p, to 64.4%, and its debt to equity ratio dropped 7.5%p, to 27.6%, at the end of fiscal 2008. On a consolidated basis, the ratios were 92.7% and 54.3%, respectively.

LG Chem expects to increase its investment in mid- to large-sized batteries. Even as the harsh business environment persists along with the global economic downturn, we will dedicate more time and effort to managing cash flow efficiently and keeping our financial structure strong and sound. Based on a principle of "investment within internal cash flow," LG Chem will continue to improve its financial structure in line with sensible approaches to investment, restructuring of low-profit businesses, and efficient management of working capital.

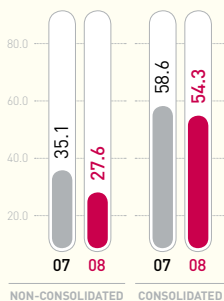
### MAJOR FINANCIAL INDICATORS

	Non-Consolidated		Consolidated	
	2007	2008	2007	2008
Total liability to equity ratio (%)	81.8	64.4	111.4	92.7
Debt to equity ratio (%)	35.1	27.6	58.6	54.3
Interest coverage ratio (X)	10.0	34.3	10.1	13.5
Return on assets (%)	11.3	13.9	10.3	10.8
Return on equity (%)	23.3	24.5	22.8	21.7

### TOTAL LIABILITY TO EQUITY (in %)



### DEBT TO EQUITY RATIO (in %)



### EQUITY

LG Chem decided to demerge its industrial materials division after attaining approval at an extraordinary shareholder's meeting on January 23, 2009. Following the demerger, the number of common and preferred stocks are to be divided by a ratio of 0.8808105:0.1191805, and will then be re-listed on the stock market.

As of December 31, 2008, LG Corp. held 33.53% of LG Chem's total stocks, foreign shareholders held 24.56%, and Korean individuals and institutional investors held 41.91%.

### STOCK INFORMATION (as of Dec. 31, 2008)

	Total Issued Common Shares	Paid-in Capital (in KRW billions)	Foreign Investor Holdings (%)
Common stock	75,238,770	376	24.56
Preferred stock	8,661,251	43	31.77
<b>Total</b>	<b>83,900,021</b>	<b>420</b>	<b>25.30</b>

### FUNDING STRATEGY

#### Liquidity Risk Management

According to its liquidity management policies, LG Chem uses long-term loans for fixed asset investment, such as plant and equipment and short-term loans, for working capital. To guard against liquidity risk, it limits short-term loans to less than 90% of its net working capital.

### Interest Rate Risk Management

An appropriate mix of fixed- and floating-rate loans is used to flexibly respond to fluctuating interest rates. Floating-rate loans are maintained in ranges between 20-40% of total borrowing.

### Foreign Currency Risk Management

LG Chem maintains an optimal level of foreign currency loans, which serves as a natural hedge against foreign exchange exposure. In 2009, the company estimates a net exposure surplus of approximately U.S. \$2.6 billion, and will maintain foreign currency loans of approximately U.S. \$300 million as a hedge.

#### INTEREST EXPENSE (in KRW billions)

	2007	2008	Change
Interest expense	77	39	38
Interest rate	5.25%	4.75%	-0.50%p

#### BORROWING BY CURRENCY (in KRW billions)

	Dec. 2007	Dec. 2008	Change
Korean Won	1,033	929	-104
Foreign currency	328	421	93
<b>Total</b>	<b>1,361</b>	<b>1,350</b>	<b>-11</b>

\* Bond issue discount excluded. Foreign capital influx via currency swap agreement is listed in KRW.

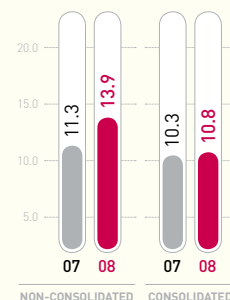
### DIVIDEND POLICY

LG Chem considers dividends to be the foremost means of returning profits to its shareholders. As determinants of dividend policy, it takes various factors into account, including the sufficiency of its capital resources for securing future growth, investment plans, and financial soundness.

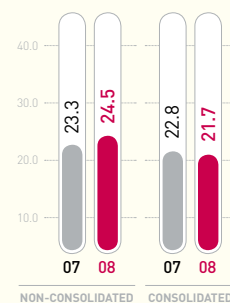
In fiscal 2008, the company decided to pay an annual cash dividend on its common stock of 2,500 won (50% of face value) per share as well as 2,550 won (51% of face value) per share on its preferred stock. Based on its earnings, the determinants of dividend payouts included investments in fostering its business competitiveness and future growth.

LG Chem is committed to leveraging shareholder value by enhancing the competitiveness of its core businesses and generating solid profits at a steady pace, as it maintains dividends at a substantial level that can ensure both the financial soundness of the company and satisfy shareholder expectations.

#### RETURN ON ASSETS (in %)

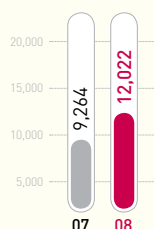


#### RETURN ON EQUITY (in %)

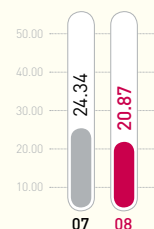


# MANAGEMENT'S DISCUSSION & ANALYSIS

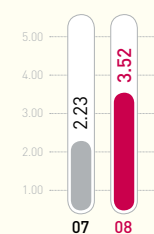
## EPS (in KRW)



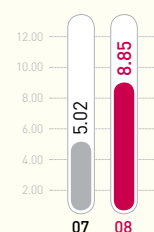
## DIVIDEND PAYOUT RATIO (in %)



## DIVIDEND YIELD RATIO, COMMON (in %)



## DIVIDEND YIELD RATIO, PREFERRED (in %)



## DIVIDEND SUMMARY

	2007	2008
Net income (in KRW millions)	686,205	1,002,585
EPS (in KRW)	9,264	12,022
Total dividends (in KRW millions)	167,006	209,202
Dividend payout ratio (in %)	24.34	20.87
Dividend payout at face value, common (in %)	40	50
Dividend payout at face value, preferred (in %)	41	51
Dividend yield ratio, common (in %)	2.23	3.52
Dividend yield ratio, preferred (in %)	5.02	8.85

## DEMERGER OF INDUSTRIAL MATERIALS DIVISION

Due to their unique nature, the petrochemicals division and industrial materials division have shown inconsistencies in their strategic directions such as corporate culture and customer base. After an extraordinary shareholder's meeting, it was decided that the industrial materials division would be launched as a new company called LG Hausys and officially demerged on April 1, 2009.

Based on production infrastructure of operational excellence, LG Chem will be reborn as a specialized chemical company that focuses on petrochemical goods, small and mid-to large-sized batteries for cars, and information and electronic materials through this demerger. At the same time, LG Hausys will shed its traditional chemical industry image and grow as an impressive B2C-based business.

Even though it had more impressive results than rival companies in the field, the industrial materials division (the forerunner to LG Hausys) had difficulty attracting the attention it deserved from investors because its profits were overshadowed by LG Chem's petrochemicals division and information & electronics division. However, this demerger will enable LG Hausys to secure capital resources more easily for new projects, as its marketing and R&D secure a sound structure for sustainable growth.

## CAPITAL EXPENDITURE

In 2008, LG Chem's total investments amounted to 713 billion won. One particularly noteworthy investment was the 87 billion won it spent on acquiring the super absorbent polymer (SAP) business, its downstream business of acrylates, from Kolon. To proactively cope with adverse business factors in the global petrochemical industry, including a rapidly increasing number of chemical production facilities in the Middle East, LG Chem is carrying out an expansion of its bisphenol-A (BPA) plants and a debottlenecking of its synthetic rubber lines as part of its product portfolio reshuffle with specialty products. With respect to information and electronic materials, LG Chem invested 42 billion into expanding electrodes and cylindrical batteries, and 64 billion won into building its seventh production line for polarizers.

In 2009, LG Chem will focus its investments on securing future growth engines rather than expanding existing business. Starting with investments in mid-to large-sized batteries for HEVs, which are expected to produce tangible results from fiscal 2009, and continuing with technology transfers from Schott, a detailed LCD glass investment plan will soon be in clear view.

LG Chem is constantly exploring new business models and mergers & acquisitions in the display and clean energy field, in which synergistic opportunities can amply foster sustainable growth and constant profits.

### 2009 OUTLOOK

Market watchers say the 2009 business outlook remains bleak due to the global recession and sluggish demand. Nonetheless, LG Chem will continue to carry out its vision of Speed Management, doubling the speed of strategy implementation and changes in corporate culture, while committing itself to its three main tasks of strengthening core businesses, innovating customer values, and increasing organizational capabilities to overcome worldwide economic hardship, as it secures a differentiated, competitive edge.

First, we will not only accelerate our efforts to enhance our competitiveness with differentiated products, but will also guarantee cost leadership to strengthen core businesses. LG Chem's petrochemicals division plans to further its cost reduction efforts even more by optimizing its rate of operations and minimizing its energy consumption rate, while its information and electronics division concentrates on taking full advantage of the internalization of core materials and improving productivity. LG Chem will also strengthen its market leadership by increasing high-value products and providing customers with precisely the products they want and when they want them.

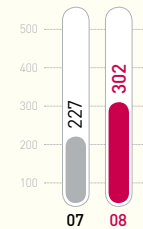
Next, if there is one thing you never sacrifice — no matter how difficult the situation may be — it is customer value innovation. We will double our efforts to create new values for our customers by consistently pursuing solution partnerships by adopting new technologies in the clean energy business, including mid-to large-sized batteries and the next-generation IT business.

Lastly, we will continue to enhance our capabilities as an organization to achieve the aforementioned goals as well as to strengthen core businesses and innovate customer values. Furthermore, LG Chem will establish a unique globalized model to follow by strengthening employee communication capabilities in the global market place and promoting localization at overseas sites.

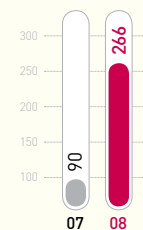
Based on the principles of Speed Management —early, fast, and real time— LG Chem will implement a “focus-on-core” business strategy and a “find the strength and make it stronger” strategy among employees and the organization, establishing itself as an internationally-renowned company with excellent performance results.

#### DIVISIONAL CAPITAL INVESTMENT

##### PETROCHEMICALS (in KRW billions)



##### INFORMATION & ELECTRONIC MATERIALS (in KRW billions)



##### INDUSTRIAL MATERIALS (in KRW billions)

