

# Remarks for the Institute for Global Economics 17 November 2015



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# SOUTH KOREA:

## Economic retrospective and prospective

- South Korea has emerged stronger from the two crises in 1997 and 2008
- Fiscal, financial and institutional factors have strengthened over time and relative to most other peer countries
- Prospects are relatively favorable
- Management of structural challenges will determine the pace of Korea's convergence with the advanced economies

# Pre-1997 crisis setting

“One of the lessons for South Korea and other leading EMs is that they cannot take for granted that the world will be enthralled by (their) economic and financial opportunities...there are many strengths, but is important that the government not become complacent. One of the lessons of the Mexican crisis is that complacency costs dearly.”

Charles Dallara, IIF Managing Director: IGE speaker, 27 January 1995

# BOK Financial Stability Index

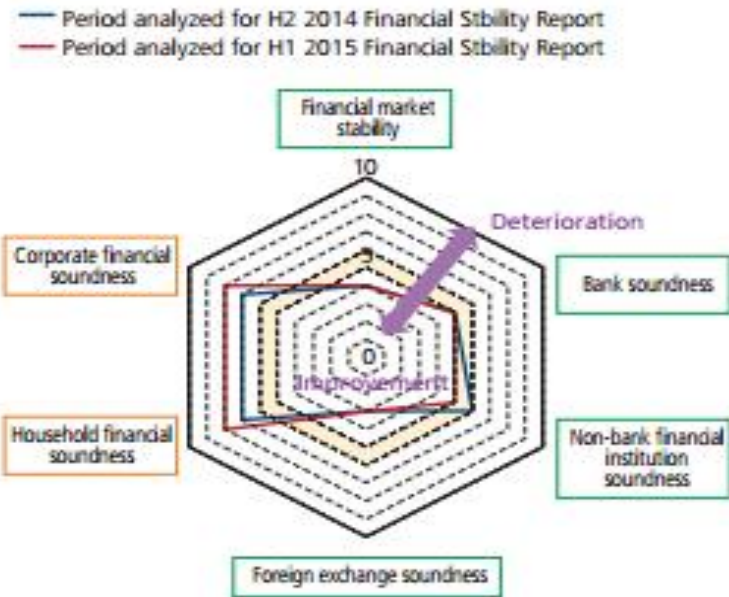


Note: 1) The Financial Stability Index is measured based on values from 0 (min) to 100 (max). The closer it is to 100, the higher the level of instability. <The level during the Asian financial crisis (Jan. 1998) equals 100>

Source: The Bank of Korea

# Korea's Financial Stability Map

Financial Stability Map™



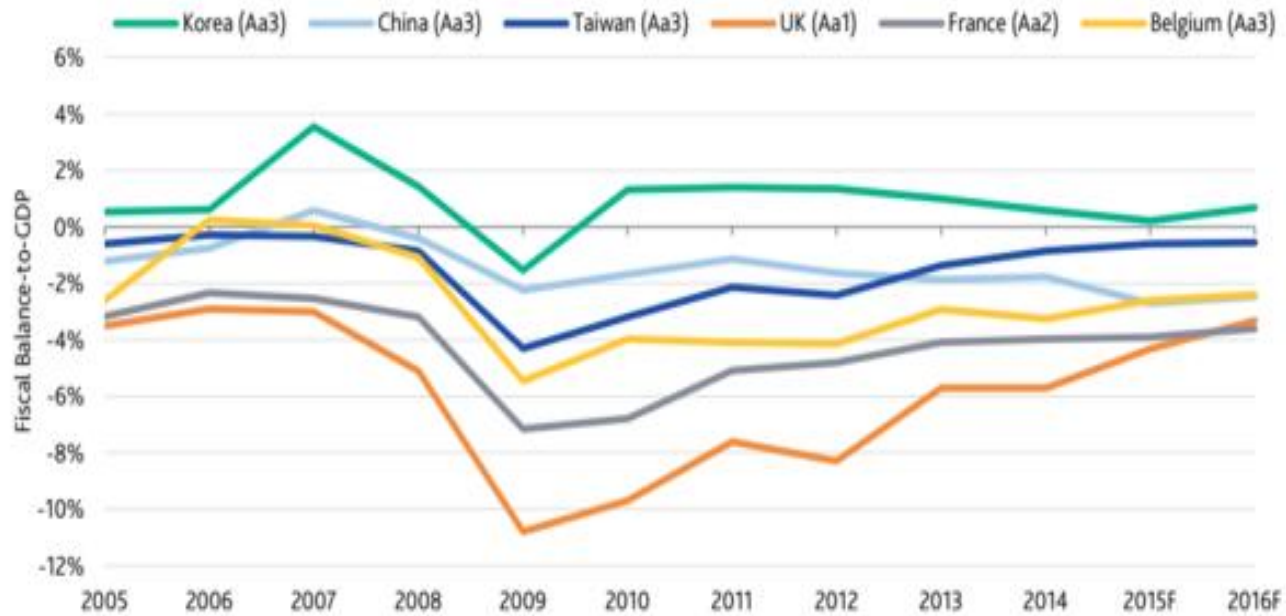
- Notes: 1) The closer to the center, the greater the degree of stability  
2)   Macprudential soundness condition dimensions,  
  Financial system dimensions

# Korea's sovereign credit recovery

- Current      Aa3
- Dec 1997      Ba1
- 1993      A1
- Nov 1986      A2

# Korea's strong fiscal fundamentals--budgetary

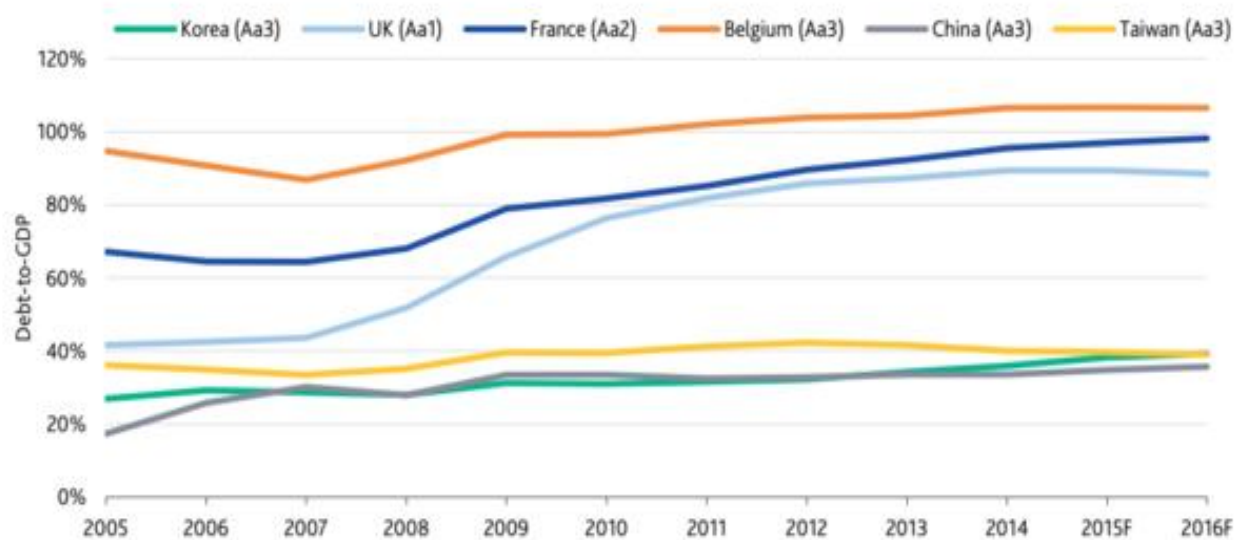
Korea's Fiscal Balance Compares Favorably to Similarly Rated Peers



Source: National authorities, Moody's

# Korea's strong fiscal fundamental--debt

Korea's Debt Burden Compares Favorably to Most Similarly Rated Peers

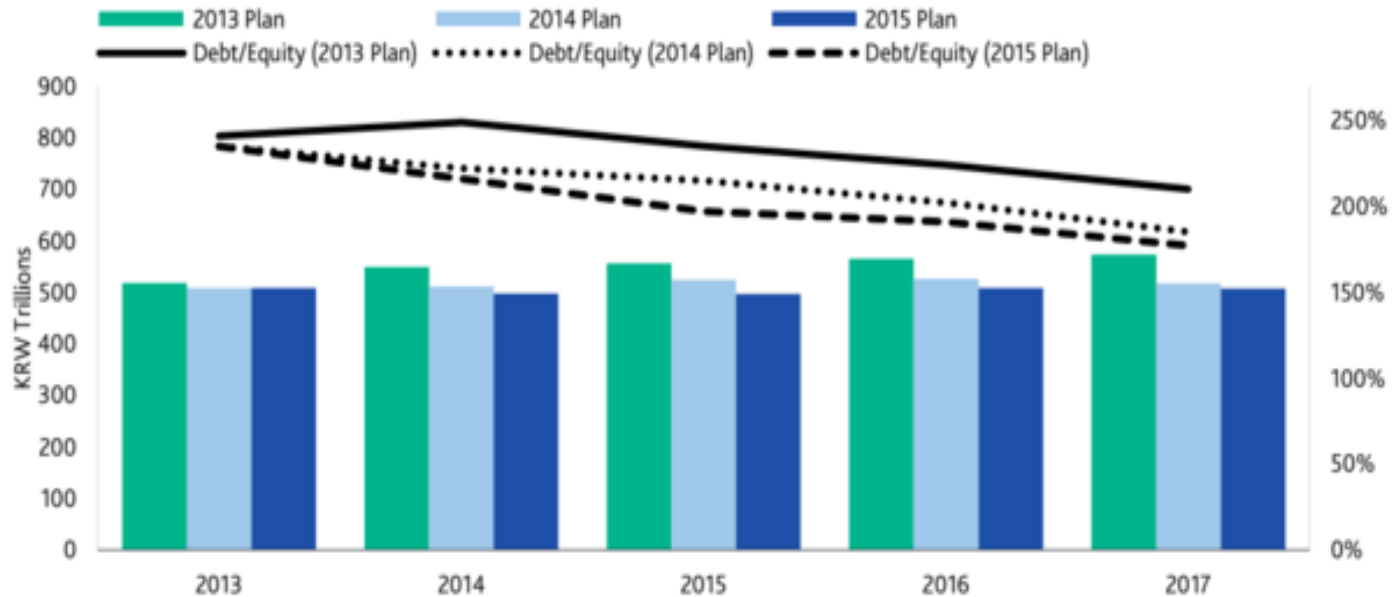


Source: National authorities, Moody's



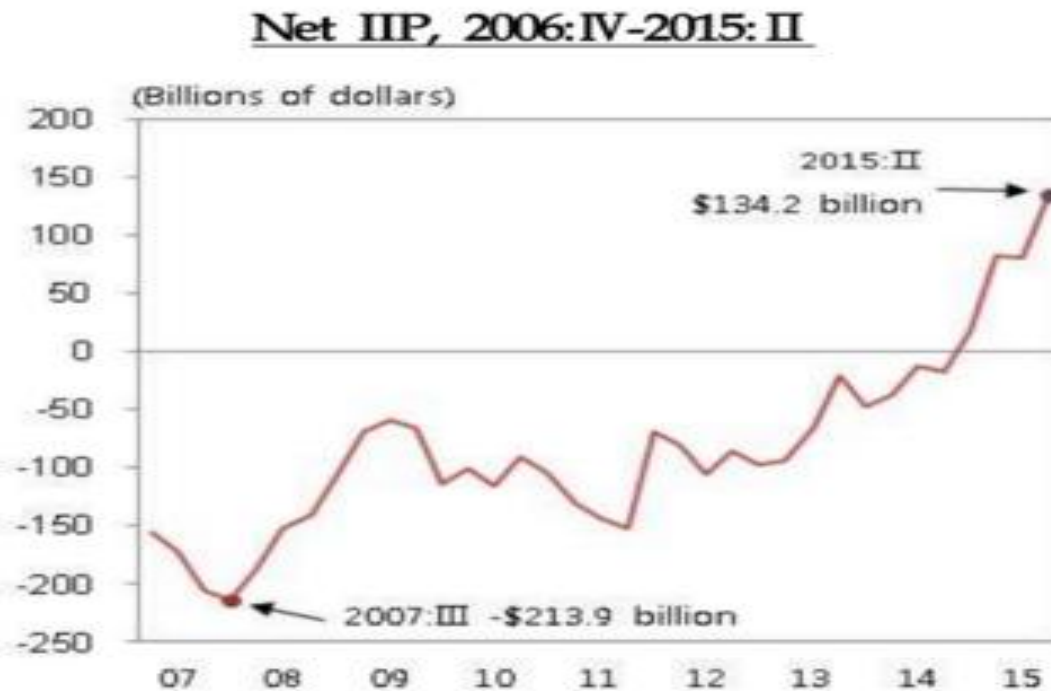
# Korea's fiscal risk: off-MOSF balance sheet public debt

Government Plans to Lower Public Institution Debt Will Lower Contingent Risks



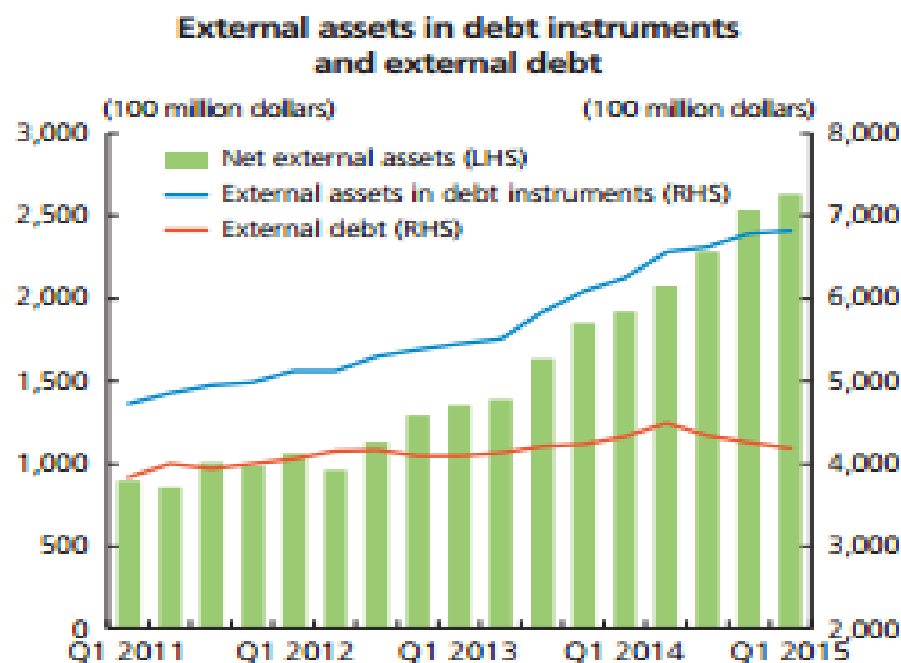
Source: Korea Ministry of Strategy and Finance

# Korea's reduced external vulnerability: Net asset International Investment Position



- Source: Bank of Korea

# Korea's net external credit cushion



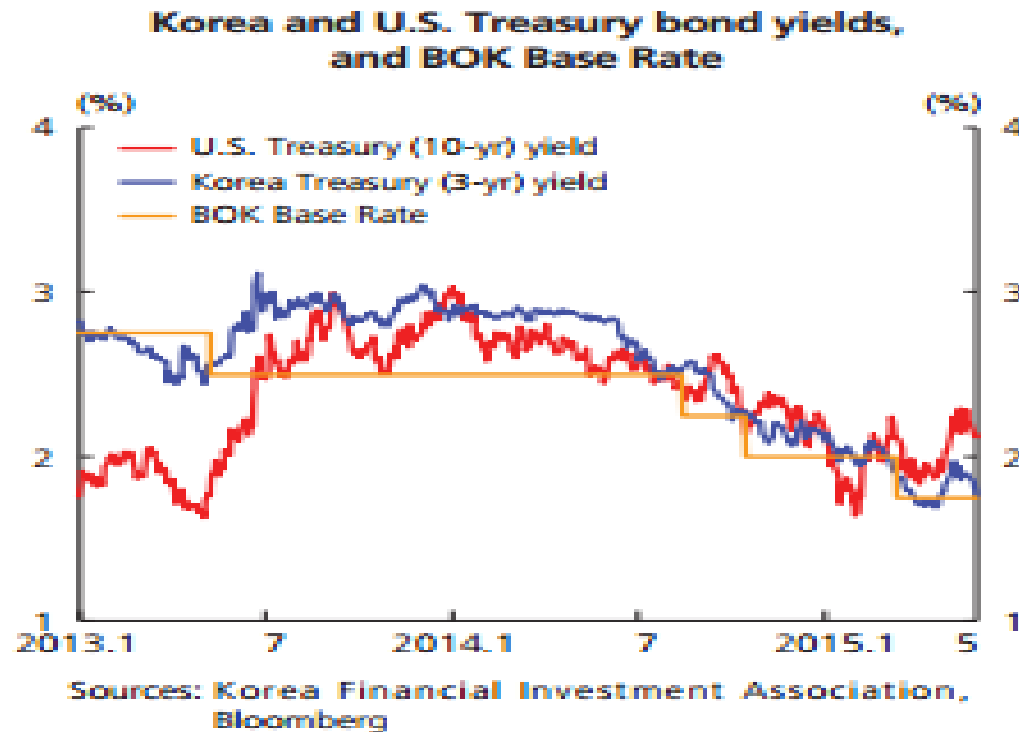
Source: The Bank of Korea

# Korea's monetary policy space

	CPI	INTEREST RATE	NIIP (% of GDP)	FX RESERVES (\$ BILLION)
KOREA	0.9	1.5	9.4	368
JAPAN	0.2	0.0-0.1	66.5	1,249
CHINA	1.6	1.5	17.1	3,514

Note: NIIP is a 2015 estimate; FX reserves from latest month in 2015—October or November  
Source: IMF Fiscal Monitor, April 2015; Trading Economics; National Sources and IMF WEO

# KTB yields have tracked BOK policy easing



# Korea's fiscal policy space

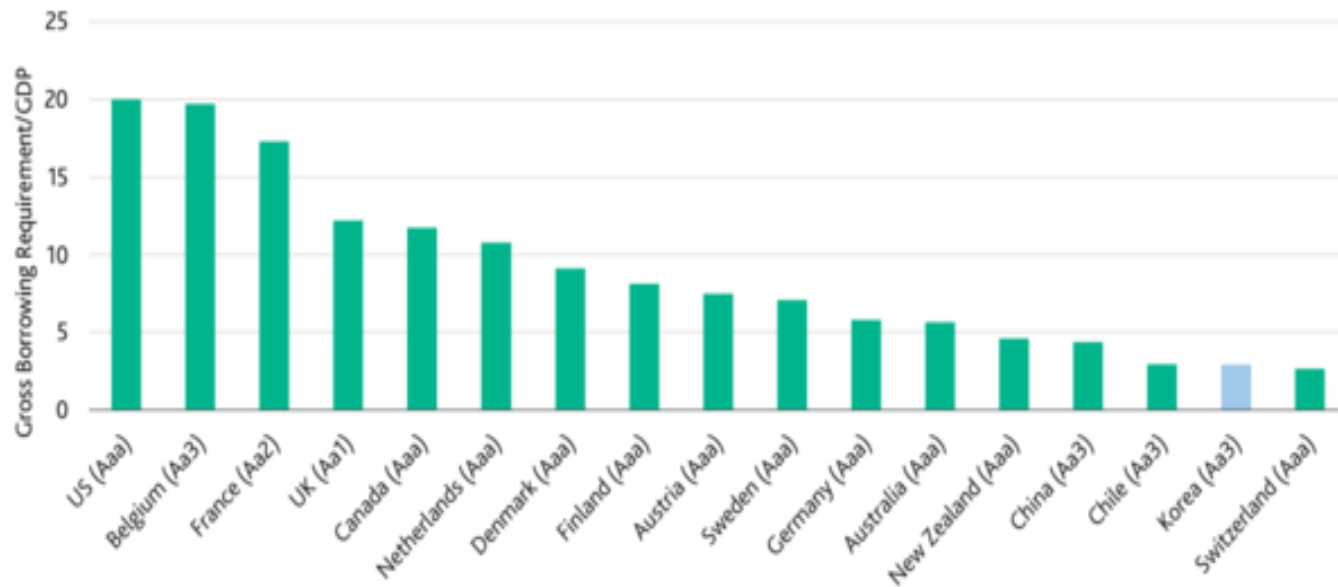
	GROSS FINANCING NEED, 2015	NONRESIDENT HOLDING OF GENERAL GOVERNMENT DEBT, 2014 (PERCENT OF TOTAL)
KOREA	2.9	13.0
JAPAN	52.7	8.1
CHINA	4.4	<1*
SPAIN	21.5	42.5

\* estimate

Source: IMF Fiscal Monitor, April 2015

# Korea's fiscal strength: low GFN

Korea's 2015 Gross Financing Needs Are Much Lower Than Most Aaa-Rated Sovereigns'



Source: IMF Fiscal Monitor, April 2015.

# Fiscal space raises debt affordability

10-year government bond yields (12 Nov):

- Korea 2.33%
- China 3.19%
- U.S. 2.32%

Sources: ADB Asian Bonds Online, US Treasury



# GDP growth performance and outlook

	1997-2006 (Average)	2015	2016	2020
KOREA	4.9	2.7	3.2	3.6
CHINA	9.4	6.8	6.3	6.3
JAPAN	0.9	0.6	1.0	0.7
UNITED STATES	3.3	2.6	2.8	2.0
MAJOR ADVANCED ECONOMIES	2.5	1.9	2.2	1.7
EMERGING MARKETS	5.4	4.0	4.5	5.3

Note: Major Advanced Economies are G7 and Euro Area Countries  
Source: IMF World Economic Outlook, October 2015

# Korea's exports: global growth and the yen

## Won / yen rate and export volume

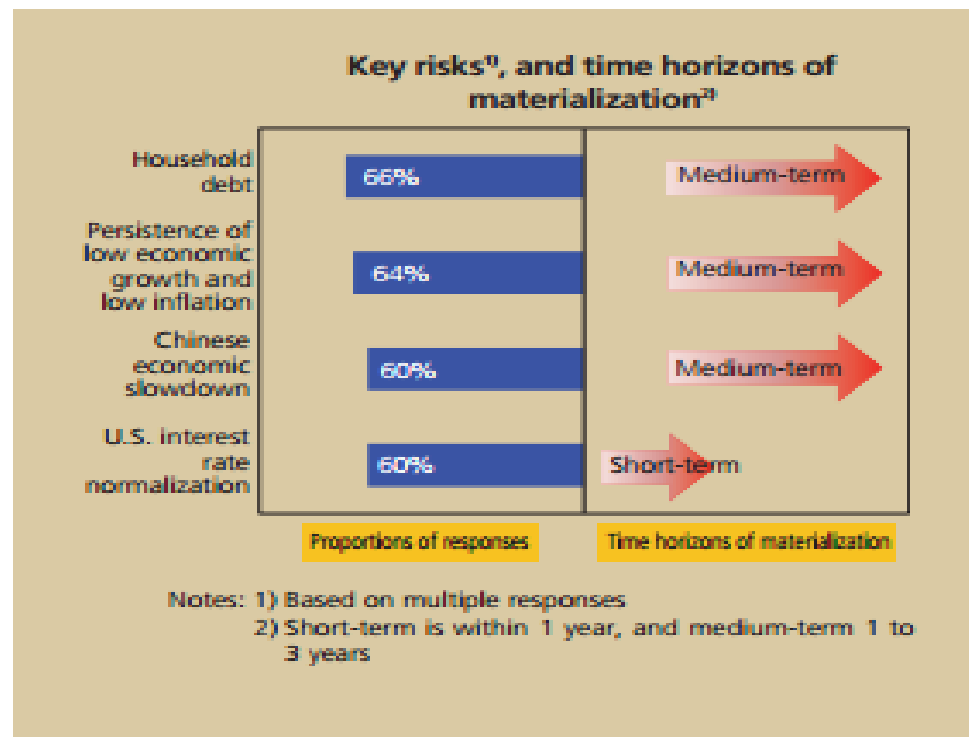
	1995.4– 1997.2	2004.1– 2007.2	2012.9– 2015.3
Rate of won appreciation against the yen <sup>1)</sup>	26.4	39.5	56.6
Rate <sup>2)</sup> of export volume growth	18.4	32.8	6.9
Rate <sup>2)</sup> of global import demand growth	15.3	27.1	6.3

Notes: 1) Percentage appreciations of won/yen rate from beginnings of decline to ends of decline

2) Three-month moving average basis

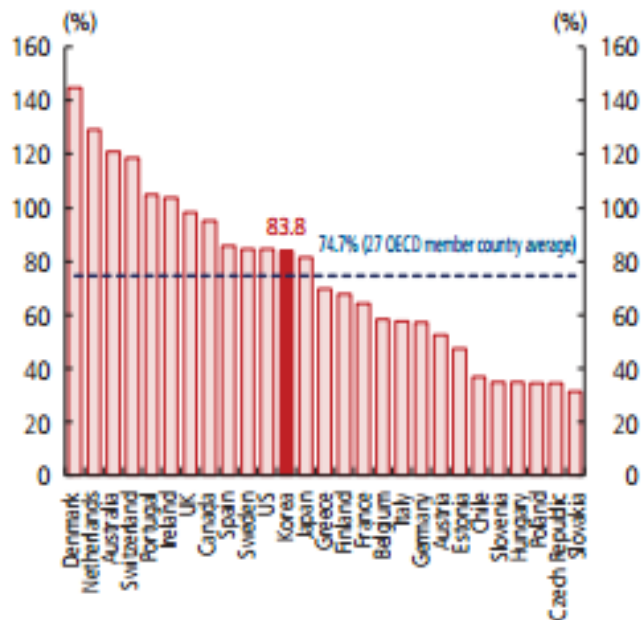
Sources: The Bank of Korea, CPB

# BOK Systemic Risk Survey, May 2015



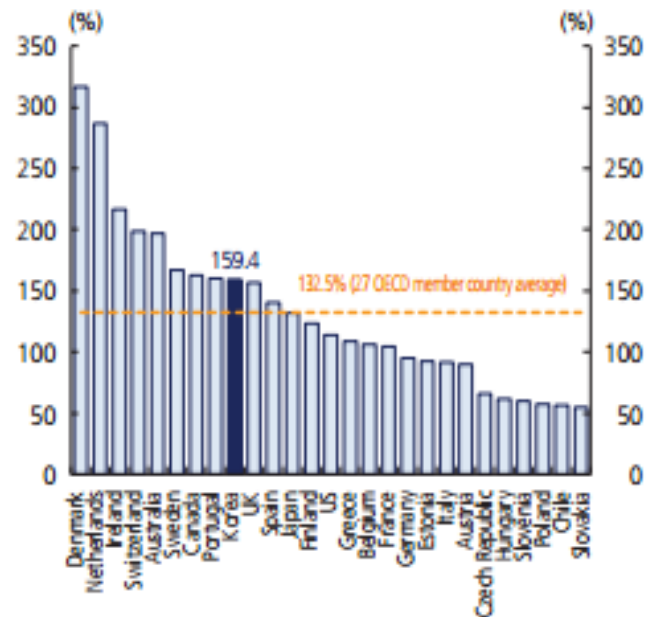
# Household debt, “a major risk factor”

<Figure I- 6> Household debt<sup>1)</sup>-to-nominal GDP ratios<sup>2)</sup> in major countries



Notes: 1) Flow of funds statistics basis  
 2) End-2012 basis  
 Sources: The Bank of Korea, OECD

<Figure I- 5> Household debt<sup>1)</sup>-to-disposable income ratios<sup>2)</sup> in major countries



Notes: 1) Flow of funds statistics basis  
 2) End-2012 basis  
 Sources: The Bank of Korea, OECD

# South Korea's structural challenges

- “....there is a possibility of our growth engines continually weakening due to structural factors....Sectoral imbalances, labor market rigidity and excessive regulation.”

BOK Governor Lee Juyeol. “Speech Commemorating the Banks 65<sup>th</sup> Anniversary.” 12 June 2015

# NORTH KOREA:

## What if it were a Frontier Market?

- Byungjin is an incomplete and piecemeal reform strategy—North Korea is far from the Frontier
- Economic reform requires external opening
- Sustained economic advance is very rare among FM economies

# Systems move into the Frontier when they open to trade and investment

Many frontier markets exhibit a high degree of trade openness  
(Trade Openness, % of GDP, 2014)



Source: Moody's Investors Service

# But FMs face BOP constraints

Current account imbalances are significantly higher than in emerging markets  
(Median, % GDP)



Source: Moody's Investors Service



# Frontier Market credit entropy

Frontier market sovereigns: How have credit ratings moved?  
(Current and originally assigned foreign currency bond ratings)

Sovereign	Current Rating	Initial Rating	Year Rating Assigned
Albania	B1	B1	2007
Armenia	Ba3	Ba2	2006
Bangladesh	Ba3	Ba3	2010
Bolivia	Ba3	B1	1998
Ethiopia	B1	B1	2014
Fiji	B1	Ba1	1999
Georgia	Ba3	Ba3	2010
Jordan	B1	Ba3	1996
Kenya	B1	B1	2012
Nigeria	Ba3	Ba3	2012
Rep of Congo	Ba3	Ba3	2013
Sri Lanka	B1	B1	2010
Vietnam	B1	Ba3	2005
Zambia	B2	B1	2012

Sovereign	Current Rating	Initial Rating	Year Rating Assigned
Belarus	Caa1	B1	2007
Bosnia	B3	B3	2004
Cambodia	B2	B2	2007
DRC	B3	B3	2013
Egypt	B3	Ba1	2001
Ghana	B3	B1	2012
Honduras	B3	B2	1998
Moldova	B3	Ba2	1997
Mongolia	B2	B1	2005
Mozambique	B2	B1	2013
Nicaragua	B2	B2	1998
Pakistan	B3	Ba3	1994
PNG	B1	B1	1998
Senegal	B1	B1	2011
Uganda	B1	B1	2013

Note: Orange shaded sovereigns denote those that are at a lower rating level currently than they were originally assigned. Green shaded areas denote upward movement. Source: Moody's Investors Service

Source: Moody's Investors Service

# Conclusion

- Reform in North Korea is not meaningful until it opens to global trade and finance
- Yet political and institutional factors will hold back reform progress and sustainability
- President Park's Northeast Asia Peace and Cooperation Initiative is a long shot, but the only one
- A bonanza would require a lot of time and work

# THANK YOU



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