

KOREA

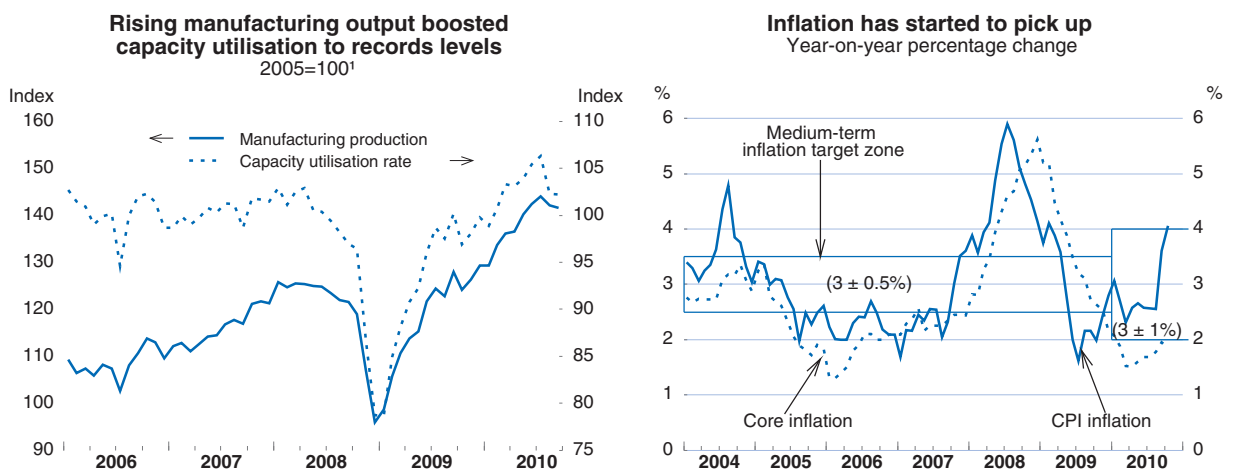
Although Korea's strong recovery from the 2008 global recession slowed in the latter half of 2010, double-digit export growth and buoyant domestic demand are projected to boost growth to a 5% rate by late 2011. The decline in the unemployment rate to less than 3½ per cent in mid-2010 and high capacity utilisation are putting upward pressure on wages and inflation.

With the economy approaching capacity constraints, fiscal policy should continue to focus on achieving the deficit-reduction targets in the medium-term fiscal plan, while the central bank should normalise interest rates. An appreciation of the won would also help contain inflation pressures. Sustaining high growth over the medium term requires structural reforms to enhance productivity, particularly in services. Expanded assistance to small and medium-sized enterprises should be phased out, not least to avoid supporting non-viable firms.

Although growth has slowed to a more sustainable rate...

After reaching a 7.3% annual rate during the first half of 2010, the fastest in a decade, output growth has slowed, in line with trends in other Asian countries. Export growth moderated significantly in the third quarter, reflecting weaker demand from Asia, notably China. Slower export growth, in turn, has damped increases in business investment and industrial production. In addition, inventory rebuilding, which accounted for one-half of output growth in the first half of 2010, appears to be nearing an end. Construction investment has been weak, mainly due to the residential sector. Moreover, housing prices are falling slightly, given the large stock of unsold homes, despite government measures to revitalise the housing market. In particular, the debt-to-income regulation on mortgage lending, which had been tightened in October 2009, was abolished until March 2011 in most of the country and transaction taxes on housing have been reduced or waived.

Korea



1. Seasonally-adjusted.

Source: Korea National Statistical Office, OECD Economic Outlook 88 Database and Bank of Korea.

StatLink <http://dx.doi.org/10.1787/888932345888>

Korea: Demand, output and prices

	2007	2008	2009	2010	2011	2012
	Current prices KRW trillion	Percentage changes, volume (2005 prices)				
Private consumption	530.3	1.3	0.2	4.3	4.6	5.0
Government consumption	143.3	4.3	5.0	3.9	2.0	3.0
Gross fixed capital formation	278.2	-1.9	-0.2	7.9	5.7	5.3
Final domestic demand	951.7	0.8	0.8	5.3	4.5	4.8
Stockbuilding ¹	8.6	0.6	-4.6	2.3	-0.1	0.0
Total domestic demand	960.3	1.4	-3.8	7.9	4.4	4.8
Exports of goods and services	408.8	6.6	-0.8	14.3	12.8	13.5
Imports of goods and services	394.0	4.4	-8.2	18.3	13.3	13.5
Net exports ¹	14.7	1.0	4.0	-1.3	0.0	0.1
GDP at market prices	975.0	2.3	0.2	6.2	4.3	4.8
GDP deflator	–	2.9	3.4	3.2	1.8	2.6
<i>Memorandum items</i>						
Consumer price index	–	4.7	2.8	2.8	3.2	3.4
Private consumption deflator	–	4.5	2.6	2.4	3.1	3.4
Unemployment rate	–	3.2	3.6	3.7	3.4	3.3
Household saving ratio ²	–	2.9	3.6	2.8	2.9	2.8
General government financial balance ³	–	3.0	0.0	1.6	2.1	3.0
Current account balance ³	–	-0.5	5.2	3.0	2.3	2.4

Note: National accounts are based on official chain-linked data. This introduces a discrepancy in the identity between real demand components and GDP. For further details see *OECD Economic Outlook Sources and Methods* (<http://www.oecd.org/eco/sources-and-methods>).

- Contributions to changes in real GDP (percentage of real GDP in previous year), actual amount in the first column.
- As a percentage of disposable income.
- As a percentage of GDP.

Source: OECD Economic Outlook 88 database.

StatLink  <http://dx.doi.org/10.1787/888932347636>

... the economy is facing capacity constraints

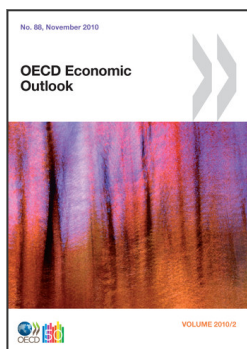
The growth slowdown coincides with signs that the economy is approaching capacity constraints. Rapid employment gains have reduced the unemployment rate to around 3½ per cent, close to its pre-crisis level, and the capacity utilisation rate in manufacturing reached a record high in July. Consumer price inflation, which had been steady at 2.6% (year-on-year) since April 2010, jumped to 4.1% in October, above the central bank's 2% to 4% inflation target, reflecting in part a jump in food prices. Monetary conditions are exceptionally relaxed, particularly given the stage of the business cycle. Although the Bank of Korea raised the policy interest rate by 25 basis points from a record-low 2% in July, it remains negative in real terms. In addition, the won has depreciated by about 5% since April in trade-weighted terms and by about 13% relative to the yen, significantly boosting Korea's export competitiveness. Significant fiscal consolidation is under way. Central government spending is set to slow to a 4.8% annual rate in nominal terms under the National Fiscal Management Plan for 2010-14, helping to reduce the consolidated central government deficit (excluding the social security surplus) from 4.1% of GDP in 2009 to 1.1% in 2012, despite cuts in personal and corporate income tax rates. The Plan projects a surplus by 2014.

Output growth is projected to pick up strongly...

Following the recent slowdown, output growth is projected to pick up to a 5% rate by late 2011, in spite of some drag from fiscal policy. Business and consumer confidence remains high, despite some decline in recent months. Competitiveness gains should help sustain double-digit export growth, thereby encouraging business investment. Construction investment is likely to turn positive as a result of the policies to promote the housing sector. Tighter labour market conditions are expected to lead to faster wage growth, underpinning buoyant private consumption. With growth picking up, a normalisation of the policy interest rate is needed to keep inflation within the central bank's target zone. Strong domestic demand growth will also reduce the current account surplus from 5.2% of GDP in 2009 to 3% in 2010.

... depending on developments in the world economy

Given that exports account for almost one-half of GDP in Korea, the world's eighth-largest exporter, the major risks relate mainly to the global economic environment. The outlook is particularly sensitive to demand from China, which accounts for one-third of Korean exports. In addition, a realignment of exchange rates could have a significant impact on Korean trade. On the domestic side, the major concern is the high level of household debt, which exceeds 150% of household income. As mortgage loans, primarily with floating interest rates, account for 94% of household debt, rising interest rates could have a larger-than-expected impact on private consumption. Another uncertainty is the pace of restructuring of SMEs, which received significant support in 2008-09 to cope with the crisis and recession.



From:
OECD Economic Outlook, Volume 2010 Issue 2

Access the complete publication at:
https://doi.org/10.1787/eco_outlook-v2010-2-en

Please cite this chapter as:

OECD (2010), "Korea", in *OECD Economic Outlook, Volume 2010 Issue 2*, OECD Publishing, Paris.

DOI: https://doi.org/10.1787/eco_outlook-v2010-2-24-en

This work is published under the responsibility of the Secretary-General of the OECD. The opinions expressed and arguments employed herein do not necessarily reflect the official views of OECD member countries.

This document and any map included herein are without prejudice to the status of or sovereignty over any territory, to the delimitation of international frontiers and boundaries and to the name of any territory, city or area.

You can copy, download or print OECD content for your own use, and you can include excerpts from OECD publications, databases and multimedia products in your own documents, presentations, blogs, websites and teaching materials, provided that suitable acknowledgment of OECD as source and copyright owner is given. All requests for public or commercial use and translation rights should be submitted to rights@oecd.org. Requests for permission to photocopy portions of this material for public or commercial use shall be addressed directly to the Copyright Clearance Center (CCC) at info@copyright.com or the Centre français d'exploitation du droit de copie (CFC) at contact@cfcopies.com.