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Budgetary Measures underpin the Korean Economy despite stagnant external demand

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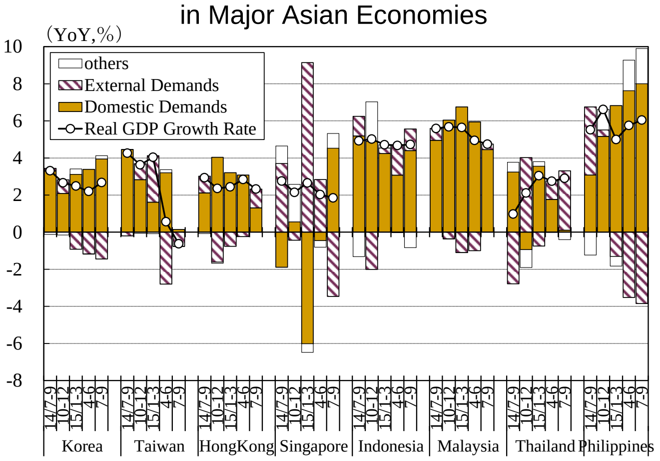
In Asia, where sluggish external demands continue to heavily weigh on the economic growth, the real GDP growth rate of the Korean economy accelerated to +2.7% YoY in July-Sept. quarter from +2.2% YoY in the previous quarter. This contrasted with the situation in other NIEs with similarly high export dependency ratio on China which experienced deceleration or negative growth and with Malaysia and Thailand, both with high export dependency amongst the ASEAN countries, which had a weak growth. (Chart 1)

The first acceleration in 6 quarters of the growth rate of the Korean economy is mainly accounted for the fiscal measures that the government implemented ahead of other countries. Since the Global Financial Crisis in 2008, the Korean economy had continued to recover driven by exports. But since the middle of 2014, domestic demands such as investments began to slow down affected by the economic slowdown of China which accounts for the largest destination of Korean exports (25% in 2014) and the sluggish exports of materials (30% of total exports in 2014, ex. fuels, chemicals and steel) reflecting the fall in prices triggered by declining resource prices. Thus the stagnation of the Korean economy became apparent earlier than other Asian countries. Factors other than exports pushed down growth such as the ferry capsizing accident in the first half of 2014 and the spread of infectious diseases in the early months of 2015. So the government implemented a series of measures to prop up the domestic economy, which included a large scaled stimulus package (3% of GDP, July 2014), reduction of consumption tax (such as reduction by 1.5% for automobiles and large home appliances which account for about 15% of retail sales, August 2015), as well as promotion of scale large sales (October 2015). As a result, the domestic demands in Korea have been on a rise especially in consumption and construction investment in spite of a slowing export growth. Korea is one of a few countries with a budget surplus and it was able to support the economy with increased expenditures at the time of the Global Financial Crisis in 2008. This relatively high availability of fiscal resources is also one of the advantages of Korea. (Chart 2)

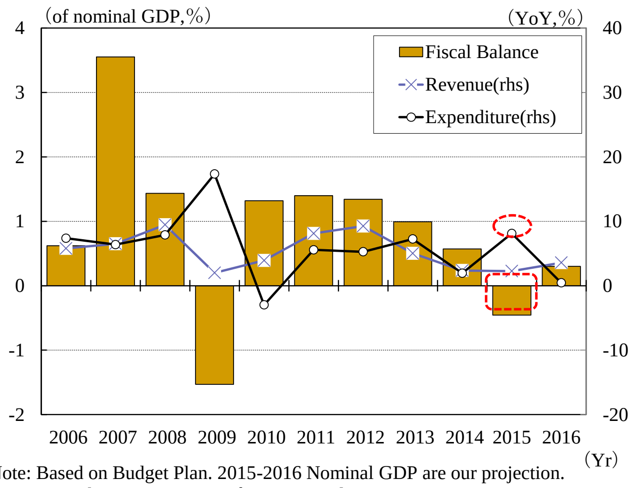
Looking ahead, Korea will be able to continue to rely on the fiscal policies to support the economy, although the pace of recovery will be constrained by the deceleration of Chinese economy. The government clearly described in its budget plan for 2016 (January-December 2016), enacted on December 2, its intention to implement about 70% of its budget expenditures in the first half of 2016 to boost economic recovery. Although room for further monetary easing is limited, because of concern over possible instability of the financial market due to a rise of US interest rates, continued stimulus from budget expenditures will support the Korean economy toward, although modestly, a sustained domestic-demand led recovery.

Chart1：Real GDP Growth Rate in Major Asian Economies



Source: Respective country statistics, BTMU

Chart2：Fiscal Balance in Korea



Note: Based on Budget Plan. 2015-2016 Nominal GDP are our projection.
Source: South Korea Ministry of Strategy and Finance, BTMU

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