Korea

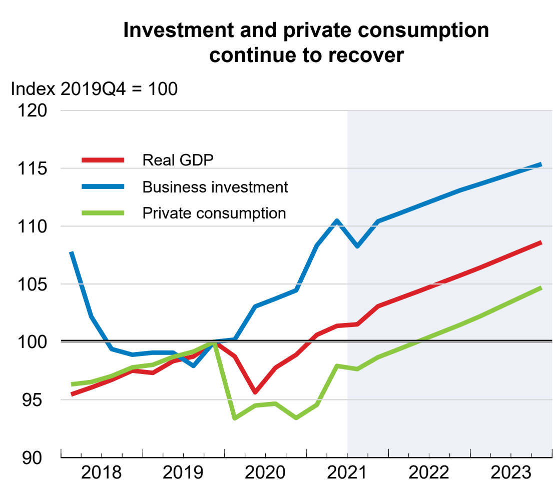
The Korean economy continues to recover following the COVID-19 shock, propelled by strong export growth, improving business investment and public support. Growth is set to reach 4% in 2021 and to remain robust in 2022 and 2023, averaging close to 3%. While distancing measures have weighed on the service sector over the past summer, rapid vaccination paves the way for an acceleration in private consumption.

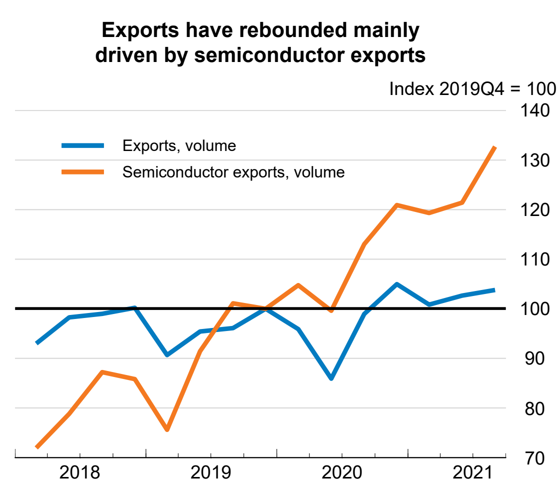
The Bank of Korea has started to normalise monetary policy to address rising inflation and high and rising household debt. Fiscal support should continue, notably to low-income households and businesses hard-hit by the pandemic, until the recovery is well under way. Relatively low public debt leaves room for continued fiscal support, but prioritising spending is important given the need to address rapid population ageing and climate change and reduce income inequality in line with the New Deal initiatives.

Rapid vaccination set the stage to ease restrictions

Strict distancing measures to contain the spread of the Delta variant, notably in the greater Seoul area, have been in place since July, holding back the recovery of customer-facing services and constraining third-quarter growth. However, following a rapid vaccination campaign, close to 83% of the total population had received their first shots and around 80% had been fully vaccinated by 25 November. This is enabling a phased easing of restrictions on business operations and private gatherings. Exports and business investment have been strong this year owing to soaring global demand, notably for semiconductors, and employment is rising. Job recovery in in-person services has lagged behind but is expected to rebound as distancing measures are lifted. The annual rate of headline consumer price inflation rose to 3.2% in October, and core inflation, excluding food and energy, reached 2.4%.

Korea





Source: OECD Economic Outlook 110 database; and Bank of Korea.

StatLink https://stat.link/31br9v

Korea: Demand, output and prices

Korea	2018	2019	2020	2021	2022	2023
	Current prices KRW trillion	Percentage changes, volume (2015 prices)				
GDP at market prices	1 898.2	2.2	-0.9	4.0	3.0	2.7
Private consumption	911.6	2.1	-5.0	3.4	3.3	3.0
Government consumption	304.7	6.4	5.0	5.5	4.3	3.2
Gross fixed capital formation	576.6	-2.1	2.6	2.6	2.0	2.2
Final domestic demand	1 792.9	1.5	-0.8	3.5	3.1	2.8
Stockbuilding[1]	21.1	0.0	-0.6	-0.3	0.1	0.0
Total domestic demand	1 814.0	1.5	-1.5	3.3	3.1	2.8
Exports of goods and services	791.8	0.2	-1.8	8.5	2.1	2.2
Imports of goods and services	707.6	-1.9	-3.3	7.5	2.4	2.4
Net exports[1]	84.2	0.8	0.5	0.7	0.0	0.0
Memorandum items						
GDP deflator	_	-0.8	1.3	2.0	1.4	0.8
Consumer price index	_	0.4	0.5	2.4	2.1	1.5
Core inflation index[2]	_	0.7	0.4	1.3	1.9	1.5
Unemployment rate (% of labour force)	_	3.8	4.0	3.6	3.1	3.1
Household saving ratio, net (% of disposable income)	_	8.1	14.1	12.0	9.9	8.2
General government financial balance (% of GDP)	_	1.0	-2.3	-2.9	-2.5	-2.1
General government gross debt (% of GDP)	_	44.2	45.4	47.8	49.2	52.6
Current account balance (% of GDP)	_	3.6	4.5	5.0	4.4	4.3

1. Contributions to changes in real GDP, actual amount in the first column.
2. Consumer price index excluding food and energy.
Source: OECD Economic Outlook 110 database.

StatLink https://stat.link/1rynfb

Monetary policy normalisation has begun, while fiscal policy remains supportive

Expansionary fiscal policy continues to support the economy. The government has introduced two sizeable supplementary budgets totalling about KRW 50 trillion (2.6% of annual GDP) this year, with programmes including cash relief as well as job creation and retention schemes. The 2022 budget spending proposal of KRW 604 trillion entails an 8.3% increase compared to the 2021 original budget. The government allocated KRW 12 trillion to reduce greenhouse gas emissions and respond to the climate crisis in the 2022 budget as a step towards Korea's 2050 net zero target. The general government deficit is projected to reach around 3% of GDP in 2021 and 2.5% of GDP in 2022, and gross general government debt is expected to rise to about 52% of GDP by 2023.

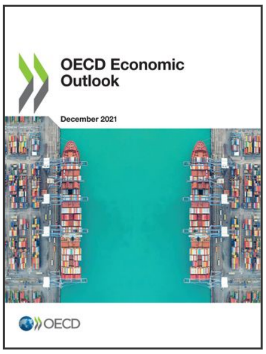
The Bank of Korea raised its policy rate by 25 basis points to 1% in November, following a similar increase in August, to contain rising inflation and household debt, and has signalled further increases. Nominal wages were up over 4% in the first half of this year but this mainly reflects a low base effect from last year.

Economic growth is expected to be stable through 2023

After a rebound of 4% in 2021, real GDP is projected to grow by 3% in 2022 and 2.7% in 2023. A gradual relaxation of distancing measures and supportive fiscal policy will boost private consumption and employment, notably in the service sector. Export growth is projected to remain robust through 2023 on the back of strong global demand for major items such as IT products, machinery and petrochemicals. However, supply bottlenecks and shortages causing delivery delays are likely to continue to hamper exports of some products. Business investment is set for solid growth, owing to strong demand for Korean products and planned government spending on key industries such as semiconductors, batteries and vaccines. Rising house prices and the build-up of household debt raise financial stability concerns.

Public support remains needed for economic recovery and sustainable growth

Fiscal support to households and companies particularly affected by the pandemic should remain in place until the economy has fully recovered. However, it should become more targeted and help facilitate job transitions. As the economy recovers, public investment should focus on accelerating digitalisation, greening the economy and reducing social inequality in line with the New Deal's orientations. In the process, it will be important to encourage the restructuring of companies and to spend more on vocational education and training for employees and youth. Monetary policy should look through the transient components of the ongoing inflation spike but become less accommodative over time. Stronger prudential policy may be needed if household debt does not level off. Meanwhile, efforts should be stepped up to supply more housing with a view to stabilising housing prices.



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