

South Korea Business Forecast Report Q2 2014

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Abstracts

Core Views

While we remain relatively constructive on South Korea's economic growth in 2014, as we expect real GDP growth to accelerate to 3.0% from 2.8% in 2013, our forecasts are fairly below consensus. We highlight growing risks from corporate Korea as an increasing number of chaebols, particularly within the construction sector, are succumbing to the prolonged slump in the domestic real estate sector.

Additionally, a slowdown in China's economy, and the ensuing drag on the Korean economy, is very much on the cards. While the prescribed targets laid out in South Korean President Park Geun-hye's economic reform plan may appear overly ambitious, the proposed drive towards deregulation and support of the services sector, if realised, will provide the Korean economy with new pillars of economic growth and set the country on a more sustainable path of economic expansion. Also, the planned pullback the public sector's involvement in the economy will aid not just in growth of the private sector, but also help to improve the government's fiscal profile.

We are not particularly sanguine towards the Korean won's performance in 2014. We are forecasting the unit to average KRW1,120/ US\$ through 2014 before ending the year at KRW1,150/US\$. Not only do we envision a weaker macro outlook in the coming year, but we also believe the strength in the currency is likely to reverse course as the relative attractiveness of other regional currencies that took a beating in the previous months start to gain traction once again. President Park Geun-hye's push to increase the country's global free-trade agreement share is largely a positive for the country. An expansion in trade volumes and increased investment will provide strong support for Korean exporters, even as Seoul attempts to carve out a more consumption-driven economy. We believe that tighter economic relations between North East Asian countries would also help foster a more stable political environment.

Key Risks To Outlook

Downside Risks To Economic Growth Forecast: Should we see a sharper-than-expected downturn in the global economy or even an implosion in South Korea's household debt market, we would certainly expect to see a substantial weakening in its exports sector, which, in turn may push the economy into a pronounced recession.

Downside Risks To Monetary Policy Forecast: In the event that the economy worsens beyond expectations, while deflationary concerns come to the fore, the central bank is likely to enact a more aggressive monetary stance.

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South Korean President Park Geun-hye's push to increase the country's global free trade agreement share is largely a positive for the country. An expansion in trade volumes and increased investment will provide strong support for Korean exporters, even as Seoul attempts to carve out a more consumption-driven economy. We believe that tighter economic relations between North East Asian countries would also help foster a more stable political environment.

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South Korea is likely to see a renewed push for constitutional change in order to address imbalances in the political system that lead to periodic instability. In addition, owing to the single-term restriction on the presidency, most presidents typically become 'lame ducks' well before departing office, leaving the country in a state of drift.

CHAPTER 2: ECONOMIC OUTLOOK

SWOT Analysis
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While we remain relatively constructive on South Korea's economic growth in 2014, as we expect real GDP growth to accelerate to 3.0% from 2.8% in 2013, our forecasts are fairly below consensus. We highlight growing risks from corporate Korea as an increasing number of chaebols, particularly within the construction sector, are succumbing to the prolonged slump in the domestic real estate sector. Additionally, a slowdown in China's economy, and the ensuing drag on the Korean economy, is very much on the cards.

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While the prescribed targets laid out in South Korean President Park Geun-hye's economic reform plan may appear overly ambitious, the proposed drive towards deregulation and support of the services sector, if realised, will provide the Korean economy with new pillars of economic growth and set the country on a more sustainable path of economic expansion. Also, the planned pullback the public sector's involvement in the economy will aid not just in growth of the private sector, but also help to improve the government's fiscal profile.

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We are not particularly sanguine towards the Korean won's performance in 2014. We are forecasting the unit to average KRW1,120/US\$ through 2014 before ending the year at KRW1,150/US\$. Not only do we envision a weaker macro outlook in the coming year, but we also believe the strength in the currency is likely to reverse course as the relative attractiveness of other regional currencies that took a beating in the previous months start to gain traction once again.

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