

The Response to the Global Financial Crisis of and Future Prospects for the ROK

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Summary

The global financial crisis, due to the Lehman shock of September 2008, has affected the ROK, causing a downturn in the economy and a sharp drop in the ROK won. For the October-December 2008 quarter the ROK's real GDP annualized growth rate amounted to -18.9%, a sizeable negative growth. The won-US dollar rate was close to 900 won to the US dollar in 2007, but the won suffered a sharp drop in August 2008, and by 24 November the rate was 1,509 won to the US dollar. With the ROK confronted with a currency crisis in 1997, an external financial crisis wrought a fallback in the domestic economy, and ultimately, with the won's plunge in value, the ROK was forced to rely on aid from the IMF. The circumstances that have arisen in this global financial crisis bear similarity to those of 1997—a domestic economy in recession and a sharp drop in the currency—and some voices have expressed concern over the ROK falling into another currency crisis.

As such trends will accelerate in the future, however, the probability that a currency crisis like that seen in 1997 may happen again is low. The reasons for this are two-fold: 1) since the Asian financial crisis, the ROK economy has transformed into one with a sound structure, and the risk of the corporate and financial sectors becoming unstable from an external "negative shock" has become low; and 2) due to improvements in the financial environment having been put in place to avoid another currency crisis, the country has been able to grow robust for the interim, even with foreign financial institutions suddenly recovering funds from the ROK. Since the currency crisis the ROK has implemented restructuring reforms in the financial and corporate sectors; this has enabled the country to bring under control all three of the vulnerabilities that it had had: those in its financial sector, corporate sector, and international balance of payments. Moreover, while the foreign exchange reserves were also at an insufficient level—including the short-term external debt being just 43.8% at the end of 1996—since the crisis, due to the current account surplus and excess capital balance inflow having continued, they have consistently increased overall. In addition, emergency provisions have also been readied, such as the conclusion of currency swaps.

In comparison to the situation the ROK faced in the Asian currency crisis, the present global economic climate surrounding the ROK economy could be said to be harsher. Consequently, if the ROK hadn't undertaken structural reforms and improved the constitution of the economy following the Asian financial crisis, the probability is high that a financial crisis would have arisen this time around. By virtue of the qualitative improvement of the structure of the economy accompanying the reforms, however, the ROK currently has no need to turn to the IMF for financial aid. Looking at the trends in the international economy for the near future, it is not possible to dismiss outright the possibility that the ROK might fall once again into a currency crisis. Given the forecast for the global economy at this point in time, however, it would be reasonable to conclude that the possibility of that is low.

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