

# CareEdge Global assigns Long Term Foreign Currency Rating of AA- (Unsolicited) to Republic of Korea

## Credit Profile

Korea's credit profile is underpinned by its strong external position, supported by its globally competitive industries. The country performs well in monetary and financial stability and has sound government finances, characterized by low government debt and strong debt affordability. The quality of its institutions and governance is also strong.

However, these strengths are partly offset by Korea's elevated private debt levels, stemming from significant household debt, as well as geopolitical tensions with North Korea, which undermine national security. Additionally, Korea's ageing population presents a structural challenge to its credit profile.

## Strengths

- Strong external position
- Sound government finances
- Strong institutions

## Weaknesses

- Elevated private debt, which stems from high household debt
- Ageing population
- Geopolitical risks from North Korea

## Key Monitorables

- Rising delinquencies particularly in real estate project finance loans to assess their implications for financial stability
- Effectiveness of government policies to manage economic and fiscal impact of an ageing population

## Key Rating Drivers

### Economic Structure & Resilience

Korea is a large economy with an economic size of USD 1.7 trillion in 2023 and a high per capita income of USD 46250 (constant PPP terms). Its globally competitive industries, such as electronics and semiconductors, are key contributors to growth but also expose the country to fluctuations in global markets.

Korea's economic growth slowed from 4.3% in 2021 to 2.6% in 2022 and 1.4% in 2023. This decline was mainly due to a slowdown in the semiconductor industry and higher interest rates, which resulted in a subsequent decline in consumption, investment and property sector activity. However, the country's economic outlook has improved, with GDP growth forecasted at 2.3% in 2024, driven by increased exports

amidst a recovery in the semiconductor industry.

Structurally, Korea is an aged society, with ~18% of its population aged 65 and above (2023). It is projected to have the highest share of elderly population among the OECD nations by 2046. This demographic shift poses structural headwinds to Korea's economic growth if sufficient measures are not taken to address the issue.

### **Fiscal Strength**

Korea's gross general government debt to GDP ratio increased substantially by ~13 percentage points between 2019 and 2023. However, its debt levels remain low at ~55% of GDP (2023). Debt affordability is strong, with interest expenses accounting for only ~3% of government revenues. Further, Korea's low external government debt, at ~18% of total government debt (2023), mitigates its vulnerability to exchange rate fluctuations and reduces risks from debt servicing perspective.

However, potential challenges exist due to contingent liabilities related to the non-financial public sector. Additionally, geopolitical risks from North Korea necessitate substantial military spending, estimated at ~11% of general government expenditure, which diverts resources from other policy priorities.

The fiscal implications of Korea's ageing population also require close monitoring as the rapid rise in the share of the elderly population could strain government finances. Currently, the government's committed expenditure is already high, with spending on pensions, salaries and subsidies accounting for ~40% of total general government expenditure.

### **External Position & Linkages**

Korea is highly reliant on exports, which account for approximately 44% of GDP (2023), and has consistently recorded current account surpluses. However, its current account surplus narrowed to 1.5% of GDP in 2022 from 4.7% in 2021, primarily due to a slowdown in the semiconductor industry and rising energy import costs. Nevertheless, the current account surplus rebounded to 2.1% in 2023 and is projected to average 3.7% between 2024 and 2028.

The country has low external debt, averaging ~35% of GDP between 2019-2023. Korea also holds sizeable foreign exchange reserves of about USD 416 billion (as of August 2024), sufficient to cover 6-7 months of imports. Additionally, Korea's large and positive net international investment position, at ~47% of GDP in 2023, adds to its external strength. However, the export-driven nature of the economy makes Korea susceptible to global shocks and a potential slowdown in key trading partners, like China and US, could pose near-term risks to its external profile.

### **Monetary & Financial Stability**

Korea has a floating exchange rate and its currency is actively traded. The Bank of Korea (BoK) prioritizes price stability and has raised the policy rate by 300bps in the current tightening cycle. As a result, inflation has fallen to 2% in August 2024 from its peak of 6.3% in July 2022, aligning with the BoK's target and raising expectations for potential rate cuts.

However, Korea's private debt levels are very high, at ~225% of GDP in 2022, posing financial stability risks. Household debt, which stands at 105% of GDP as of 2022, is among the highest in the OECD. While non-performing loans remain low, delinquency rates have increased due to higher interest rates and a subdued property market. Nonbank financial institutions are seeing more pronounced asset quality deterioration, particularly with increasing delinquency rates in real estate project finance loans. However, overall capital adequacy ratios of financial institutions remain above regulatory requirements. Additionally, stress tests conducted by the BoK indicate that these ratios will generally remain above regulatory standards even under macroeconomic shocks. Nonetheless, some vulnerable nonbank deposit-taking institutions may see significant deterioration in health. However, defaults among these institutions are unlikely to trigger systemic shocks, given their small share and low interconnectedness with the rest of the financial system. Still, the situation requires close monitoring.

### **Institutions & Quality of Governance**

Korea's governance strength is reflected in its high percentile rankings across the Worldwide Governance Indicators. However, the Legoland default in 2022 raised institutional concerns - when Gangwon's governor initially refused to honour a debt guarantee. Nonetheless, the government's swift response, which included various market stabilization measures, helped restore market confidence.

Korea faces external security threats from North Korea. While missile testing by North Korea has intensified in recent years, the risk of this escalating into a serious conflict remains low for now. Still, the situation warrants vigilance. To bolster its defense capabilities, Korea has been strengthening military ties with the US.

The April 2024 National Assembly (NA) elections yielded a status quo outcome, with the opposition, led by the Democratic Party of Korea (DPK), retaining majority control in the NA. This may pose challenges for Korea's President, Yoon Suk Yeol from the People Power Party (PPP), in advancing policies and reforms smoothly. However, the opposition failed to secure a two-thirds majority, which is required to override presidential vetoes and approve impeachment proceedings.

Korea – Select Indicators									
	Unit	2018	2019	2020	2021	2022	2023	2024 F	2025 F
<b>Economic Indicators</b>									
Nominal GDP	USD Billion	1725	1651	1645	1818	1674	1713	1761	1843
GDP Per Capita (Constant-PPP)	USD	42011	42804	42442	44326	45569	46250	47379	48534
Real GDP Growth	%	2.9	2.2	-0.7	4.3	2.6	1.4	2.3	2.3
GFCF/GDP	%	30.4	30.1	31.3	31.6	32.2	32.2	-	-
Gross Domestic Savings/GDP	%	35.9	34.3	35.6	35.9	33.2	32.2	-	-
Exports (G&S)/GDP	%	41.7	39.3	36.4	41.9	48.3	44.0	-	-
Working-Age (15-64) Population (% Share in Total)	%	72.8	72.5	72.0	71.5	70.9	70.4	69.8	69.0
Old-Age (65+) Population (% Share in Total)	%	14.5	15.1	15.8	16.7	17.5	18.4	19.3	20.3
<b>Fiscal Indicators – General Government</b>									
Fiscal Balance/GDP	%	2.6	0.4	-2.2	0.0	-1.6	-1.0	-0.6	0.1
Revenue/GDP	%	22.9	22.9	22.9	25.7	27.1	23.9	23.9	24.4
Expenditure/GDP	%	20.4	22.6	25.1	25.7	28.7	24.9	24.5	24.3
GG Gross Debt/GDP	%	40.0	42.1	48.7	51.3	53.8	55.2	56.6	57.3
GG External Debt (by Creditor)/GG Gross Debt	%	12.2	13.3	15.2	15.7	17.5	18.2	-	-
Interest/Revenue	%	3.2	3.2	3.3	2.9	3.1	-	-	-
<b>External Indicators</b>									
Current Account Balance/GDP	%	4.5	3.6	4.6	4.7	1.5	2.1	2.9	3.4
FDI, Net Inflows/GDP	%	0.7	0.6	0.5	1.2	1.5	0.9	-	-
Outstanding FII Liabilities/GDP	%	38.6	44.9	59.3	54.7	48.5	55.6	-	-
NIIP/GDP	%	25.3	31.4	29.6	37.7	47.8	47.3	-	-
Foreign Exchange Reserves	USD Billion	403.7	408.8	443.1	463.1	423.2	420.1	-	-
Import Cover	Months	7.5	8.1	9.8	8.0	6.2	6.6	-	-
External Debt/GDP	%	25.6	28.5	33.5	34.7	39.7	38.7	-	-
<b>Monetary and Financial Indicators</b>									
CPI Inflation	%	1.5	0.4	0.5	2.5	5.1	3.6	2.5	2.0
Exchange Rate (Average)	LC per USD	1100.7	1166.3	1179.4	1145.5	1293.0	1306.9	-	-
Non-Performing Loans/Total Gross Loans	%	0.3	0.3	0.2	0.2	0.2	0.3	-	-
Private debt, loans and debt securities/GDP	%	187.4	196.2	212.8	219.5	224.7	-	-	-

Sources: International Monetary Fund, World Bank, Bank for International Settlements, National Sources, CareEdge Global

Note: F - Forecast; PPP – Purchasing Power Parity; GFCF – Gross Fixed Capital Formation; Exports (G&S) – Exports of Goods and Services; GG – General Government; FDI – Foreign Direct Investment; FII – Foreign Institutional Investment; NIIP – Net International Investment Position; Data refers to fiscal/calendar year and actual/estimate as reported by the source; Where general government data is unavailable, central government data is used; Latest available data for 2023

## Rating History

Instrument	Type	Rating	Date
Issuer Rating	Long Term Foreign Currency (Unsolicited)	AA-	October 3, 2024

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## Criteria Applied

CareEdge Sovereign Rating Methodology

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