

Korean 2020 budget

South Korea's budget for 2020 includes an increase in government spending of 9.3%.



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9.3% Increase in government spending

A net boost of about 2.2% GDP

"As expansionary as possible"

Finance Minister, Hong Nam-ki, has described the 2020 budget as being "as expansionary as possible". Perhaps a more literal translation would be "as expansionary as feasible", since clearly, more could have been done.

But the 9.3% increase in government spending is impressive, and even though this is whittled down in its effectiveness by some revenue increases from tax measures, that still leaves a net expansion of government spending of some KRW42tr, or about 2.2% of GDP.

As far as fiscal thrust goes, I'd have to say that this is pretty good, though critics point to Korea's debt-to-GDP ratio, which is now forecast to rise to 39.8% and argue that with such an enviably low

debt ratio, the government should have done more.

This is probably not the final story

Such criticisms are somewhat harsh, in our view. Korea is facing what is undoubtedly one of the most negative cyclical backdrops for some time - a combination of a global technology slump in demand (volumes) and prices, exacerbated by the global downturn in trade, amplified regionally by the US-China trade and technology war.

The local spat between Japan and South Korea over war-time events doesn't help and is ill-timed, and the lingering economic weakness in both economies is no doubt a catalyst fueling this argument. It is hard to see a circuit-breaker to this barring outside intervention (the US?).

In any case, some more positive signs of a bottoming in the electronics cycle are becoming evident, and if so, further fiscal stimulus may not be necessary. If, however, this turns out to be a false dawn, then indeed, more will be needed. Today's budget does not preclude a further stimulus package later, and a supplementary budget can be forthcoming if necessary once the situation is more clear.

Budget detail

From what we can gather from newswire headlines, until a more detailed breakdown appears on the Finance Ministry website, the current budget aims to increase South Korean self-reliance in materials/parts, which sounds like a response to the loss of Japanese "whitelisting", and could be viewed as a deadweight loss of the ongoing argument.

But spending on automated "smart factories" sounds like a positive supply-side measure, though begs the side-question of how it helps to boost employment and wages..?

As for the debt-to-GDP ratio, such a low ratio is a rare asset these days, and should not be rashly traded away for a few years of debt-fuelled and unsustainable growth. South Korea is wise to tread with some caution. This won't be the only year when the Finance Ministry is asked to pull a rabbit out of a hat, so it makes sense to tread carefully with this finite resource.

Bank of Korea probably on hold

The Bank of Korea decides whether to follow up the July 25bp rate cut tomorrow with a further cut. We don't think they will. For one thing, this budget measure does some of their stimulus work for them. But mainly, we suspect they will want to see which way the Fed moves in September before committing to a further cut. We expect one further 25bp rate cut from the BoK in 4Q19.

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