

## Press Release

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Creative Finance  
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### CHINA'S ECONOMIC SLOWDOWN AND ITS IMPACT ON KOREA'S ECONOMY

#### CHINA'S 'NEW NORMAL'

The IMF recently downgraded China's economic growth forecast in 2015 and 2016 to 6.8% and 6.3% respectively, slower than the stable growth of 7% in three years since 2012. The growth rate of around 6% is still high, given the size of China's GDP; however, the actual impact of such slowdown from 7% to 6% could be felt far more profound.

China's slowdown is attributed to excessive and inefficient investments by its massive economic stimulus plan. Inventory adjustments and deleveraging will weigh on China's economy for a considerable period of time. It will be difficult to resolve oversupply in property market in a short period.

To manage a soft landing of Chinese economy, the Chinese government set out a new economic model, so-called '**Xin Chang Tai(新常态, new normal)**' since President Xi Jinping came to power in 2013. The new growth model is aimed to shift Chinese economy from export-driven rapid growth to consumption-led stable growth. It also includes structural reform, diversification of growth drivers and liberalization of financial markets.

The effectiveness of the Chinese government's stimulus plan to downward pressure is key to a soft landing of Chinese economy as it would take time for structural reform to achieve results. The Chinese government still has capability to prevent a hard landing of Chinese economy. However, emerging economies also need to be prepared in response to the spill-over effect of China's new normal.

#### IMPACT ON KOREA'S FINANCIAL MARKET

There is a possibility that volatility might increase due to worries over China's economic slowdown and potential spill-over effects of its structural reform.

However, market participants view that it is unlikely for Chinese slowdown to cause a serious financial crisis. Since the 2008 global financial crisis, Korea's economic fundamentals have been steadily improved. Its current surplus has grown to USD 89.2 billion in 2014 from USD 3.2 billion in 2008; its foreign currency reserve has increased from USD 201.5 billion in 2008 to USD 370.8 billion in July 2015; and its short-term foreign debt ratio out of its total foreign reserve has decreased from 73.9% in 2008 to 30.8% in July 2015.

## **IMPACT ON KOREA'S REAL ECONOMY**

China's slowdown and structural reform will basically act as downside risks to Korea's economy. In the short-term, China's domestic consumption will fall due to economic slowdown, which will eventually result in a drop in Korea's export to China. In the mid to long-term, if we aren't well prepared for China's shift to new growth model, no matter it succeeds or fails, Korea's economy will be faced with significant threats.

## **IMPLICATIONS FOR POLICY RESPONSE**

The government should strengthen its monitoring and take preemptive measures to prevent external risk factors such as China's slowdown and US interest rate hike from spilling over into the Korean economy and financial markets. To this end, the FSC will make sure the structure of household debt should be more stable with a greater share of fixed, amortized loans. We will also strengthen monitoring of corporate debt and enable a market-driven corporate restructuring by establishing a specialized company for corporate restructuring. The government will continue to stimulate more demand and improve market infrastructure to stabilize stock markets.

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