GREEN/20/17

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Green Statement from Mr. Sigurgeirsson and Mr. Evjen on the Republic of Korea - Financial System Stability Assessment (SM/20/65)

We thank staff for the comprehensive report and Messrs. Heo, Shin, and Yoo for their informative Buff statement and appreciate the overview of the range of sweeping measures taken by the authorities to limit contagion and to mitigate the economic impact of the coronavirus. The Korean financial system is one of the largest and most developed in Asia. On the back of robust economic growth, new regulations, and continued state presence, most parts of the banking system are prudentially strong. However, challenges remain, such as elevated household debt, an adverse demographic shift, a lower growth and interest rate environment, shortcomings in the oversight of financial conglomerates, and fintech developments. We broadly share staff´s assessment and would like to offer the following remarks.

Elevated household debt and growing balance sheet vulnerabilities pose a risk to financial stability. We note staff's assessment that the overall financial system appears resilient for the present. However, vulnerabilities and growth-related uncertainties remain. Household lending growth, primarily related to housing, has slowed but the household debt ratio of disposable income stands at about 180 percent, among the highest in OECD countries. Household leverage in the real estate sector remains high. Large sections of the financial sector are exposed to the housing market and household debt.

Korea has demonstrated a strong willingness to act on household sector risks. Many macroprudential and other measures have been taken to curb house prices and credit growth. We commend the authorities for implementing conservative borrower based prudential measures, such as restrictions on loan-to-value, which have reduced the near-term risk of sharp house price corrections We note that there appears to be signs of overvaluation of house prices in the Seoul area.

An overarching macroprudential strategy should be developed. We note that no entity has sole responsibility for financial stability. We agree with staff that when multiple agencies have multiple primary objectives, the result could be delays in taking measures and lack of accountability. Hence, we encourage the authorities to consider whether a clearer delineation of responsibilities is needed and assigning a body (for example MEFM) macroprudential oversight as its sole primary objective. Moreover, a macroprudential strategy would take account of the complementarities between different policy measures, i.e. both borrower-based and lender-based measures (e.g. the countercyclical buffer). Such strategy could also ensure consistency over time in policy implementation and enhance accountability.

Oversight of financial conglomerates should be enhanced. Supervision should have a legal mandate to regulate financial conglomerates which do not have a straight-forward holding structure. While capital requirements apply at the holding company level, liquidity requirements currently only apply at banks and other financial subsidiaries. We agree that this is a gap in supervision that should be addressed given the growth of non-banking activities within systemically important banks banking groups.