GREEN/20/22

March 24, 2020

Green Statement from Ms. Levonian and Ms. Vasishtha on the Republic of Korea—Financial System Stability Assessment (SM/20/65)

We thank staff for a well-written report and Messrs. Heo, Shin, and Yoo for their informative Buff statement, which provides a very timely update on the COVID-19 situation in Korea. We wish to express our deepest condolences to the people of Korea for the tragic loss of lives in the wake of the COVID-19 outbreak. We commend the authorities for their swift implementation of a range of fiscal, monetary, and other policy measures to mitigate the impact of the pandemic.

The Korean authorities have implemented significant policy measures since the 2013 FSAP and the financial system has remained relatively stable. We welcome the authorities' continued efforts at upgrading the supervisory, legal and prudential frameworks for the financial sector, strengthening the crisis management framework, and keeping pace with international standards and practices in other G20 jurisdictions. Banks and insurers, in aggregate, appear to be resilient to severe macro-financial shocks. Nevertheless, vulnerabilities remain in the form of elevated household debt and uncertainty around growth prospects. As well, the incidence of COVID-19 cases is expected to exert a significant drag on economic and financial activity, although the government's proactive policy responses should tamper some of the fallout. We broadly concur with the thrust of the staff appraisal and offer the following remarks for emphasis.

We note the staff and authorities' view that the macroprudential framework has been working well. We also welcome staff's acknowledgement that there is no "one-size-fits-all" approach for countries when it comes to macroprudential frameworks. An effective macroprudential oversight framework hinges upon agencies having clear mandates, a clear shared perspective on meeting their objectives, and engaging cooperatively with their counterparts. Korea's multi-agency system for macroprudential oversight has served it well through close coordination and cooperation among the various agencies. Nevertheless, we support staff's suggestion to further strengthen the framework by establishing macroprudential oversight at the primary objective of the existing Macroeconomic and Finance Meeting (MEFM) – an agency responsible for coordinating assessments of systemic risks and financial policy interventions.

Elevated household debt and growing household balance sheet vulnerabilities pose significant risks to financial stability. The level of household debt is among the highest in OECD countries, although proactive macroprudential measures have contributed to a moderation of household debt growth and an improvement in the quality of household loans in recent years. At the same time, household balance sheets have weakened as leverage and debt service ratios have risen. Against this backdrop, we welcome the authorities' strong willingness to tackle household sector risks and would encourage close monitoring of the evolution of household indebtedness, especially for older cohorts given the ongoing demographic shifts.

Finally, the authorities' growing awareness of climate risks is a welcome development. We note positively that Korea has become a large supplier of Environmental, Social, and Governance (ESG) bonds. We also welcome the Bank of Korea's efforts to actively participate in the global discussion on climate and environment-related financial risks, including through its recent participation in the Network for Greening the Financial System (NGFS). We share staff's view that a comprehensive action plan to assess climate and green finance trends as well as stress-testing of climate risks will be valuable.