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THE PENIN

Korea's Economy Slowed in the Third Quarter, but Still on Track for 4.0% Growth in 2021

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Author: [Randall S. Jones](#)

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Korea's real GDP increased 1.2% (saar) in 2021Q3, a significant slowdown from the first two quarters of the year, reflecting a decline in private consumption (table below). A tightening of social distancing measures since July, aimed at slowing a fourth wave of COVID-19 infections, reduced spending on "consumer-facing services". For example, demand in the food and lodging sectors is more than 20% below its January 2020 level. A second

consecutive quarterly decline in gross fixed capital formation was blamed on supply bottlenecks. Net exports accounted for more than half of third-quarter growth as exports rebounded and imports fell in line with domestic demand.

	2019	2020	2020 Q3	2020 Q4	2021 Q1	2021 Q2	2020 Q3
GDP	2.2	-0.9	9.2	4.6	7.1	3.1	1.2
Private consumption	2.1	-5.0	0.7	-5.1	5.0	15.0	-1.1
Government consumption	6.4	5.0	0.6	-1.7	6.5	16.7	4.7
Gross fixed capital formation	-2.1	2.6	-0.3	7.3	10.4	-1.7	-7.5
Construction	-1.7	-0.4	-14.7	14.9	5.4	-8.9	-11.6
Facilities	-6.6	7.1	25.3	-2.5	26.9	4.6	-9.1
Intellectual property	3.1	4.0	3.3	5.5	1.0	5.8	4.1
Final domestic demand	1.5	-0.9	0.3	-0.6	7.0	9.6	-2.1
Stockbuilding ¹	0.0	-0.6	-1.4	-0.4	0.3	0.3	0.1
Total domestic demand	1.5	-1.5	-5.2	-2.2	8.4	10.9	-1.8
Exports of goods and services	0.2	-1.8	82.9	22.9	8.2	-7.6	6.1
Imports of goods and services	-1.9	-3.3	25.9	6.1	12.0	11.9	-2.5
Net exports ¹	0.8	2.0	3.6	1.6	-0.3	-1.8	0.8

1. Contributions to changes in real GDP (percentage of real GDP in previous year). Source: Bank of Korea

Employment has increased significantly during Korea's recovery from the pandemic. The number of people with paid positions in August 2021 was up 2.1% from August 2019 before the pandemic, a gain of 433,490 jobs. More than one-third of these jobs, however, were for less than 17 hours of work per week. The situation is deteriorating for young people. The number of people in the 15 to 29-age group with full-time jobs has fallen 3.7% since August 2019.

Although growth slowed in 2021Q3, the Bank of Korea has maintained its August 2021 projection of 4.0% growth this year. Growth will be sustained by the "living with COVID-19" strategy introduced in November. Under this approach, COVID-19 will be treated as an infectious respiratory disease, such as seasonal influenza, allowing an easing of social distancing rules. The new strategy is made possible by Korea's success in immunizing its population. Immunization started relatively late in Korea; as of May 1, 2021, only 0.5% of the population was fully immunized. By November 9, 2021, the share was one of the highest in the OECD area at 76% (figure below).

The “living with COVID-19” initiative will be carried out in three phases:

Phase 1: restaurants in the Seoul area had a curfew of 10 p.m. (midnight in the rest of the country). As of November 1, curfews are abolished. The government introduced a “vaccine pass” system, which requires a vaccination certificate or a negative test result for entry into entertainment facilities and indoor gyms.

Phase 2: greater attendance at large-scale events, such as concerts and sporting events, will be allowed using the vaccine pass system. At present, professional sports teams in the Seoul area are permitted to have fans fill 30% of capacity, assuming they are vaccinated (20% for indoor facilities). Beginning in mid-December, the ceiling is expected to increase to 75% of capacity.

Phase 3: the restriction on private gatherings, which is currently limited to eight people (on the condition that four are fully vaccinated) will be removed by late January. However, masks will remain mandatory both indoors and out until the last phase.

The relaxation of COVID-19 restrictions is expected to boost private consumption, especially for consumer-facing services. In addition, fiscal policy will continue to support the economy, as two supplementary budgets, totaling about KRW 50 trillion (2.6% of GDP), were launched in 2021. In August, the Bank of Korea became the first Asian central bank to begin normalizing monetary policy by raising its policy interest rate from its record-low of 0.5% to 0.75%. Additional hikes are expected to address inflation, which has surpassed the 2% target, and rising household debt. In June 2021, household debt reached a record high

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of KRW 1.81 trillion, matching Korea's GDP. Despite policies to stabilize household debt and cool the housing market, the relaxation of social distancing measures and fiscal support are likely to support robust growth.

Randall S. Jones is a Non-Resident Fellow at the Korea Economic Institute of America. The views expressed here are the author's alone.

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