

## **Euler Hermes: Beyond MERS, exports remain South Korea's growth driver**

**SEOUL – 24 JULY 2015** – Although household spending and tourist arrival numbers have suffered as a result of the Middle East Respiratory Syndrome (MERS) outbreak, South Korea's export economy shows resilience, finds Euler Hermes, the world leader in trade credit insurance. In real terms, exports will contribute more than half of total GDP growth by 2016, despite headwinds to demand from its largest trading partners.

Economies of scale and pricing power position South Korea well to benefit from greater segmentation of global product supply chains. Its export base is expected to expand by an additional US\$71 billion in 2015 and 2016, i.e. 5.0% of its current GDP.

Important indicators instill confidence in the economy and those businesses trading with South Korean companies. Business insolvencies at the end of 2014 stood at a record low, having decreased by 16% compared to a year earlier. Fiscal policies designed to support home buyers had also boosted investment in the construction sector, signaling an end to the sector's prolonged troubles. Before MERS incidents impaired consumer confidence, domestic consumption was also on an upward trajectory.

Hopes that domestic consumption could play a larger role in the economy have, however, been stifled by public concern surrounding the MERS infections in May and June. Retail sales have taken an immediate hit as consumers began avoiding shops, restaurants and other public spaces. Elevated household debt further weighs on consumer spending.

The government has acted quickly to contain the impact of MERS. A supplemental budget of KRW15 trillion was enacted in early July. With public debt at less than 40% of GDP in 2015, South Korea has the rare luxury of increasing public spending without eroding investor confidence. Acting with equally swift determination, the central bank cut benchmark interest rates to a record low of 1.5% in June.

More than ever, South Korea's economy depends on the agility of the country's export industry. Exporters are confronted with sluggish demand in the US and weaker demand from China. Many industries also face significant challenges as the Korean Won's real effective exchange rate is now more than 10% above its 5-year average, resulting in lower price competitiveness particularly vis-à-vis Japanese peers.

South Korea's exporters thus face tough choices. In order to compensate for their currency's relative strength and win business abroad, many of them may offer more favorable credit terms to buyers. Average days sales outstanding (DSO) have been relatively stable at around 70 days for the past four years, but did witness a slight increase to 71 days in 2014. DSO measures the delay businesses encounter between delivery of their goods to the buyer and receipt of payment for these goods. The longer the delay, the higher the likelihood that businesses further down the supply chain face financial distress or have greater negotiating power at the expense of exporters.

In light of these findings, Fabrice Desnos, head of Euler Hermes Asia Pacific Region, observed: "As delayed payments and even buyer default become more frequent risks or experiences for exporters, corporates should view trade credit insurance as an important financial tool in today's challenging market environment."



More information: <http://www.eulerhermes.com/economic-research/country-reports/Pages/South-Korea.aspx>

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