Fiscal Rule of Korea

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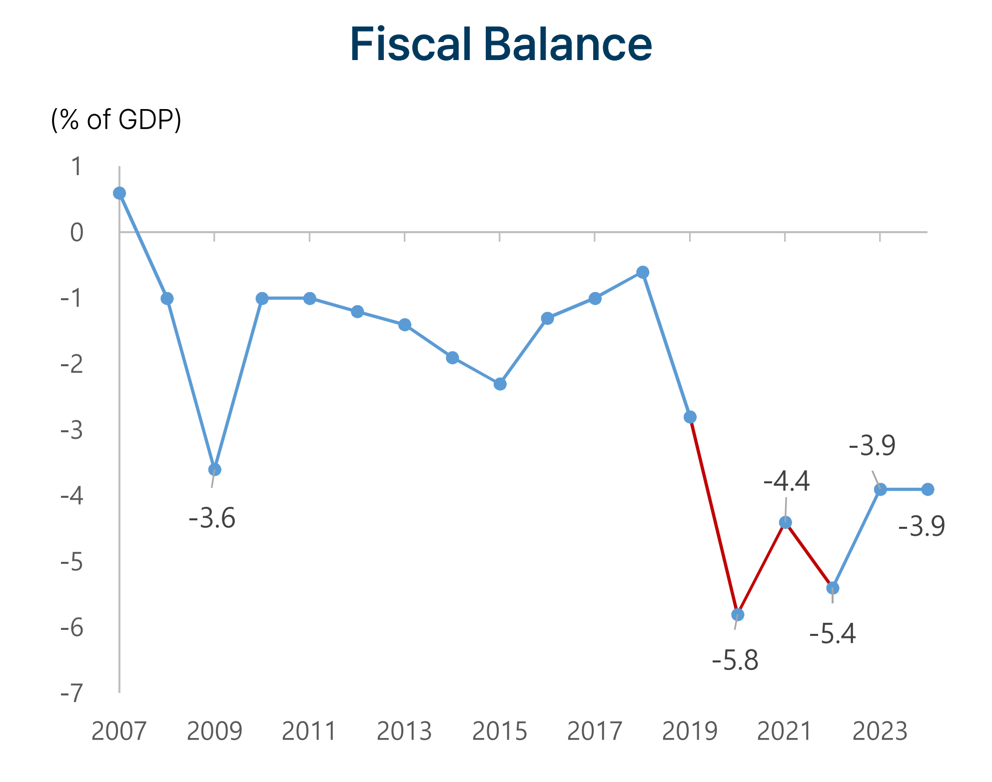
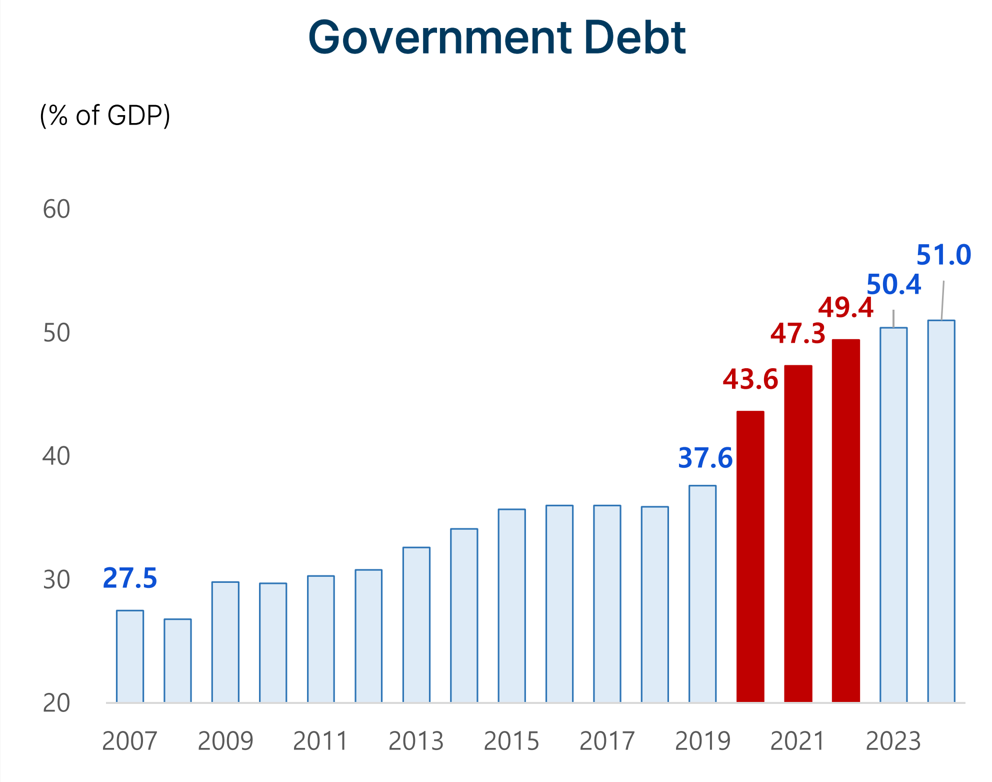
Fiscal Condition: Fiscal Balance and Debt

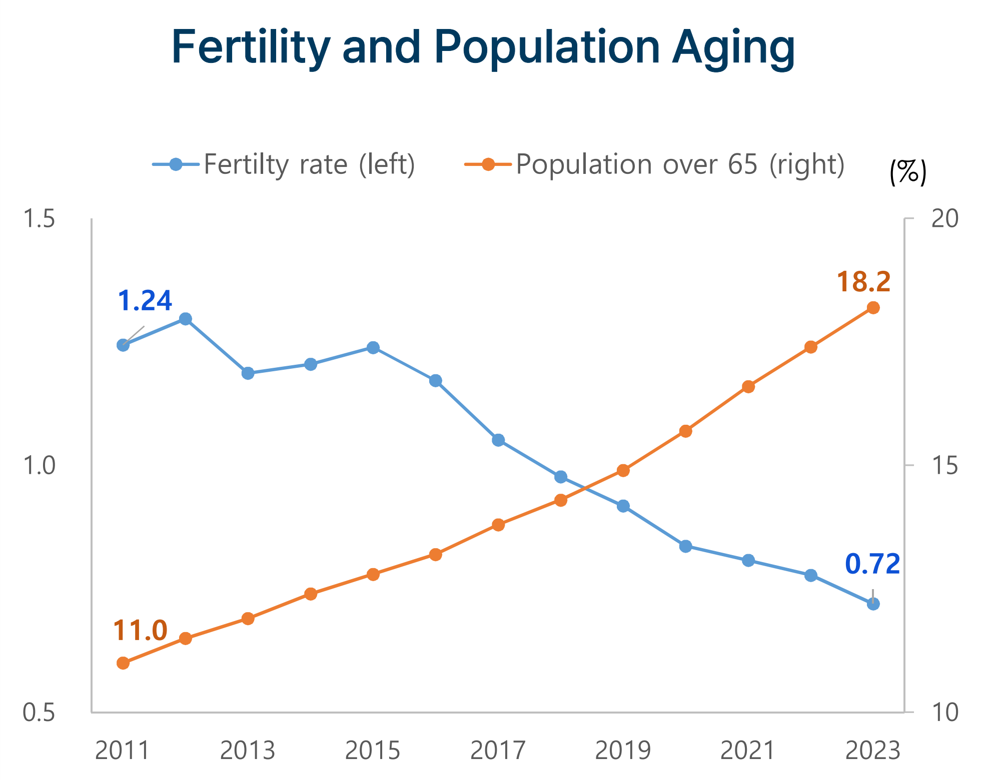
◆ Korea's fiscal balance and government debt have worsened since 2020

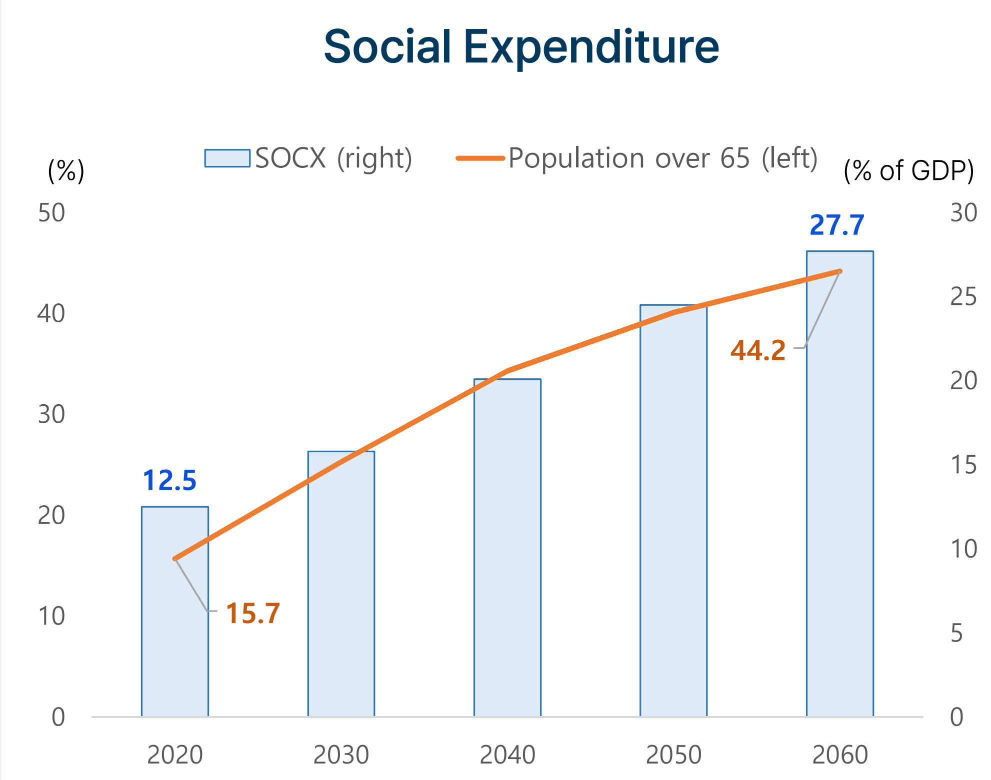




Fiscal Condition: Demographic Headwinds

◆ Rapid aging and rise of SOCX are upcoming challenge to deal with

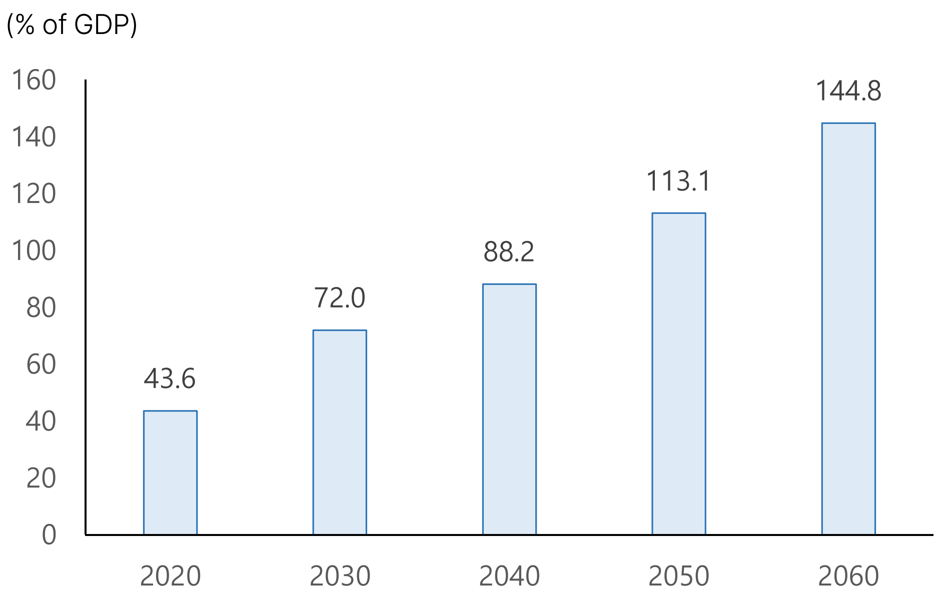




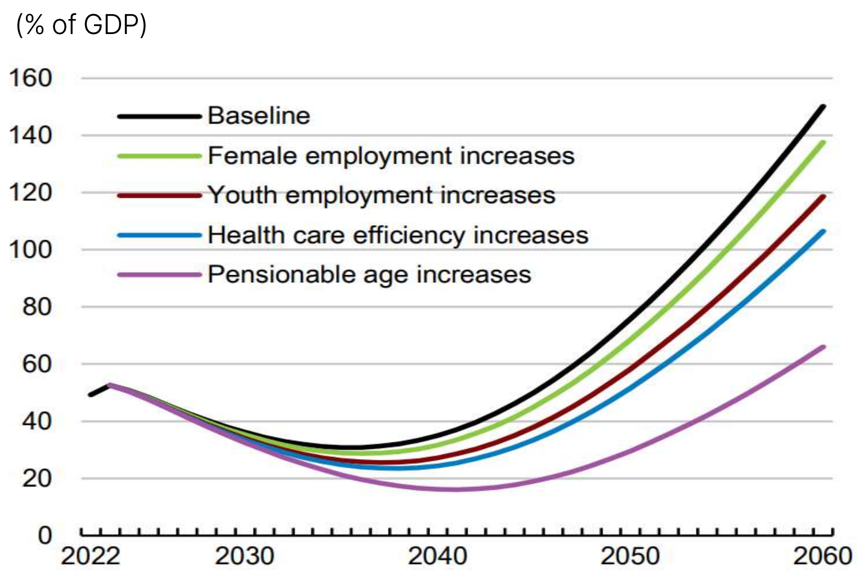
Fiscal Condition: Long-term Fiscal Outlook

◆ Government debt to GDP is projected to exceed 140% in 2060

KDI Outlook



OECD Outlook



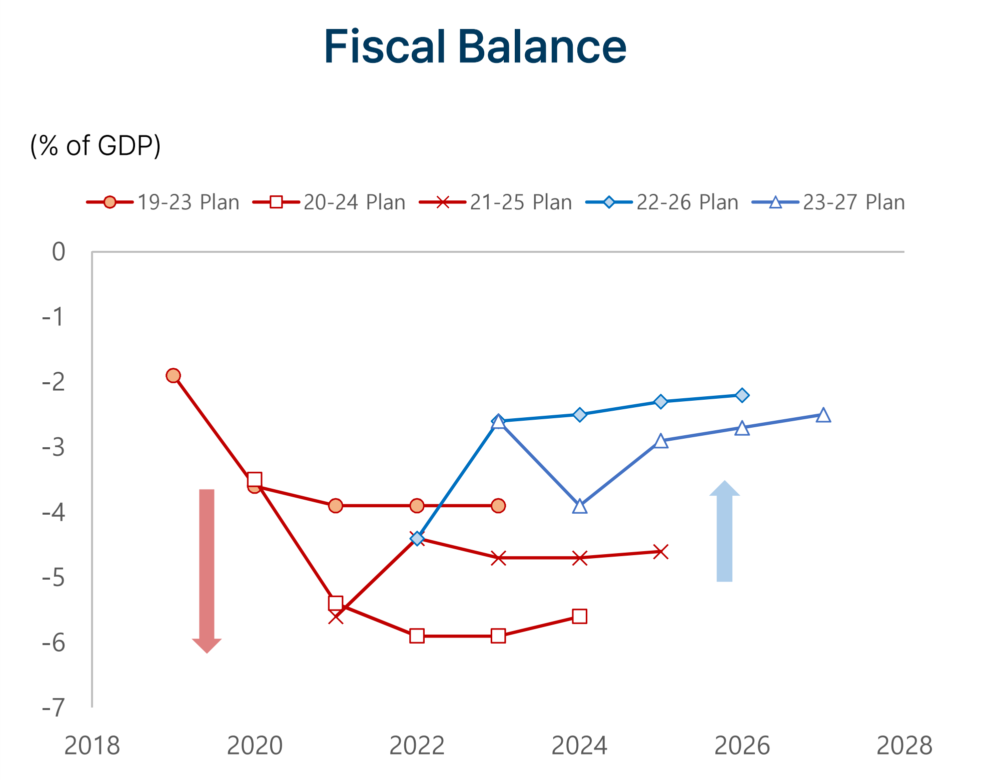
Old Fiscal Framework

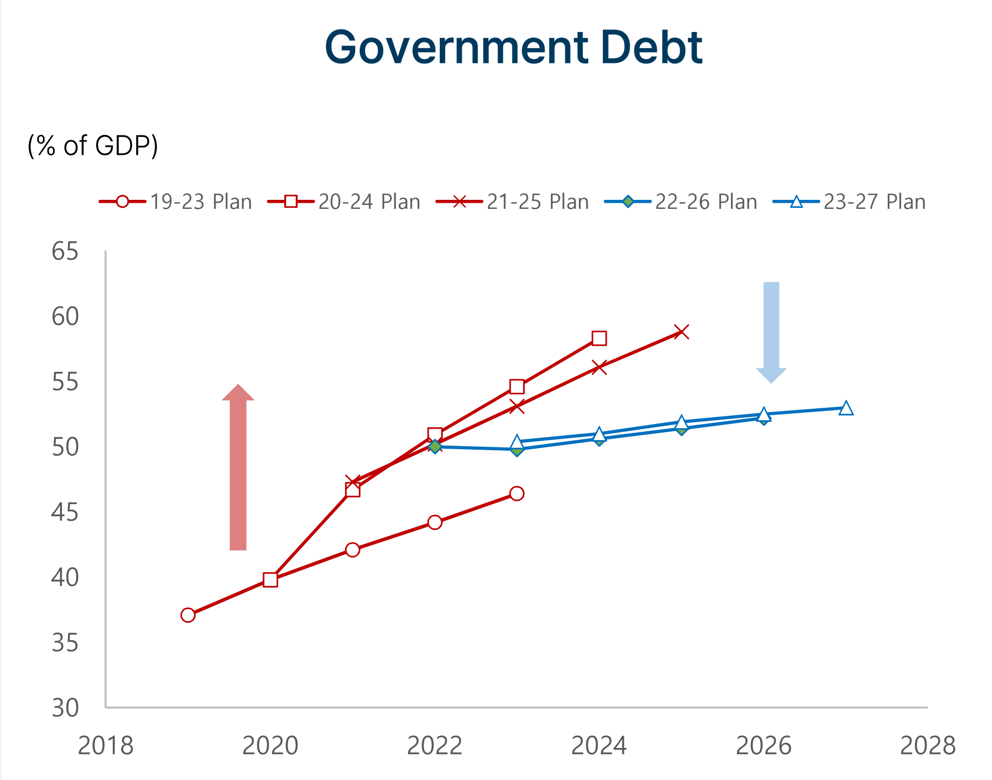
◆ Korea has fiscal frameworks for maintaining fiscal sustainability

National Finance Act	✓(Article 16) Budgeting Principles: secure financial soundness and minimize the burdens of people
Budget Process	✓ Top-Down Budgeting: expenditure ceiling set beforehand ✓ Performance Budgeting: project performance review every year
Nat'l Finance Management Plan (MTEF)	✓ 5-year Projection for GDP growth, revenue, expenditure ✓ 5-year Target for fiscal balance, government debt level ✓ Fiscal Consolidation Plan and Investment Plan by Budget Sector

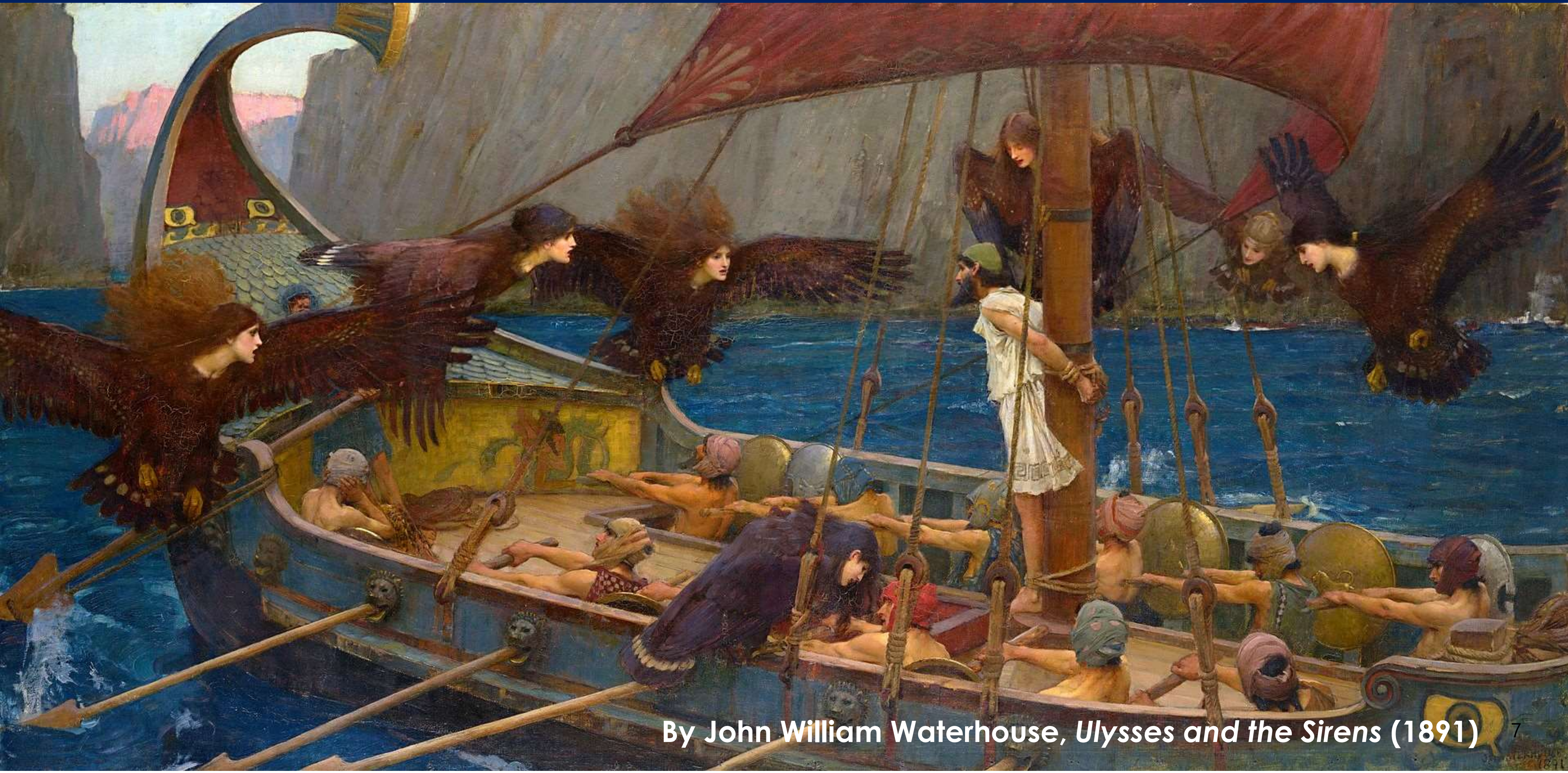
National Fiscal Management Plan (MTEF)

◆ Fiscal rule is needed as a strong discipline on the budget





Do we have the guts to hold ourselves to the mast?



By John William Waterhouse, *Ulysses and the Sirens* (1891)

New Fiscal Framework: Fiscal Rule

◆ Korea's fiscal rule is a type of budget balance rules (BBR)

RULE TYPE

Balance rule

+

Debt indicator as complementary

CEILING

Managed balance -3%

When debt exceeds 60% of GDP

Managed balance -2%

※ **Managed balance = fiscal balance** (total revenue – total expenditure) **– social security funds** (National Pension, Private School Staff Pension, Unemployment Insurance, Industrial Accident Compensation and Prevention)

Fiscal Rule: Escape Clause

◆ **Fiscal rule ensures agile fiscal response to economic crisis**

Supplementary Budget	Escape Clause
1. War, large scale disasters	1. War, large scale disasters
2. Significant economic condition change (e.g. recession)	2. Significant economic condition change (e.g. recession)
3. Expenditures by legal mandates	

Fiscal Rule: Normalisation Measures

◆ **Normalisation measures should be implemented after the exemption**

✔ Include Fiscal consolidation measures in the NFMP

① Improve spending efficiency, e.g. discretionary expenditures restructuring

② Expand fiscal revenues, e.g. reduce tax exemption, etc.

③ Enhance fiscal management schemes, etc.

✔ Use all carried over tax revenue surplus on debt repayment

Fiscal Rule: Additional Measures

✔ Raise required use of net carry-over to pay back principle

	Carried-over tax revenue surplus (A)	
①	Local Govt. transfers settlement (B)	· general transfers(domestic tax 19.24%) / education(20.79%)
②	Public Fund Repayment Fund (C)	· (A-B) X 30% or above
③	Debt repayment (D)	· (A-B-C) X 30% or above → 50% or above
④	Supplementary budget / tax revenue(E)	· A-B-C-D

✔ Review the adequacy of ceiling every 5 years

Fiscal Rule: Evaluation

◆ Korea's fiscal rule proposal has generally positively evaluated

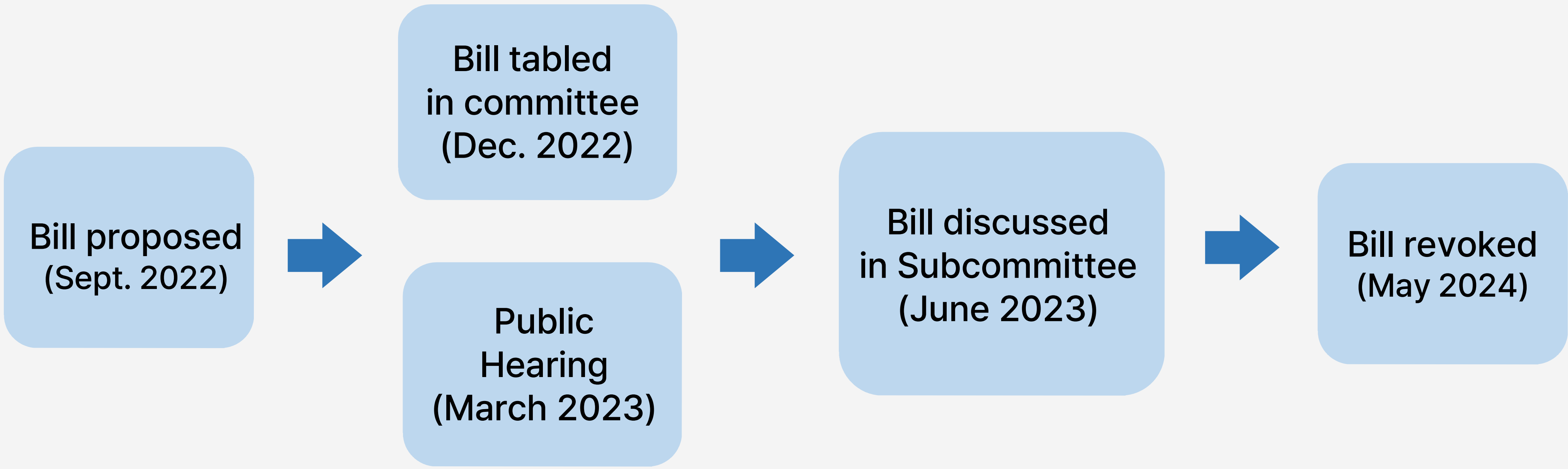
"A rules-based fiscal framework would help anchor public finances amid long-term challenges from rapid population aging" (Oct. 2023)

"The government announced a revision to the proposed fiscal rule, which is welcome" (Sept. 2022)

"Passage of a fiscal rule could help anchor fiscal policy in the medium term" (Oct. 2023)

Fiscal Rule: Legislation Status

◆ The bill was revoked in the 21st National Assembly, but will revive in the 22nd



Why did not they have the guts then?

The Committee in the 21st National Assembly (27 June 2023)

Rethinking Fiscal Rule

◆ Korea's fiscal rule has conundrums in the foreseeable future

✔ Social insurance (pension, healthcare, LT care etc.) deficits

✔ Response to low fertility, low potential growth, and climate change

✔ Harmony with counter-cyclical monetary policy

Thank you

Ministry of Economy and Finance