<u>Welcome Remark</u>

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Good morning everyone,

Let me begin by expressing my deep gratitude to Honorable Governor Juyeol Lee of the Bank of Korea, Director Tiwari of the IMF's SPR Department, and their dedicated staff, for organizing a timely and meaningful conference today.

I'd also like to extend warm welcome to all distinguished participants and guests, and thank them for their presence.

We have many world-renowned experts and policy-makers here today; and I'm sure we will have a very productive day.

Distinguished guests,

We all know that "history does not repeat itself", but "it rhymes" instead.

In this spirit, I'd like to quickly reflect upon past financial crises that have fundamentally changed global financial landscape; share with you my thoughts on the perils of the increasing leverage in the contemporary context; and propose some directions for policy responses.

Just like its dictionary definition, "leverage" increases the amplitude of business cycles.

In this sense, all major financial crises we have experienced in the past are closely related to the rise and decline of leverage.

For instance, at the root of the Asian Financial Crisis of 1997 was excessive corporate debt, of both financial and non-financial origin.

The Global Financial Crisis of 2008 was triggered by imprudent subprime loans in the U.S.

Similarly, the European Debt Crisis of 2010 broke out with excessive public and private debt in a small number of European countries.

In its Global Financial Stability Report published October this year, the IMF reported that there was a 26%p growth in the average emerging market corporate debt-to-GDP ratio in the period of just one decade; and the ratio recorded 74% in 2014.

A sharp rise of corporate debt level in Asia was particularly noteworthy.

In this changing global economic environment, the high level of debt in emerging market is raising concerns of yet another turmoil in global financial market.

Ladies and gentlemen,

Emerging market economies in Asia have been experiencing a growth slump, together with a high level of leverage. This is one distinguishing feature of the debt problem in Asia today.

I believe this phenomenon is closely related to 2 significant shifts in the global economic landscape: one is normalization of the U.S. monetary policy; and the other is China's growth strategy change.

These 2 distinct shifts make debt management rather challenging task for emerging market economies in different manners:

The U.S. policy rate lift-off would provoke a series of debt redemption demands as it would make global liquidity less abundant and depreciate emerging market currencies.

On the other hand, the slow-down of the Chinese economy and its structural shift would decelerate economic growth in emerging market economies and thus make it more difficult for them to sustain their debt-level.

Just as we are more prone to fall off a bicycle at a slower speed, stagnating growth can quickly transform manageable debt-level into a substantial burden.

In this context, the governments of emerging market economies are in a rather difficult situation with managing their debt-level. If they increase the leverage for the sake of economic growth, they may face increased risk for their overall economy.

On the other hand, if they emphasize the deleveraging for the sake of risk management, an economic slump may ensue and increase debt burden – and these may trigger foreign capital flight.

Indeed, it is high time that emerging market economies implement well-targeted policy responses to avoid falling into a debt-deflation trap.

Distinguished participants,

Against this backdrop, I'd like to propose the following 3 prescriptions which I believe are necessary for emerging market economies in Asia to successfully tackle the impending debt problem.

First, I’d like to call for a combination of expansionary policies and macro-prudential measures.

As I mentioned, today’s economic environment presents twin policy objectives to emerging market economies: they need to both intercept the growth slump and manage the debt-level.

In this regard, policy-makers should take two-track approach as well: Strong upward momentum in business cycle should be reinforced by expansionary macroeconomic policy packages and creation of effective demand at micro-level.

At the same time, individual economies should mend internal credit risk vulnerabilities.

In fact, Korea has been deploying such combination of measures.

Together with expansionary policies like fiscal stimulus packages, Korea has pushed forward with ambitious consumption boosting measures from individual consumption tax cut to Korea Black Friday sales. Thanks to these efforts, Korea has achieved 1.3% growth in the 3rd quarter of this year on a quarter-to-quarter basis, all in the midst of persistent worldwide economic slump. It was also the highest such growth in the past 5 years.

Moreover, the Korean government is encouraging transition of household debt type, towards fixed-rate, amortizing loans.

In addition, it has been promoting advanced loan review techniques to strengthen debt management efforts.

To better manage corporate debt, the Korean government has been doing its best to shape the environment into the one that is conducive to preemptive, market-friendly corporate restructuring.

For example, it has been pushing forward with government legislation that aims to promote voluntary structural reorganization in private sector.

Second, I'd like to emphasize the importance of FX-related macro-prudential measures, especially as a preparation against potential capital flights.

Although emerging market economies in Asia are significantly sounder than before, the current environment is not too friendly for them; and current shifts in external environment do not look too good.

The authorities should strengthen their external debt management efforts as they bear in mind that a market shock can lead to a sudden rise of foreign capital outflow.
Having realized this, the Korean government has long been operating various macro-prudential measures, such as the macro-prudential levy.

Thanks to such efforts, Korea's external soundness has been improving: The external debt level has been on the decrease, and the share of short-term external liabilities has been decreasing as well.

Finally, I'd like to draw your attention to international coordination efforts for financial stability.

Close international cooperation is more necessary than ever to contain the spread of financial market unrest, especially if it were to arise from emerging market debts.

I would very much like to reiterate the need for reinforcing multi-layered financial safety net, including currency swap agreements between advanced economies and emerging market economies; improving effectiveness of regional financial safety net; and surveillance activities and financial assistance of the IMF as the global lender of last resort.

The G20 has been instrumental in this effort for strengthening the global financial safety net.

For instance, it decided to resume the International Financial Architecture (IFA) Working Group, which Korea was asked to co-chair.

I am optimistic that the G20 will play a central role next year, and deliver tangible outcomes for enhancing the International Financial Architecture.

Distinguished participants and guests,

Having experienced a financial crisis in 1997, Asian economies rectified systematic anomalies and improper practices from the past.

With an enhanced financial system, their capacities against external shocks have been vastly improving.

Many Asian countries have adopted floating exchange rate regime; and short-term external liability to FX reserve ratio has substantially decreased.

Nonetheless, I don’t think it is never too early to examine potential risks and prepare appropriate policy measures in case of a contingency: A stitch in time will surely save nine.

I have no doubt that today's discussions will serve as an occasion for us to assess potential risks in the region, and they will strengthen our crisis response capabilities.

Thank you.