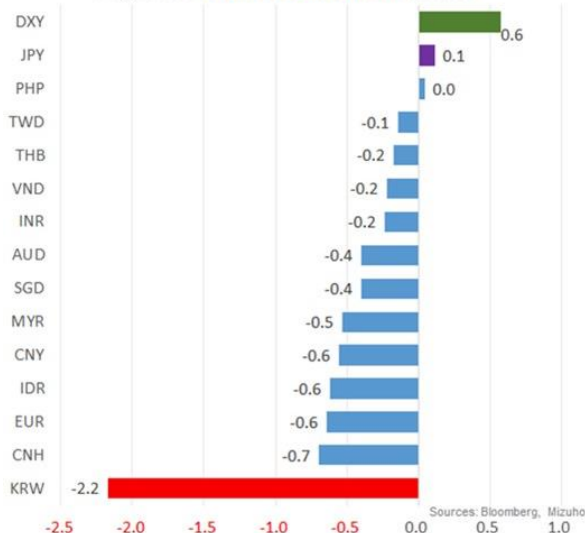
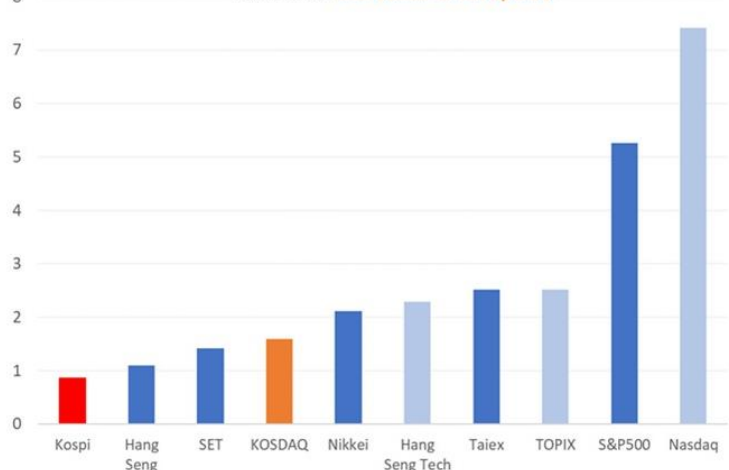


Macro Brief – Korea Risks: Short-Lived Martial Law Jolt, But Sticky Risk Premium?

AXJ (% Chg, Month-to-Date for Dec 2024): **KRW**
Slumps on Martial Law Decree although Revoked.
 Some **Stickiness around KRW Risk Premium** &
 Heightened **Downside Sensitivities** Expected.



Price-to-Book Ratio: The "**Korea Discount**" is Distinct & Profound. Even
 Korea's star **tech sector is Not Spared**.



- **President Yoon’s shocking, albeit short-lived, declaration of martial law** raises uncomfortable **questions of political risk premium on KRW assets**.
- **Martial Law Decree Ditched**: To be sure, the *martial law attempt has been promptly defused* by resounding Parliamentary opposition, which forced Yoon to walk back on the martial law decree.
- **Backfired Politically**: What’s more, Yoon’s **attempt to seize power** and tame opposition **by means of martial law has truly back-fired**.
- In fact, **Yoon’s chances of political survival are dismal**. It is merely a **matter of time before he is ousted with fresh Presidential elections (likely in H1 2025)**.
- **Nonetheless, Korea’s Risk Premium Not Unscathed**: *But* despite an arguably efficient political mechanism to safeguard democracy and free markets, **Korea’s perceived risk premium may not be unscathed**.
- **Deterrence Welcome**: Admittedly, the **failed attempt at martial law** may be of **some deterrence** for any future President to invoke it with impunity.
- **Economic Interests a Check**: Moreover, and crucially, **overwhelming economic interests** of the private sector will act as **a consistent and dynamic check** against **engineered political upheavals**.
- **But Political Risks Linger**: Nonetheless, worries of **underlying political fractures/factions** and the *resultant impediments to efficacious policy-making* remains *a bugbear*, with **attendant political risk premium**.
- **Pre-Existing Economic Challenges**: What’s more, **pre-existing economic challenges**, from *housing market risks, relatively lagging semiconductor performance* and *fiscal headwinds*. continue to be stress points for policy and politics.
- **Exacerbated by Trump 2.0 Tariff Threats**: Worse, with impending **Trump 2.0 tariffs**, Korea risks greater *economic blowback from collateral damage to its key upstream position* and bi-lateral US trade imbalance.

- **Reflexivity & Stickier Risk Premium**: And to George **Soros'** famous point about **reflexivity**, risks often don't work in isolation, instead feeding into, and off, each other.
- **& Stickier Risk Premium**: And this **renders risk premium downwardly sticky** for some time.
- **Fiscal Implications**: The risk is that an already **drawn-out budget process** (that was crimping the President's discretionary funds) **may be further delayed**. This may *inevitably delay pass-through of fiscal buffer* for the economy (GDP).
- **Bank of Korea**: While the **BoK** has (rightly) stepped in to be the **liquidity provider of last resort**, its underlying policy dilemma is further accentuated. The **undermined KRW raises the bar for rapid/imminent rate cuts** (although the direction of travel is down for rates).

Equities: “Korea Discount” Could Stick

- In the equities space, this **attempt at martial law retards attempts to diminish the Korea risk premium**.
- Namely, the “Corporate Value-Up Program” may have been set back.
- Consequently, the so-called “Korea discount” may be rendered **harder to shake off** quickly.

FX: KRW may be Prone to Under-performance

- **KRW**, which went into a **tailspin** to fall ~3% (to 1445 levels) on the martial law announcement jolt, has since **partly recovered**; and is *now “only” down less than 2%* (at 1420-1430).
- Alongside spill-over Trump 2.0 tariff risks, **KRW could face greater downside sensitivities**.
- *To some extent this could favour a long JPY/KRW position in relative terms (and to be USD agnostic)*.

Yields: Risk Premium may Widen

- Earlier last month a sharper drop in KGB yields was partly induced by the surprise BoK cut.
- And there is an underlying, structural drag on KGB yields from spill-over deflation shock risks from China.
- But these are not to be mistaken for diminished risk premium.
- We expect credit spreads may pushback (widening by 20-30bp is not unimaginable).

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