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South Korea’s Household Debt Crisis and Its Impact on Korean Society

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ABSTRACT

South Korea’s household debt crisis was brought to the forefront of the minds of millions of people around the world due to the hugely popular Netflix series *Squid Game*. In *Squid Game*, individuals with large amounts of personal debt engage in childhood games like “Red Light, Green Light” but with a macabre twist: they must risk their lives and the lives of others to win a cash prize that could relieve themselves of crushing debt. This paper examines the major economic, financial, and societal factors that contribute to the ever-worsening household debt crisis in South Korea. In the past 25 years, South Korea has endured several major economic and financial crises, notably the 1997 Asian Financial Crisis, the 2017 Global Financial Crisis, and the Covid-19 Pandemic. In particular, the Asian Financial crisis in 1997 brought about significant changes to South Korea’s financial, corporate, and labor sectors, primarily due to reforms imposed by the International Monetary Fund (IMF). Furthermore, run-away housing prices, elevated levels of self-employment, and societal structures and behaviors unique to Korea have exacerbated the household debt crisis. All these factors have contributed to the growth and the continuing trend of extreme household debt that disproportionately impacts South Korea’s youth, self-employed, and part-time workers.

Introduction

South Korea’s struggle with household debt was prominently showcased in *Squid Game*, a nine-episode television show that garnered over 111 million viewers worldwide. In *Squid Game*, a deeply indebted middle-aged man is competing against 455 similarly indebted individuals for a chance to win ₩45.6 billion (approximately 38 million US dollars). Participants play in games that are based on innocent children’s games, but the outcome of each game is anything but innocent. Losing means death, and eventually, only one person will remain standing to take home the prize. Even with this knowledge, participants continue to play the games despite the deadly consequences because of their desperation to lift the burden of debt. According to many viewers, *Squid Game* accurately portrays the harsh debt crisis that many South Koreans are currently suffering from (Winter et al., 2021).

In 2021, household debt in South Korea amounted to about 107% of its Gross Domestic Product (GDP), which ranks among the highest in the world, higher than any other Asian country (Trading Economics, 2021). Additionally, South Korea's debt measured as a percentage of its net disposable income was 201% in 2021. In comparison, the United States’ debt as a percentage of net disposable income was 101%, half that of Korea's (OECD, 2022).

How did Korea come to a point where its household debt is greater than 100% of its GDP – the highest in Asia? This paper seeks to investigate the major factors driving the deepening household debt crisis and its impact on society.

Background

Economic Miracle on Han River

It is crucial to examine South Korea's economic history to properly understand the household debt issue in the country. Korea was under Japanese colonial rule from 1910 to 1945. Upon independence, the country was divided into Soviet and American spheres of influence, which eventually became the Democratic People's Republic of Korea (North Korea) and the Republic of Korea (South Korea) (Pruitt, 2018). Following the bloody aftermath of the Korean War, South Korea was a devastated country in abject poverty. However, during the post-Korean War period (from 1953 to the Asian Financial Crisis in 1997), South Korea experienced phenomenal economic growth often described as "the Miracle on the Han River" (ROK-Center, 2019). South Korea's GDP per capita grew from less than $158 USD in 1960 to over $13,403 USD in 1997, a stunning increase (World Bank, 2020).

1997 Asian Financial Crisis

After years of sustained economic growth, South Korea and several other Asian countries entered a severe financial crisis in 1997. Foreign investors, reeling from losses in other Asian countries, started to withdraw their investments and loans to South Korea, reversing the capital inflows that had once helped finance South Korea's economic growth. As a result, during the first quarter of 1998, real gross domestic product decreased for the first time in eighteen years, dropping by an annualized rate of 3.6% (Lee, H., 1999). The yearly unemployment rate in 1998 jumped to 6.8%, in contrast to 2.6% just a year prior.

In response, the South Korean government received an International Monetary Fund (IMF) financial bailout worth $59 billion. As a condition for receiving the intervention of the IMF, the South Korean government agreed to pursue economic reform in the financial and corporate sectors as well as labor reform. In February 1998, greater labor market flexibility was instituted with the revision of the Labor Standard Act (LSA), which legalized layoffs for managerial reasons. The revision of the LSA facilitated necessary layoffs in the process of financial and corporate sector reforms. While South Korea was able to avoid a sovereign default with the help of IMF bailout funds, the austerity measures imposed on South Korea by the IMF have had a long-lasting adverse effect on South Korean society. The 1997 crisis - and the response to it - negatively affected Korean people across all segments of society, but low-income households, women, young workers, the poorly educated, and first-time job seekers were hit the hardest (Lee, H., 1999).

While South Korea's economy has since recovered from the 1997 financial crisis, for many without a college education or a job at one of Korea's large conglomerates, the crisis never truly ended. After the crisis, irregular, part-time employment became far more common in South Korea, as under pre-crisis labor laws it was almost impossible to fire workers (Borowiec, 2017).

2007-2009 Global Financial Crisis

The Global Financial Crisis from 2007 to 2009 hit South Korea hard again. During this crisis, capital flowed out of Asian countries, including South Korea, leading to a severe credit crunch, or an abrupt reduction in the availability of credit in the form of bank loans and mortgages. The crisis disrupted the interbank lending market, the medium by which banks extend loans to one another that used to provide about one-third of Korean bank funding before this crisis (Bernanke, 2019). Consequently, South Korea's GDP shrank from about $24,086 to $19,143, decreasing over 20% during this period (World Bank, 2020).

Accelerating Housing Prices Under President Moon Jae-In

Following the impeachment of President Park Geun-Hye and riding off opposition to corruption in the conservative Saenuri Party (presently known as the People Power Party), President Moon Jae-In took office as a liberal reformer promising to control the growth in housing prices, particularly in the Seoul metropolitan area where over 50% of the population of South Korea resides. However, despite countermeasures intended to curb speculation, housing prices soared under his watch (Figure 1). His policies were ineffective as the average price of an apartment in Seoul increased by 90% since he took office in 2017 (Kim, S., 2021).

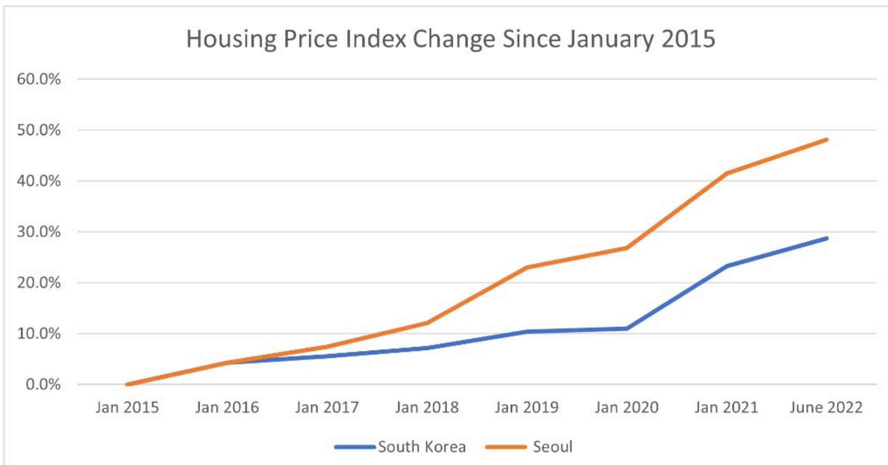

Figure 1. Housing Price Index Change Since January 2015.

The steep rise in housing prices in Seoul in recent years has prompted many young South Koreans to take out outsized amounts in loans to buy property (Kwon, 2020). This meteoric rise in housing prices has led to record high mortgage and household debt in Korea that has yet to slow down, and the sum of nationwide household debt in South Korea doubled from 2011 to 2021 (Figure 2).

Figure 2. Total Value of household debt in South Korea from 2011 to 2021 (in trillion South Korean Won).

COVID-19 Pandemic

The COVID-19 pandemic heavily impacted private consumption and the labor market. Consequently, overall unemployment increased to four percent but the unemployment rate for people aged 15 to 29 years old increased significantly to nine percent in 2020 (Yoon, 2022a). Furthermore, the extended unemployment rate for people aged 15 to 29 was twenty percent in 2020. The pandemic impacted part-time and independent contractors disproportionately compared to salaried, full-time workers, as one survey conducted in 2021 showed that about 33% of part-time and independent contractors reported losing their jobs, compared to eight percent of full-time employees (Yoon, 2022b).

Factors Driving Household Debt

Rise of Personal Loans and Credit Cards

One of the key factors driving household debt is the rise of personal loans. After the Asian financial crisis in 1997, lending for household loans surged. This rise in household loans was due to weak corporate loan demand, as well as monetary and fiscal policies that made it easier to obtain personal loans to stimulate the economy, in addition to the rise in living standards and home prices in South Korea. Another factor contributing to the rise of personal loans is the increased use of credit cards, spurred by a post-1997 crisis policy that provides tax benefits for merchants accepting credit cards and, for cardholders, income tax deductions linked to their credit card purchases. These incentives have contributed significantly to the Korean credit card lending boom of 1999 to 2002 (Kang and Ma, 2003).

Korea's Jeonse System and Its Impact On Youth

Jeonse is a rental system that is unique to South Korea. In this system, instead of paying a monthly rent, the tenant deposits about 65% of the value of the property to the property owner, typically over a period of 2 years. At the end of the term, the property owner returns the original deposit. Since 2017, loans extended to Koreans in their 20s and 30s to pay their *jeonse* rents have more than doubled. Indeed, the combined value of *jeonse* loans extended to Koreans in their 20s and 30s in the last four years was about 61.5 percent of all *jeonse* loans, reflecting the fact that many Koreans in their 20s and 30s are unable to purchase a house in the nation's red-hot real estate market, and instead are settling for the *jeonse* rent system (Jung, 2021).

Furthermore, many young Koreans cannot even afford *jeonse* loans. Instead, they live in *goshiwons*, small dormitory-style rooms with a desk, a bed, and sometimes a bathroom. They were originally meant as a temporary place for students to isolate themselves from distractions to study for exams, but due to Korea's housing crisis, they have become a common housing type for many people, including millennials who cannot afford regular housing. (Teh, 2021). According to the Land and Housing Institute in 2017, approximately 22.6 percent of young single-person households live in substandard apartments smaller than 150 square feet, which is significantly higher than the overall household rate of 12 percent (Shin, 2020).

Risky Financial Behaviors

Given the economic plight of Korean youth, there has been a rise in the risky investment trend of borrowing to invest, known in Korea as "bittoo," with many taking on loans to buy stocks on margin and to invest in risky, speculative investments such as cryptocurrency. In 2020, retail investors purchased a record number of local shares worth over sixty trillion won (about $50 billion) by using loans taken out specifically for buying investment shares as well as using savings, overdrafts, and other loans (C. Kim, 2020).

In addition, it is common for young Koreans to splurge on branded goods to the point of becoming indebted, a trend that became more pronounced during the pandemic. One of Korea's largest department store chains, Hyundai Department Store, reported that luxury shoppers in their twenties have been steadily on the rise recently. That number grew from 27.5 percent in 2018 to 37.7 percent in 2020 despite Covid-19's negative impact on most other industries (Yang 2021, Figure 3).

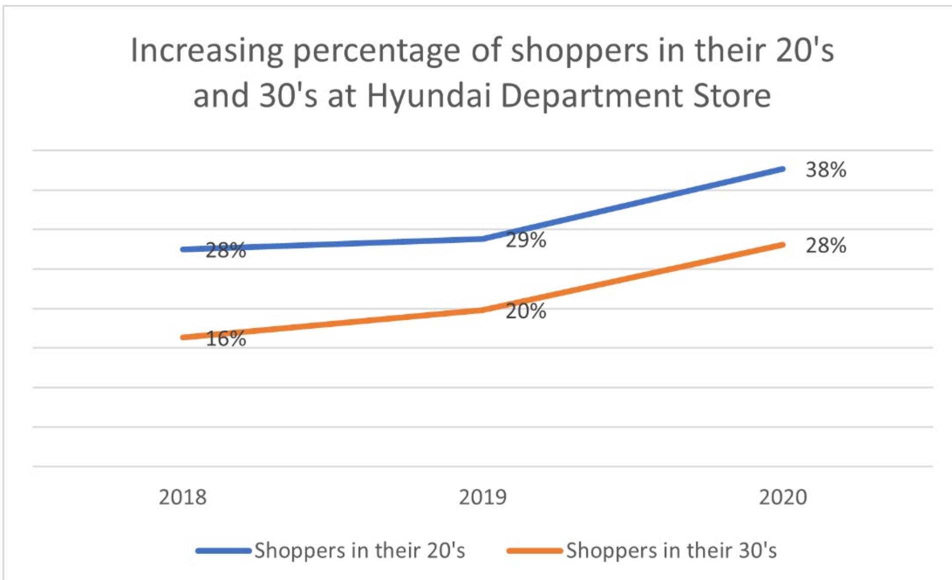

Figure 3. Increasing percentage of shoppers in their 20's and 30's at Hyundai Department Store.

Excessive Self-Employment

According to the OECD, the self-employment rate for Korea is 24.6% as of 2020, one of the highest in the world. For comparison, the self-employment rate in the United States was 6.3% as of 2020. While some in South Korea are self-employed by choice, many have no other choice but to be self-employed. During the Asian Financial Crisis of 1997, many corporations went bankrupt or downsized, facilitated by a new labor policy that relaxed the rules for layoffs. Many newly laid-off employees joined the ranks of the self-employed. A similar phenomenon occurred during the 2007-2009 Global Financial Crisis, although at a smaller scale and primarily among the younger workers as companies reduced the number of new hires. The majority of self-employed either have no employees, work under temporary contracts, or work as outsourced laborers for larger firms. They are closer to laborers than entrepreneurs but without the social insurance and labor protections afforded to traditional employees (E. Lee 2022).

In addition, the average amount of debt for the self-employed, according to the Financial Supervisory Service, is five times that of the general population (K. Kim, 2018). During economic downturns, such as one caused by the COVID-19 pandemic, the self-employed are disproportionately impacted due to the loss of customers and tightening credit lines from traditional lenders, which forces some to borrow from non-traditional, extremely high-interest rate loans. Unfortunately, self-employment is becoming a progressively less viable option for those without an income due to competition arising from the increasing number of self-employed businesses, as well as larger businesses gaining increased influence in sectors traditionally dominated by self-employed businesses (E. Lee, 2022).

Rising Youth Unemployment Rate

The official unemployment rate for Korean youth (those from age 15 to 29) in March of 2021 was 10 percent. However, according to Statistics Korea, the *de facto* jobless rate for Koreans aged 15 to 29 in May 2017 was 22.9 percent and has been increasing every year, reaching a record of 27.2 percent in January 2021. Despite Moon Jae-in administration's policies and spending geared to create jobs, the job market for young Koreans in their twenties and early thirties remains extremely difficult, as more than one-quarter of young Koreans are unemployed or underemployed (Figure 5) (Y. Kim, 2021).

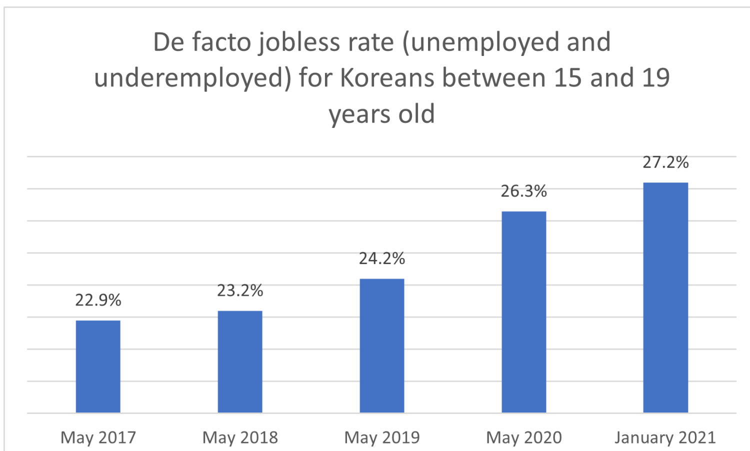

Figure 4. De facto jobless rate (unemployed and underemployed) for Koreans between 15 and 19 years old.

Impact on Individuals and Society

Rising Personal Bankruptcies, Financial Stress

Moreover, personal bankruptcies have been on a steady increase in recent years. As reported by the National Court Administration, personal bankruptcies filed in 2020 reached a total of 50,379 cases, a 10.4 percent increase from the previous year and the most since 2015 ("Personal", 2021). Unfortunately, in South Korea, those who file personal bankruptcies face a lengthy list of employment restrictions, and the stigma of failure stays with them for a long time. According to bankruptcy judge Ahn Byung-wook, "Due to traditional practices in the banking industry, business owners in South Korea face a high likelihood of taking the debt burden from the business they run." Individuals are often forced to stand surety for loans their companies borrow, a practice that, although banned for public financial institutions in 2018, business owners claim still occurs regularly ("No", 2021).

Low Birth Rate

South Korea's fertility rate in 2021 was 1.1, the lowest of any country in the world, according to the United Nations Population Fund's (UNFPA) World Population Dashboard. One of the biggest factors contributing to such a low fertility rate is debt, as many younger South Koreans decide against getting married for financial reasons. The price of housing has skyrocketed in recent years, making it extremely difficult to buy or rent new properties without going into extreme and unsustainable amounts of debt. Additionally, due to the high demand for quality education in Korea, the cost of raising a child is extremely high as well. As of 2019, about 75% of Korean students attend private education academies from an early age to get into a top-ranked university. According to one survey, the average cost of private academies was about 429,000 won ($3500) per month. Therefore, for an increasing number of South Koreans, staying financially dependent on parents is becoming the best way to stay out of debt, leading to fewer marriages and a lower fertility rate (J. Lee, 2021).

Suicide

Suicide is an extremely prevalent issue in South Korea. South Korea has the unfortunate distinction of having the highest suicide rate among OECD nations, more the double the OECD average (OECD, 2021). According to Statistics Korea, suicide was the number one cause of death among those aged 10 to 39, with a recent surge among teen boys and young women in their 20s (KBS), The causes of suicide are complex and are not only due to personal and mental health issues, but also related to economic and social factors (D. Jung). When compared to other Asian countries with similarities in geography and culture (Japan, Hong Kong, Singapore, and Taiwan), the rising trend of suicide rates over the past three decades was unique to South Korea. Data analysis showed a negative correlation between economic growth and suicide rates, particularly for working-aged people, and the association between suicide rates and economic adversity such as unemployment and economic contraction was particularly strong among middle-aged men in South Korea. It is important to note that financial or economic stress is not unique to South Korea. But the degree to which it permeates South Korean society is uniquely elevated due to incredibly high household debt and the intense cultural stigma of financial failure (Hong, Knapp).

Interestingly, plotting the suicide rate per capita against household debt in OECD nations shows little to no correlation between suicide rate and debt (Figure 5). This shows that South Korea's debt crisis, along with its impacts such as an extremely high suicide rate, is unique and likely to be heavily influenced by cultural and economic factors such as extremely stressful lifestyles, poor work-life balance, poor social safety net, and a high-pressure educational system.

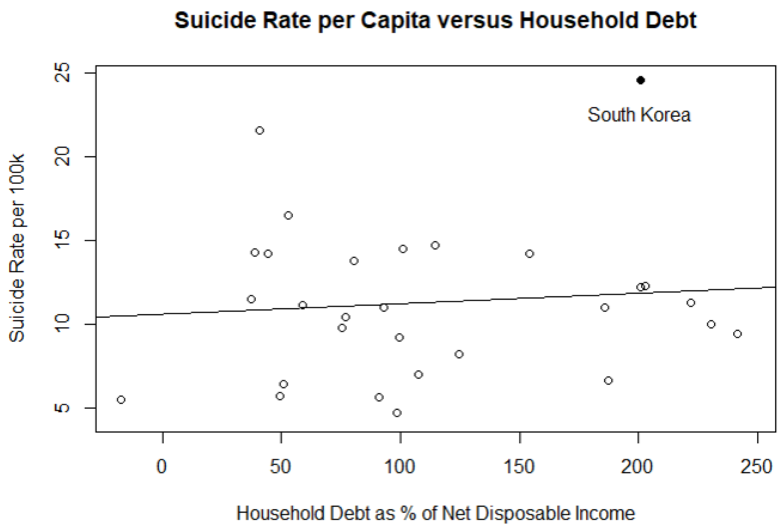

Figure 5. Suicide Rate per Capita versus Household Debt.

Conclusion

Unfortunately, many familiar with socioeconomic, financial, and cultural issues facing South Korea agree that the macabre television series *Squid Game* is not far off from accurately depicting the harsh reality of the South Korean household debt crisis. South Korea's run-away housing prices, mounting personal loans, and credit card debts, high youth unemployment, excessive self-employment rate, and inadequate social safety net result in an incredibly stressful financial burden for many South Koreans. These issues are especially prevalent among the young as they are less likely to be employed but incur more debt for mortgage or *jeonse* loans.

Moreover, this household debt crisis contributes to Korea's devastatingly high suicide rate, the highest among OECD nations, as well as the lowest birth rate in the world which threatens the very social structure of South Korea in the long term. It is abundantly clear that the household debt crisis facing South Korea is extremely serious and further exacerbates already negative cultural aspects such as poor work-life balance and few social programs. Further research into social, fiscal, and corporate reforms, especially regarding loan and labor laws, should be undertaken to reduce the impact of the household debt crisis in all parts of Korean society.

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