

HRI

Monthly Economic Review

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I . Recent Global & Domestic Economic Trends

Global Major Economies

The economic growth rate of USA and China slows down. Financial crisis of Euro zone reemerging.

The US economic growth rate marked 4.1% in the fourth quarter of 2011, but slowed down to 2.0% in the first quarter and to 1.5% in the second quarter of 2012. The individual consumption growth rate in the second quarter of 2012 stayed at 1.5%, reduced by 0.9%p compared with the previous quarter, and the government expenditure also shrank by 1.4% compared with the previous quarter. The consistent appreciation of US dollar against Euro is further weakening the competitive edge of US export products.

The concern about the European financial crisis is reemerging as the credit rating of Germany, the most powerful economy of Euro Zone, was downgraded amid the growing concern over the possibility of Spain's default. The outlook of Germany's credit rating was also readjusted down with the composite PMI recording 47.3, the lowest for three years. The possibility of Spain's default is growing with the Spanish government 10 year bond yields having reached a record high 7.71%.

Japan's trade balance turned into the black, while the domestic market remained depressed. The industrial production of June showed -0.2%, and the growth rate of retail sales at 0.2%, a slow-down compared with the previous month. The economic growth rate of China of the second quarter of 2012 was 7.6%, marking for the first time below 8% since 7.9% of the same quarter of 2009 due to the reduction of export caused by the European financial crisis. The export amount of China in the first half of 2012 was US\$954.3 billion, only a 9.2% increase compared with the first half of 2011.

Global Financial Market

Equity markets in US and Europe rallied in July with hopes of improvement in the Euro Zone economy

Share prices of the US and Europe markets rose in July with hopes of improvement in the Euro Zone economy, as Mario Draghi, the governor of ECB announced that he would commit in earnest to resolve Euro Zone financial crisis. The DJIA came back to 13,000s despite the stagnant domestic market and weakening competitive edge. The DAX index of Germany was up despite the Euro Zone's overall poor performance. Nikkei was down with Japanese yen continuing to appreciate, preventing Japan from economic recovery. China's SSE composite index was down mainly due to the shrinking export growth rate.

The JPY/USD exchange rate appreciated in July despite Japanese government's positive measures to turn it otherwise due to the increasing demand for yen. EUR/USD exchange rate depreciated in July and August as the concern over the Euro crisis grew again. The CNY/USD exchange rate was slightly down in July compared with the previous month.

<Economic indices of major countries>

(Unit: %)

Economic Sectors		2011	2012			
		Annual	Mar	Apr	May	Jun
US	Industrial Production	4.1	-0.5	0.8	-0.2	0.4
	Retail Sales	7.9	0.3	-0.6	-0.2	-0.5
EU	Industrial Production	3.5	-1.4	-2.0	-2.3	-
	Retail Sales	-0.6	1.0	-2.4	-0.3	-
Japan	Industrial Production	-3.5	1.3	0.2	-3.1	-2.0
	Retail Sales	-1.2	10.3	5.7	3.6	0.2
China	Industrial Production	13.7	11.9	9.3	9.6	9.5
	Retail Sales	17.1	15.2	14.1	13.8	13.7

<Financial indices of major countries>

(Unit: p, yen, euro, yuan)

Economic Sectors		2011	2012			
		Annual	May	Jun	July	Aug
US	DJIA	12,218	12,393	12,880	13,009	13,094
EU	DAX	5,898	6,264	6,416	6,772	6,810
	EUR/USD	0.772	0.809	0.804	0.816	0.821
Japan	NIKEI	8,455	8,543	9,007	8,695	8,555
	YEN/USD	77.66	79.10	79.37	78.17	78.25
China	SSE composite Index	2,199	2,372	2,225	2,104	2,131
	CNY/USD	6.3190	6.3578	6.3575	6.3795	6.3674

Sources: US department of Commerce; Eurostat; The People's Bank of China; Reuters

Korean Economy

The domestic economy is deteriorating due to the decreasing export amount caused by the global economic environment and depressed domestic market.

The growth rates of retail sales shrank in a large scale, and the growth rate of the facility investment index continued to fall with declining investment in general machinery, electric and electronic goods. The growth rate of construction is also falling.

Export amount in July of 2012 marked US\$44.6 billion, 8.8% less than the same month of 2011. Particularly, intermediate goods including steel and petrochemical products suffered a setback due to the declining demand and falling price. Import amount was also down by 5.5%, leaving the trade balance in the black, US\$2.7 billion surplus in recession.

The unemployment rate stayed at 3.2% in June with more people finding jobs, and the consumer price inflation rate marked 1.5% in July, the lowest since July 2009.

BSI in manufacturing recorded 85 in June, 81 in July, and 70 in August, showing downward trend for the four consecutive months. Composite leading index and cycle variation value marked 99.5 in May and 100.0 in June, still remaining near the critical line 100.

Share prices rose in July with the expectation for Euro Zone financial crisis to be resolved, and KRW/USD exchange rate strengthened. Interest on corporate debentures also continued to show downward trend in July.

KOSPI rose in July as the Euro Zone's economic uncertainty decreased with strong determination announced by EU's financial policy authorities to deal with reemerging Euro Zone financial crisis, but fell slightly in August.

The KRW/USD exchange rate fell in July due to the reduced uncertainty of financial market, but was up in August thanks to the announcement of strong determination made by the governor of ECB. The corporate bond yield rates (BBB-) dropped by 0.26%p in July and 0.09%p in August.

Korea's major economic indices

(Unit: p, %, won/dollar)

Economic Sectors		2011					2012				
		Annual	1/4	2/4	3/4	4/4	1/4	2/4	June	July	Aug
Domestic Market	Retail Sales	4.3	5.4	5.7	4.7	1.9	2.0	1.0	0.6	-	-
	Facility Investment Index	0.7	5.4	5.7	-3.1	-4.7	9.3	-0.7	-5.6	-	-
	Construction	-6.7	-12.6	-6.6	-8.4	-0.5	-3.7	-10.9	-16.5	-	-
Foreign Trade	Export Growth Rate	19.0	29.6	18.6	21.4	9.0	3.0	-1.6	1.1	-8.8	-
Employment/Prices	Unemployment Rate	3.4	4.2	3.4	3.1	2.9	3.8	3.3	3.2	-	-
	Consumer Price	4.0	3.8	4.0	4.3	4.0	3.0	-	2.2	1.5	-
Finance	KOSPI	-	2,107	2,101	1,770	1,826	2,014	1,854	1,854	1,882	1,849
	KRW/USD	-	1,097	1,068	1,178	1,152	1,133	1,145	1,145	1,131	1,135
	Corporate Bond (BBB-)	10.38	10.61	10.50	10.31	10.12	10.05	9.69	9.25	8.99	8.90

Sources: Bank of Korea, National Office of Statistics, Foreign Trade Association

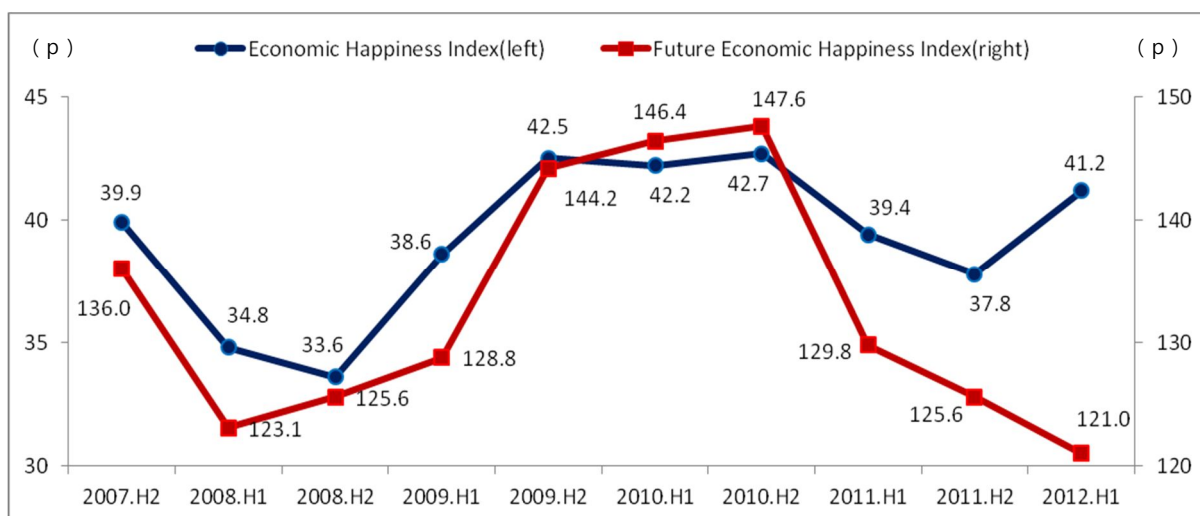
II. Economic issues facing Korea

□ Future Economic Happiness Index at Record Low

How high is Korea's Economic Happiness Index?

Hyundai Research Institute (HRI) has been publishing Korea's Economic Happiness Index (EHI) semiannually since January 2008, indexing the state of subjective sense of happiness in relation to economic factors including individual's income, consumer prices and unemployment. Economic happiness index comprises financial security, economic superiority, economic progress, economic equality, economic insecurity, and general sense of happiness. HRI conducted the 10th survey on 1,000 ordinary citizens in the form of questionnaires (May 30th - June 13th 2012) with maximum sampling error of ±3.09% and confidence level of 95%. Despite the unstable global economic environment which lasted throughout the first half of 2012, the survey revealed that the economic happiness index of Korea rose by 3.4p to 41.2 compared with the previous survey thanks to price stability and the reduction of unemployment rate. The future economic happiness index, however, fell by 4.6p to 121.0, a record low since the survey commenced in January 2008, highlighting a growing concern over the economic climate in the second half of 2012.

< Economic Happiness Index Trend >



Note: The economic happiness index starts from 0 to the maximum of 100 with its middle value 50, while the future economic happiness index starts from 0 to the maximum of 200 with its middle value 100.

Who is economically the happiest as of 2012?

As of July 2012, the happiest Korean people in terms of economy are thought to be the female civil servants in their 20s who are university graduates, unmarried, and living in Daejeon and Choongnam Province area, while the unhappiest are the males in their 60s, unemployed with low income/assets and low educational background.

The survey also revealed that the higher the job security, the higher the sense of economic happiness; the civil servants seem to have the highest economic sense of happiness followed by professionals, office workers, housewives, the self-employed, others, and then finally the unemployed. It is notable that the economic happiness index of the self-employed is 37.6, consistently below the average due to the lasting domestic business slump.

Different age groups showed different level of economic sentiment; the 20s showed 47.1, the highest, while the 60s and above only 37 consistently showing declining level of economic sentiment due to the financial responsibility for the households.

The higher the education level, the higher the sense of economic sentiment; the economic happiness index of those with degrees of graduate school and higher was 48.8, while the index of the middle school leavers was only 31.9, leaving a huge gap of 16.9p, which shows that the higher the education level, the higher the level of income and the economic security.

The survey shows that the economic happiness index of females was 41.8, while that of males was 40.6. It also shows that the unmarried seem happier economically than the married

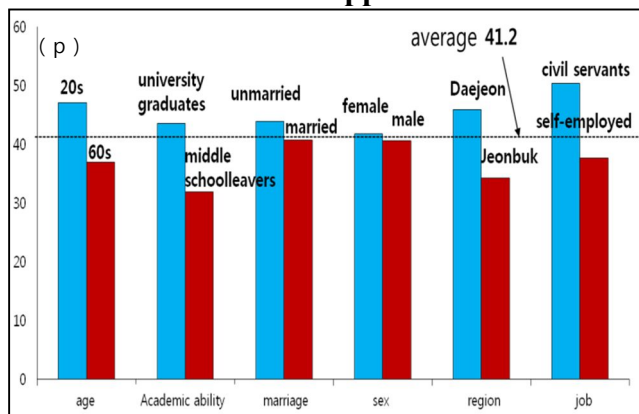
The more income and assets, the higher the sense of economic happiness. Demographically, Daejeon and Choongnam province are the highest at 45.9 and 45.6, where many high-tech industrial complexes are located and where Saejong metropolitan city is being formed and established in earnest. The improving real estate market in this region and expectation for the development of newly-born Saejong city are among the factors for the higher sense of satisfaction. Cheonbuk province is the lowest with 34.3.

Price Stability and Job security are the Core to the Sense of Economic Happiness

Although the GDP per capita of Korea has steadily risen, as many as 84.6% of Koreans think their sense of economic satisfaction is the same as or less than before, for which the decrease of real income, price instability, job insecurity seem to be the main causes. People are demanding the government take action to enhance the effectiveness of policies to stabilize prices of the necessities of life, to create jobs, and to let the people get the feel of the improved sense of economic happiness. To raise the sense of economic happiness, the government should:

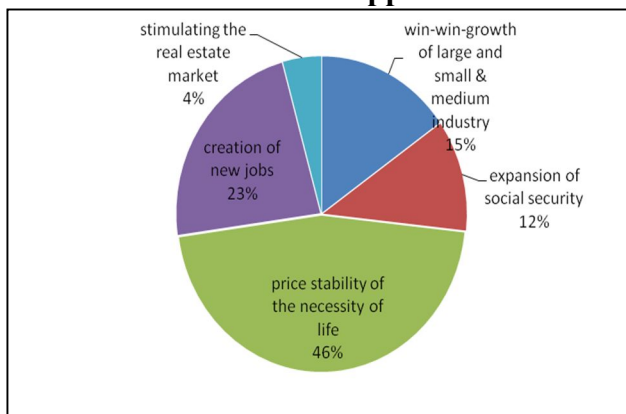
1. Focus on policies to stabilize prices, and set up systematic plans to cope with major causes for price instability such as climate change, surge of raw material prices, and rise of public utility rates, in different stages for each foreseeable cause.
2. Continue to endeavor to create and expand good quality jobs to suit different age groups and different class of people, and strengthen the policies to encourage large businesses for investment and to encourage small and medium business for globalization.
3. Prepare measures to ensure the soft landing of household debt which is the most serious threat to Korea's economy in the second half of 2012, and provide low interest rate loans and intensify incentives for people in the lower income bracket to convert their debts to long-term installments to repay the household debt, and introduce variety of policies to stimulate the real estate market.

< Economically the happiest / the unhappiest >



Source: HRI

< Policies to Enhance the Sense of Economic Happiness >



Source: HRI

III. The North Korean Issues

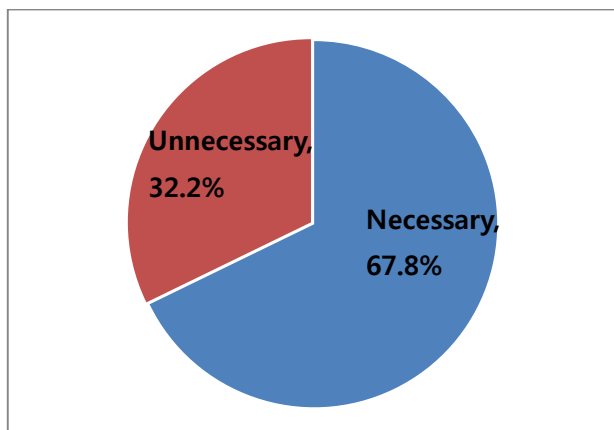
□ Easing of the South and North Korean Tension and Geumgang-san Tour Project

With the Geumgang-san Tour operation suspended for four years, HRI conducted a survey on 1,012 ordinary citizens in the form of questionnaires (June 28th – July 3rd, 2012) with maximum sampling error of $\pm 3.08\%$ and confidence level of 95%. The survey shows that majority of people want the Tour to be resumed in the earliest possible time, as the Geumgang-san Tour is the icon of the promotion of understanding, reconciliation, and peace between South and North Korea. The resumption may not take place immediately, but the desire to join the Tour when resumed seems quite high; six out of ten said it is necessary to change the direction of government policy for more flexibility, and expressed concern over the prospect of inter-Korean relationship for 2013.

Geumgang-san Tour Project is the icon of the promotion of understanding , reconciliation, and peace between South and North Korea.

The survey shows that seven out of ten responded that the Geumgang-san Tour should be immediately resumed, as it is the icon of the promotion of understanding of one another, reconciliation, and peace between South and North Korea. Age group of 40s and above and politically progressive people (78.1%) supported this idea more than the conservatives (61.8%). Compared with a similar survey conducted in 2009, one year after the Tour was suspended, the respondents who agreed that Geumgang-san Tour Project is the icon of the promotion of understanding of one another, reconciliation, and peace between South and North Korea increased from 69.2% to 75.2%; this seems to support the idea that the recognition of the significance of Geumgang-san Tour Project has grown as time goes on.

< The Resumption of Geumgang-san Tour Project >



Source: HRI

< The Significance of Geumgang-san Tour Project >

The Significance of Geumgang-san Tour Project	2009.7	2012.7
1. An ordinary Sightseeing Product	30.8%	24.8%
2. The catalyst for the promotion of understanding between the South and North Korea	34.9%	39.1%
3. Symbol of reconciliation, and peace between S and N Korea	34.3%	36.1%

Source: HRI

Desire to join the Tour high when resumed, although it may take time.

The number of respondents who are willing (46.6%) to visit Geumgang-san is higher than those opposing (32.8%). Particularly, among the respondents willing to visit Geumgang-san, the number of people who have already been to Geumgang-san before (50.7%) is higher than who have not yet (46.3%). The survey also shows that as many as 78.3% think there is little chance for the Tour to be resumed within the office term of the present government, reflecting the disappointing sentiment about the prolonged suspension.

< Willing to visit Geumgang-san when resumed >

Willing to visit when resumed	Total	Have been to before	
		yes	no
1. very willing	16.6%	26.1%	15.9%
2. willing	30.0%	24.6%	30.4%
3. half and half	20.6%	10.1%	21.4%
4. not willing	17.0%	23.2%	16.6%
5. not at all	15.8%	15.9%	15.7%

Source: HRI

< Possibility of resumption within the office term of the present government >

Possibility of resumption within the office term of the present government	Total
1. very high	0.6%
2. high	3.2%
3. half and half	17.9%
4. low	34.2%
5. very low	44.1%

Source: HRI

High ‘yes’ to the idea of resuming Gaeseong Tour Project to begin with.

Six out of ten respondents (58.8%) think it is first necessary to resume Gaeseong Tour Project prior to Geumgang-san. The older the age group, the higher ‘yes’ response. Gaeseong Tour being smaller in scale and located near the well progressing Gaeseong Industrial Complex, the respondents appear to be of the opinion that Gaeseong Tour is easier to resume than Geumgang-san Tour.

< Necessity to resume the Gaeseong Tour as first step >

Necessity to resume the Gaeseong Tour to begin with	Total	Age group			
		20s	30s	40s	50s & above
1. necessary	58.8%	53.9%	55.5%	59.5%	66.5%
2. not necessary	41.2%	46.1%	44.5%	40.5%	33.5%

Source: HRI

Majority of people voice for flexible policies toward the North

Majority of people expressed their discontent with the present government’s policy toward the North, and showed negative view of the prospect of two Korea’s relationship for 2013, and called for shift to more flexible policy. With regard to the assessment of the government’s policy toward the North, only 13.8% said ‘happy’, whereas 44.5% ‘not happy’ and 41.8% ‘mediocre’. Most of the respondents (82.4%) were pessimistic about the prospect of inter-Korea’s relationship for 2013 with 59.2% saying ‘similar to what it has been’ and 23.2% ‘will deteriorate’. Seven or eight out of ten (75.4%) called for a policy shift for more flexibility.

< Present government’ policy toward the North >

Presentgovernment’ policy toward the North	Total
1. very happy	2.8%
2. happy	11.0%
3. mediocre	41.8%
4. not happy	27.4%
5. not happy at all	17.1%

Source: HRI

< Prospect of inter-Korea’s relationship for 2013 >

Prospect of inter-Korea’s relationship for 2013	Total
1. will improve	15.9%
2. same as before	59.2%
3. will deteriorate	23.2%
4. don’t know	1.6%

Source: HRI

< Ideal next government’s policy toward the North >

Ideal next government’s policy toward the North	Total
1. total review	9.9%
2. more flexible policy	65.9%
3. maintain present policy	24.2%

Source: HRI

To improve the relationship between South and North Korea, the following policies are suggested.

1. Policy shift for more flexibility is needed to improve the inter-Koreas relationship and the stability of the Korean peninsula, which should be proposed to the North in the Presidential address to be made in a forward-looking manner on Independence Day, Aug 15th.
2. Geumgang-san Tour Project is a symbol of the starting point to reinstate the South and North Korea relationship and expand economic cooperation between the two Koreas. The government should continue to endeavor to resume talks with the North for the re-opening of Geumgang-san Tour, while trying to organize reunion events for the families separated across South and North Korea, taking this coming Chuseok (a traditional national holiday for both the South and the North) as a good opportunity for reconciliation.
3. If Geumgang-san Tour is not to be resumed in the near future, Gaeseong Tour should be resumed to begin with, as it is much smaller in scale than Geumgang-san Tour and located near the well progressing Gaeseong Industrial Complex.

[Annex] Domestic and Global Economic Indices

Domestic/Global Growth Rate

Category	2010					2011					2012
	Annual	1/4	2/4	3/4	4/4	Annual	1/4	2/4	3/4	4/4	Annual(E)
US	3.0	3.9	3.7	2.5	2.3	1.7	0.4	1.3	1.8	3.0	2.1
Euro Region	1.9	0.4	1.0	0.4	0.3	1.4	0.8	0.2	0.1	-0.3	-0.3
Japan	4.4	6.1	5.2	2.3	-0.6	-0.9	-6.8	-1.5	7.0	-2.3	2.0
China	10.3	11.9	11.1	10.6	9.8	9.2	9.7	9.5	9.1	8.9	8.2
Korea	6.3	8.7	7.6	4.5	4.9	3.6	4.2	3.5	3.6	3.3	4.0

Note: 1) IMF figures of April 2012 for 2012 global projections; Hyundai Research Institute figures for Korean projections.

2) Annual rates were compared with those of previous term for the US and Japan, with the rates of the previous term for Euro region, and with the same term in the previous year for China and Korea.

International Finance Index

Category		End of 2010	2011		2012		Compared with previous day
			End of Jun	End of Dec	Aug 1	Aug 2	
overseas	Ten-year Treasury Bond Interest (%)	3.30	3.16	1.88	1.52	1.48	-0.04 %p
	JPY/USD	81.19	80.66	77.66	78.41	78.25	-0.16 ¥
	USD/EURO	1.3350	1.4492	1.2955	1.2237	1.2180	-0.0057 \$
	DJIA(p)	11,578	12,414	12,218	12,938	12,824	-114 p
	Nikkei(p)	10,229	9,817	8,455	8,650	8,510	-140 p
Domestic	Three-year Government Bond Interest Rate (%)	3.38	3.76	3.34	2.83	2.79	-0.04 %p
	KRW/USD(KRW)	1,134.8	1,067.7	1,151.8	1126.5	1131.7	5.2 KRW
	KOSPI(p)	2,051.0	2,100.7	1,825.7	1,879.9	1,869.4	-10.5 p

International Raw Materials Price Index

Category		End of 2010	2011		2012		Compared with previous day
			End of Jun	End of Dec	Aug 1	Aug 2	
International Oil Prices	WTI	91.40	95.18	99.22	88.86	87.14	-1.72 \$
	Dubai	88.80	106.75	104.89	101.04	101.73	0.69 \$
CRB Future Indices		332.80	338.05	305.30	299.23	294.50	-4.73 p

Note: The CRB index is calculated by giving the same weight to the prices of a total of 19 major commodities including grains, crude oil, industrial raw materials, and precious metals. The index is widely acknowledged as an international standard for the price of raw materials.