

# Monthly Economic Review

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[Annex] Domestic and Global Economic Indices

## **I. Recent Global & Domestic Economic Trends**

### **Major Economies**

*The US and Japan's economy shows a slow recovery, China maintains good growth, though not as good as used to, while EU still remains in economic recession*

The US shows a healthy state of economy with its ISM manufacturing index rising from 53.4(Mar. 2012) to 54.8(Apr. 2012), staying above the critical line 50. The unemployment rate improved to 8.2% in March, the lowest so far since January 2009 when it recorded 7.8%. However, the continuing slump of the real estate market, which is the main sector of capital income, and an increasing number of people giving up seeking employment present an optical illusion of unemployment rate.

EU's financial uncertainty has been eased to some extent with the provisional approval of the second bailout for Greece and second supply of long-term liquidity by the ECB. However, the absence of a fundamental solution for the financial crisis, the lack of confidence in Greece practicing its austerity budget, and a deteriorating Spanish financial environment still present several causes for concern.

Japan's economy, despite its export slump, shows sign of slow recovery thanks to the continuing upward tendency of industrial production and the expanding growth rate of retail sales.

China's PMI increased from 51.0(Feb. 2012) to 53.1(Mar. 2012), recording three consecutive months of upturn, enabling industrial production and retail sales to continue to grow.

### **Global Financial Market**

*Fluctuations of global share price and currency exchange rate has decreased, expecting the concern over EU's financial crisis would reduce.*

The DJIA maintained similar level in April to the previous month's despite the poor economic indicators of the US, expecting the concern over EU's financial crisis would be diminished. However, it dropped by 2.9% in May due to the concern over EU's financial crisis growing back. The DAX index of Germany was down by 12.7% in April with the rumor circulating of the possible downgrading of France's credit rating and dropped again in May by 4.2%. Nikkei index also fell in April by 5.6% due to the deteriorating business performance and dropped again in May by 5.0%. China's SSE composite index was up by 5.9% in April with the growing expectation for monetary policy easing, and rose again by 0.5% in May.

The JPY/USD exchange rate depreciated in April by 2.5% from the March closing rate with the expectation for the additional quantitative easing by the Bank of Japan, but appreciated in April by 2.5%, while EUR/USD exchange rate depreciated by 0.5% in April due to the concerns over the possible economic recession in the Euro zone and further depreciated by 1.9% in May owing to Spain's deteriorating fiscal health compared with the previous month's closing rate. The CNY/USD exchange rate was down by 0.1% in April due to the major Chinese companies' poor business performance of the first quarter, but was up in May by 0.03%.

## Economic indices of major countries

(Unit: %)

Economic Sectors		2011		2012		
		Annual	Dec	Jan	Feb	Mar
US	Industrial Production	4.1	0.9	0.7	0.0	0.0
	Retail Sales	7.7	0.3	1.5	1.0	0.8
EU	Industrial Production	3.5	-0.9	0.0	0.4	-
	Retail Sales	-0.6	-1.0	1.1	-0.1	-
Japan	Industrial Production	-3.5	2.3	0.9	-1.6	1.0
	Retail Sales	-1.2	0.7	3.1	2.0	-1.2
China	Industrial Production	13.7	12.8	-	11.4	11.9
	Retail Sales	17.1	18.1	-	14.7	15.2

(Unit : p, yen, euro, yuan)

Economic Sectors		2011	2012			
		Annual	Feb	Mar	Apr	May
US	DJIA	12,218	12,952	13,212	13,214	12,835
EU	DAX	5,898	6,856	6,947	6,761	6,475
	EUR/USD	0.772	0.743	0.752	0.755	0.770
Japan	NIKEI	8,455	9,723	10,084	9,521	9,045
	YEN/USD	77.66	80.51	82.41	80.35	79.87
China	SSE Composite Index	2,199	2,428	2,263	2,396	2,409
	CNY/USD	6.3190	6.2991	6.3058	6.3099	6.3079

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

### Korean Economy

*Despite signs of domestic recovery, Korean market is not making solid progress. Korean economy appears to show a weak recovery having passed through the trough thanks to the continuing trade surplus.*

The growth rates of retail sales and facility investment index shrank in a large scale, and construction turned into the red with the poor performance in building of residential houses, industrial plants and civil engineering sector.

The trade balance continued to remain in surplus although the export decreased by 4.7% compared with the same month of 2011, as the import was also down by 1.4% in the same month.

The unemployment rate fell in April, 2012 by 3.7% due to the rising number of people in their 20s and 50s being employed and increasing number of people employed in service industry. The consumer prices fell in April by 2.5% with the prices of agro-fishery, livestock and other industrial products falling.

BSI rose to 84 in March, to 85 in April, and to 90 in May showing upturn for four consecutive months. Composite leading index and cycle variation value marked 99.8 in March 2011, making it close to the critical line 100.

***The geo-political risk issues involving North Korea brought down the share prices and exchange rates depreciated in April. Interest on corporate debentures showed downward trend.***

KOSPI fell by 1.6% in April due to the geo-political risk involving N. Korea's rocket launching in April and the plummeting share prices of the businesses with poor performance in the first quarter of this year, and dropped again by 1.6% in May mainly because of stock sales by foreigners.

Despite the persistent concern over the possibility of Europe's financial crisis, the KRW/USD exchange rate appreciated by 0.3% in April with the sales of US dollars by export industries, but depreciated in May by 0.9%. The corporate bond yield rates (BBB-) rose by 0.05%p in April with expectation for a recovery of the domestic market, but fell by 0.14%p in May as the domestic stock market stayed weak.

**Korea's major economic indices**

(Unit: p, %)

Economic Sectors		2011					2012				
		Annual	1/4	2/4	3/4	4/4	1/4	Feb	Mar	Apr	May
Domestic Market	Retail Sales	<b>4.3</b>	5.4	5.7	4.7	1.9	1.9	5.4	<b>0.0</b>	-	-
	Facility Investment Index	<b>0.7</b>	5.4	5.7	-3.1	-4.7	9.0	23.8	<b>1.0</b>	-	-
	Construction	<b>-6.7</b>	-12.6	-6.6	-8.4	-0.5	-3.8	9.0	<b>-7.9</b>	-	-
Foreign Trade	Export Growth Rate	<b>19.0</b>	29.6	18.6	21.4	9.0	3.0	20.6	<b>-1.4</b>	<b>-4.7</b>	-
Employment/Prices	Unemployment Rate	<b>3.4</b>	4.2	3.4	3.1	2.9	3.8	4.2	<b>3.7</b>	-	-
	Consumer Prices	<b>4.0</b>	3.8	4.0	4.3	4.0	3.0	3.1	<b>2.6</b>	<b>2.5</b>	-
Finance	KOSPI	-	2,107	2,101	1,770	1,826	2,014	2,030	2,014	<b>1,982</b>	<b>1,950</b>
	KRW/USD	-	1,097	1,068	1,178	1,152	1,133	1,119	1,133	<b>1,130</b>	<b>1,140</b>
	Corporate Bond(BBB-)	-	10.58	10.38	10.24	10.01	10.06	10.01	10.06	<b>9.79</b>	<b>9.65</b>

## **II. Economic issues facing Korea**

### **□ Five positive signs for the recovery of export business**

#### **Current state of export business**

The recent export business shows a downturn due to the deteriorating foreign circumstances including the financial crisis in Europe. January 2012 recorded a trade deficit of US\$2.2 billions for the first time in two years. The export for March and April also recorded a negative growth rate of -1.4% and -4.7% respectively. The continuing downturn of export business is a cause for concern for lower growth rate and its impact on the whole economy of Korea, as export plays a pivotal role as a safety pin for the GDP and foreign exchange holding. Here we look into some positive sides home and abroad and propose policies for the recovery of export business.

#### **Positive Circumstances for the Recovery of Export Business**

##### **1. Economic recovery of advanced countries**

The composite leading indices of advanced countries and emerging countries both recently turned into upturn, predicting the recovery trend from the second quarter. The economic indicators of leading export countries also show slow recovery.

##### **2. Sustainable competitive edge of export industries**

The number of Korean export commodities enjoying the largest market share in the world increased to 131 items in 2010 from 49 in 2002, showing a continuing rise. Most of the export items with competitive edge including automobiles managed to maintain sales increase amid the global financial crisis.

##### **3. Recovery of IT-related export industries**

The export of IT-related products achieved a record-breaking performance in 2011 for the second consecutive year, showing more than twice as much as the average of the whole trade balance and therefore contributing to turning the trade balance in the black. Although the export circumstances turned unfavorable due to the European financial crisis and the softer prices of memory semiconductor products, the export is expected to increase with the prices of LCD panels and semiconductor products rising in the near future.

#### **4. Sharp increase of petrochemical products amid high oil prices**

The export volume of petrochemical products surged as the oil prices sharply increased. It is positioned as one of the major export items of Korea as of February 2012.

#### **5. Improvement of export circumstances through the FTA with the US concluded**

The FTA with the US has enabled Korea to equip with ever more competitive edge of export prices in the markets including the EU and ASEAN, raising hope for export growth. The strengthened government policies are also in place to support the export industries. The FTA with the US, the biggest single market, is particularly expected to boost the export of key export items including automobile, electric and electronic products, and textiles.

### **Proposal**

It is essential to keep on investing in R&D and to determine and cultivate emerging industries and highly value-added export items to enhance the competitive edge. The government policy to make most of the FTAs with the US and the EU should be expanded. It is also necessary to find new countries and regions with healthy economies and explore niche export markets with good understanding of its culture and characteristics. It is recommended to expand the export market of petrochemical products, intensify the monitoring of foreign exchange market, manage the risk of foreign currencies, and to enhance the competitive edge of export industries in preparation for the appreciation of KRW, as the fluctuations of oil prices and foreign exchange rate are anticipated to widen.

### **III. The North Korean Issues**

#### **□ Current state of the development of border area between N. Korea and China, and its ripple impact.**

Recently, cooperation between N. Korea and China is increasing to develop the border areas including Yalu river and Tuman river areas. China's investment in N. Korea in 2010 recorded 12.1 million US dollars, more than twice as much as 5.86 million dollars invested in 2009. China has already launched the development of Liaoning coastal economic belt in the basin of the Yalu river(2009~2020) and the construction of East railway(2006~2020) along with the ChangJitu development plan in its wish to secure an exit to the East Sea and a logistical base for the north-east Asia region. The coastal economic belt plan is to seek common wealth

in the coastal and the inland areas with six cities including Daren and Dandong as its pivotal point of economic development. East railway plan is to construct a railway of 1,389 km connecting Mudanjang of Heilung province through to Tunghwa of Jirin province and Daren of Liaoning province. N. Korea took a positive attitude toward the complex development of Rajin, Seonbong, and Hwanggeumpyung areas in its wish to get out of the economic difficulty brought about by the prolonged international isolation and the strained South-North Korean relationship by attracting as much foreign investment as possible. N. Korea designated Raseon as a special city to develop it as a hub for international cargo brokerage, processing export, finance, and tourism, and held a ground-breaking ceremony in Raseon and Hwanggeumpyung in June 2011. N. Korea is also planning to introduce a scheduled cruise vessel travelling from Hunchun ~ Raseon ~ Geumgang-san, having had a demonstration tour in September 2011.

### **Success chance of the development of the border area and its limitation**

The success chance of the development project of the border areas between N. Korea and china is relatively high compared with projects to develop Raseon and Shineuiju Special Zone launched in the past for the following three reasons:

1. Both China and N. Korea share the common ground of urgent need for developing the area, and therefore both are determined for the successful development.
2. N. Korea and China both have a strong central government which can make swift decisions with its own initiatives with no or little resistance from local governments or state-run companies.
3. The poor infrastructure for economic cooperation between N. Korea and China has now considerably improved with the increasing amount of investment from China and N. Korea's positive attitude for the development unlike its reluctant stance in the past.

It is, however, not without limitation. The ambiguity and uncertainty in the legal interpretation and system operation, stiff labor management, unstable political climate hanging over the Korean peninsula, reluctance to open to the rest of the world, and lack of policy credibility are causes for concern. N. Korea is therefore required to refer to the successful cases of economic reform achieved by Vietnam and Poland and make efforts to earn credibility from the international community by taking positive actions to introduce new policies to attract foreign investment: various tax benefit, guarantee of self-managed employment by investors, declaration for more positive reform and openness policies, and removal of non-economic causes for insecurity.



## Ripple Effect

The successful development of the border areas between N. Korea and China would bring a dual effect to Korean peninsula. Positive side is that it will prompt N. Korea to reform and open, which will in time lead N. Korea to build a good foundation for economic cooperation with foreign countries and foreign investment from private sectors. The improvement of logistic and industrial infrastructure will also enhance the chance for S. Korean businesses to participate in the Special Zone in N. Korea. On the other hand, the over-dependence of N. Korean economy on China and China's preemptive move to acquire concessions to develop N. Korea's underground resources are causes for concern, which may in due course result in China's influence on N. Korea's economy and politics increasing. Another negative aspect is that there is a possibility for China to use Rason harbor for military purpose, posing a threat to the security of the region.

## [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 Area	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-area, and with the same term in the previous year for China and Korea.

## International Finance Index

Category		End of 2010	2011 년		2012 년		
			End of Jun	End of Dec	May 7	May 8	Compared with previous day
Overseas	Ten-year Treasury Bond Interest (%)	3.30	3.16	1.88	1.87	1.84	-0.03%p
	JPY/USD	81.19	80.66	77.66	79.91	79.86	-0.05 ¥
	USD/EUR	1.3350	1.4492	1.2955	1.3058	1.2993	-0.0065\$
	DJIA(p)	11,578	12,414	12,218	13,009	12,932	-77p
Domestic	Nikkei(p)	10,229	9,817	8,455	9,119	9,182	63p
	Three-year Government Bond Interest Rate (%)	3.38	3.76	3.34	3.38	3.39	0.01%p
	KRW/USD (KRW)	1,134.8	1,067.7	1,151.8	1,138.5	1,135.6	-2.9 원
	KOSPI(p)	2,051.0	2,100.7	1,825.7	1,956.4	1,967.0	10.6p

## International Raw Materials Price Index

Category		2010 close	2011		2012		
			End of Jun	End of Dec	May 7	May 8	Compared with previous day
International Oil Prices	WTI	91.40	95.18	99.22	98.09	97.15	-0.94\$
	Dubai	88.80	106.75	104.89	109.24	108.97	-0.27\$
CRB Future Indices		332.80	338.05	305.30	297.46	295.13	-2.33p

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



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