

The 12th Central Banking Seminar

Opening Address

October 12, 2004

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Governor

The Bank of Korea

(Opening remarks)

Ladies and gentlemen,

Let me extend a hearty welcome to you, central bankers gathered from all over the world to attend the Bank of Korea's "Central Banking Seminar". I would like to extend my particular thanks to Mr. Stefan Schönberg, Head of International Relations Department in the Deutsche Bundesbank.

The Central Banking Seminar, now in its 12th year, is taking its place as a valued occasion for promoting interchange and cooperation among central bankers, and as a forum for the debate of common policy issues and the search for appropriate responses.

(Imbalances in the Global Economy)

The topic chosen for this seminar is "Current Global Imbalances and the Challenges for Central Banks".

Many experts point to the huge U.S. current account deficit as the most significant problem giving rise to imbalances in the global economy. The U.S. current account deficit rose fourfold from 136 billion dollars in 1997 to 530 billion dollars last year. And the ratio of the U.S. current account deficit to current GDP similarly increased from less than 2% in 1997 to more than 5% during the first half of this year. The greater part of the U.S.

current account deficit arises from its trade with Asian countries. These countries, in turn, mainly invest foreign reserves built up from their current account surpluses in the U.S. Treasury market.

Some take the optimistic view that this level of imbalance is sustainable, given the high productivity growth of the United States and its low risk premium along with the predominant position of the U.S. dollar in international financial markets. Others, however, say that the imbalance cannot be maintained because, in line with the increasing indebtedness of the United States, the burden of external interest payments will also be augmented.

Anyway, as the scale of the imbalance is constantly growing, the pessimistic view can only become more persuasive than the optimistic one.

(Measures to Adjust the Global Imbalance)

Should confidence in the U.S. dollar weaken as a result of the continual widening of the U.S. current account deficit, there is the possibility that the demand for U.S. dollar-denominated assets may decrease. This would bring about instability in international financial markets by leading to a weak U.S. dollar and pushing up interest rates in the United States.

In this respect, it is desirable that the global economic

imbalance represented by the large-scale U.S. current account deficit should be adjusted as soon as possible. Also, considering that this problem has become deep-rooted to some degree, the unilateral efforts of either the deficit country or the surplus countries will be inadequate. What will be essential is international understanding and cooperation.

First of all, the United States, whose current account is in huge deficit, should strive for fiscal tightening as well as the lifting of its private-sector savings ratio. In contrast, those countries with current account surpluses, generally Asian countries, should boost domestic consumption through structural reform as well as heightening the flexibility of their currencies' exchange rates.

If, however, these policy responses were to be put in place abruptly within a short period, it could give rise to various side-effects such as a slowdown of the U.S. economy and the shrinkage of Asian countries' exports. Therefore, these steps should be undertaken gradually, in line with the development of the global economy and the situation of international financial markets. At the present time, the institutional stability of the global economic system and the flexibility of international financial markets are much greater than before. Accordingly, provided the adjustment of the imbalance can be attained step by step with the close cooperation between countries, then, in my opinion, we are sure to overcome these adversities.

(Closing Remarks)

We, central bankers, therefore, should show wisdom of by preparing our winter coats before autumn fades. In this respect, I hope that this seminar will prove valuable opportunity to examine carefully problems that may arise and come up with specific countermeasures.

Besides this, I hope that it will be the chance for us to share experiences as to how the global economic imbalance has influenced individual countries and how they have responded to it. For example, though Korea has recently seen its exports increase sharply, domestic demand has been held back, because production is being moved to low-wage countries and employment opportunities are not growing enough to encourage private consumption. As a consequence, various imbalances have also been growing in the Korean economy including that between exports and domestic demand and that between export-oriented large companies and domestic demand-dependant SMEs. Accordingly, Korea is conducting macroeconomic policy to support the revival of domestic demand including the Bank of Korea's reduction of its policy rate this August and the government's expansion of fiscal spending. It also involves structural reforms such as the pursuit of industrial structure upgrading.

Ladies and gentlemen,

Although the schedule for this seminar is rather demanding, I hope that all participants will have the time to cultivate mutual friendships and to enjoy some aspects of Korean culture as well as the beauty of the autumnal mood.

In closing, I give my sincere thanks to all those involved in the preparations for this seminar and ask them to do their utmost throughout to make it a great success.