

## A CHALLENGE TO THE ALL-TIME HIGH

### *Stock Market Review*

The equity market reflects the strong growth of the Korean economy in the first half of this year. In spite of outstanding economic growth, the Korea Stock Price Index (KOSPI) had steadily fallen until it reached a yearly low at 847.09 on May 27. After the local elections on June 27, the KOSPI gradually recovered with the growing certainty about tight monetary control and with the additional 3 percentage (up to 15 percent) allowance of equities purchase by foreigners. On July 13, the KOSPI regained the 900 level, and reached 977.29, gaining 130 points, or 15.4 percent from the low of the year.

After climbing up to 977.29 points, however, the market faced massive selling pressure from short-term profit-taking. The profit-taking trimmed a rise in the market that was buoyed by the inflow of foreign capital into the stock market in early July. Institutional investors maintained their net selling position. Also, many individual investors stayed on the sidelines as a result of lack of direction.

The customers' deposits at brokerage houses were down from 2.9 trillion won in mid-July to 2.5 trillion won on August 19. As a result, stock prices drifted lower because of lack of incentive. The market showed a dramatic retreat to 908.01 points on August 19, battered by the rumor that a former president has 400 billion won in accounts opened under aliases.

The market rallied again during September, driven by high liquidity, a change in tax laws, and improved market sentiment about market prospects. The KOSPI, which began the month at 911.36, moved up to 1,010 point level gaining 11 percent. During the rally trading volume reached 50 to 60 million shares per day. Much of the buy-

ing came from individual investors, who poured approximately 400 billion won into the stock market. Customers' deposits at brokerage houses rose from 2.5 trillion won at the onset of the month to as high as almost 3.0 trillion won on September 20.

After such a rapid rise, the market settled into a profit-taking period. Even though there have been several attempts during October to challenge the previous high of 1012.29 points of September 21, it is unlikely that another rally will occur in November.

### *Economic Conditions of the Market*

The Korean economy has continued to grow strong this year, even stirring up the prospect of overheating. The nation's real or inflation adjusted gross domestic product (GDP) is predicted to increase by 8.9 percent this year. Listed companies whose fiscal year ends in December are estimated to have achieved a 21 percent growth in sales and a 37 percent increase in net earnings in the first half of the year. Despite this roaring economic growth, the trade and current account deficit widened in the first six months of the year and overshadowed the continued healthy growth of the nation's economy.

While the economy expands rapidly, inflation is slowing down. It is, therefore, unlikely that the government will intervene to contain the economic growth, noting that the growth rate of consumer spending, 5.8 percent, is lower than that of gross domestic product, 8.9 percent. Surprisingly enough, consumer prices for the first half of 1995 rose only by 4.3 percent over the same period last year, which is the lowest level since 1987. Accordingly, the nation's annual inflation is expected to be at the government's original goal

for this year. Overall, economic expansion will continue until early next year. Some slowdown in economic activity can be considered as normal adjustment. In addition, the economy is expected to have a soft landing next year with a 7.6 percent growth rate.

### *Supply of and Demand for Stocks*

At any given time, 'supply and demand' factors are important in explaining the Korean market situation. The Securities Supervisory Board (SSB) is monitoring the schedules of new listings and rights issues in the exchange to prevent the market from being flooded by an excessive number of issues at a particular time. If we look at the number of issues to reach the market during the second half, it is encouraging that the volume of new issues will decrease to about 6.4 trillion won in value from the original 8 to 10 trillion won.

As we can see in the table, 60 percent of the expected new issues, approximately 3.9 trillion won in value, were supplied in the first half of this year. Out of about 2.5 trillion won to be issued in

the second half, seasoned issues account for 1.9 trillion won, which is down from 3.6 trillion won in the first half. On the other hand, the volume of unseasoned issues will increase from 1,301 billion won in value of 9 issues to 4,540 billion won. In addition, if the KOSPI exceeds 1,000 points, the SSB will allow Korea Telecom and two Hyundai companies to go public in the fourth quarter.

Demand for stocks for the second half of 1995 is expected to increase significantly compared with the first half of this year. Above all, the amount of money trust in commercial banks has increased about 30% (28 trillion won) from the previous year. At least 5% of the increased fund, 1.4 trillion won, is available to purchase stocks during the second half of 1995. Thanks to successful sales of domestic closed-end funds and foreign beneficiaries, investment trust companies will have about 1 trillion won worth purchasable funds during the period. Also, the insurance companies' fund of 690 billion won and the brokerage houses' fund of 300 billion won with a total asset increase of 15 percent are expected to create additional demand in the market.

As a result, the total demand of institutional investors for stocks in the second half of this year

### Supply of New Stocks

(100 million won)

	First half of 95	Second half of 95	1995 total
Seasoned issues	36,131	19,000	55,131
Unseasoned issues	1,301	4,540	5,841
Others*	1,300	1,800	3,100
Total	38,732	25,340	64,072

\* Others include the sale of the equity stake in public corporations held by the government and seasoned issues at the over-the-counter market.

is estimated to reach 3.01 trillion won. As we can see from the supply and demand analysis above, it is encouraging that the combined value of these new listings and rights issues is less than the estimated demand for investment in the second half.

### *Market Outlook*

The Korean economy will be in the expansion phase through the year with the peak in the first half of next year. The yearly growth rate of GDP in 1995 is likely to reach around 8.9 percent. With a low inflation rate, it is anticipated that the booming Korean economy will move into a soft-landing phase without high unemployment rates or an abrupt drop in aggregate demand. Corporate earnings are rising rapidly and the price to earnings ratios (PERs) are at the lowest level for the last seven years. Thus, the stock market would catch up to the strong growth of the Korean economy in the fourth quarter of this year.

One of the most important factors that influenced the market has been the interest rate level. Market interest rates have been stable at a low 12 percent level since August, due to decreased corporate investment demand and abundant liquidity provided by brisk foreign trade. Also, ample funds which flowed into securities firms after the lifting of the stock investment ceiling for foreigners helped to lower the market interest rates. Not surprisingly, the yield on three-year corporate bonds dropped to 12.10 percent on October 21 from 13.90 percent on August 1.

Recently, both money-market and long-term interest rates showed a strong downward trend, reflecting abundant liquidity in the near future. There has been high correlation between declining interest rates and a rising stock market in Korea. The 12 percent level was the prevailing interest rate when the equity market was very strong in 1993 and 1994.

In addition to falling interest rates, the enforce-

ment of the real name system for real estate transactions, the expected imposition of global taxation on financial income scheduled to begin January 1996, restructuring of the domestic securities industry, and economic cooperation between the North and South are other incentives for stock price recovery. Most importantly, the implementation of global taxation on financial income will likely shift as much as 6 trillion won to the stock market.

Another time-honored sign favoring the continued upward movement of the market is the recent rise in individual investors' deposits at securities companies. The deposits of 3 trillion won suggests that individual investors, who still account for 65 percent to 70 percent of daily trading, are prepared to invest more in shares in the near future. In addition, foreign investment funds are expected to flow continuously into rapidly growing markets including Korea's.

Overall, an upbeat movement will emerge in the fourth quarter. The KOSPI is more likely to challenge the long-awaited 1,100 point milestone some time in late November, possibly breaking the all time high of 1,145.01 on November 9, 1994.

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