

ECONOMIC SOFT-LANDING LOOKING GOOD

Modest Decline in Industrial Output Growth

Korea's industrial output grew 8.2 percent in February from a year ago, following a 12.4 percent growth in January. Thus for the first two months, output increased at a 10.3 percent annual rate, down compared to the 14.1 percent growth over the same two-month period last year, but up from the 7.4 percent for the Nov.-Dec. period of last year. The increase in output in February is attributed to the brisk production of heavy-chemical goods such as semiconductors, automobiles and machinery.

However, the output gap between the booming heavy-chemical sector and the sluggish light industries further widened in February. Statistics showed that the output of the heavy-chemical industries increased 11.2 percent, while the output of light industries decreased 3.4 percent.

Boosted by brisk production, the average capac-

ity utilization rate of the manufacturing sector rose to 83.4 percent in February, up from the 80.9 percent of a year ago and the 82.2 percent in January. In contrast, business inventories increased 18.7 percent in February, up from the 3.6 percent a year ago and the 16.2 percent in January.

Orders for domestically manufactured machinery only increased 6 percent in February from a year ago, a sharp decline from the 34.3 percent jump in January. Imports of machinery rose 7.1 percent in February from a year ago, compared to the 45 percent surge in January. However, the categories of consumption in February indicated a steadily increasing trend compared to the growth rates of January.

Overall, the economy is likely to avoid a sharp decline and will grow around 7.2 percent this year. In other words, recent national economic indicators show that the likelihood is high that the economy will make a soft-landing if the current high-cost and low-efficiency industrial structure continues to improve and gains a competitive edge in

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<Recent Industrial Activities>

		(year-to-year change, %)					
		1995			1996		
		Jan.	Feb.	Jan.-Feb.	Jan.	Feb.	Jan.-Feb.
Output	Output	9.2	19.8	14.1	12.4	8.2	10.3
	Heavy-Chemical Sector	12.6	23.5	17.7	15.0	11.2	13.1
	Light Sector	-0.4	10.2	4.5	2.7	-3.4	-0.3
Consumption	Inventories	3.9	3.6	3.6	16.2	18.7	18.7
	Capacity Utilization Rate	85.1	80.9	83.0	82.2	83.4	82.8
	Wholesale & Retail Sales	11.2	6.8	10.0	5.3	11.9	8.4
Investment	Shipment of Consumer Goods	11.9	16.8	14.4	6.2	6.3	6.3
	Domestically-Made Machinery Orders	35.8	58.8	47.0	34.3	6.0	19.4
	Imports of Machinery	22.2	68.4	43.3	45.0	7.1	24.6

Source: National Statistical Office

the face of ever-intensifying international competition.

Declining Interest Rates

The March inflation rate of 0.8 percent was lower than January's 0.9% but higher than February's 0.4%. The 3.4 percent monthly rise in public service charges and 1.3 percent monthly rise in individual service charges led to increases in consumer prices. However, the prices of agricultural, fisheries and livestock products only increased 0.5 percent from February. Consumer prices rose 2.2 percent during the first quarter of this year. Given this quarterly inflation rate, it is not easy to say now whether the Government will be able to accomplish its annual inflation target of 4.5 percent.

Recently both short- and long-term interest rates have been continuing their downward trend, reflecting sufficient liquidity in the domestic financial market. The parliamentary elections did not particularly affect interest rates or cause them to fluctuate.

The yields on both 91-day certificates of deposit, a benchmark short-term interest rate, and on three-year corporate bonds, a benchmark long-term interest rate, have maintained downward trends. Due to stable market interest rates, the central bank has had plenty of room to maneuver in managing the money supply.


The Bank of Korea announced that annual M2 growth rate, which has been stable since last September, was set within the 11.5~15.5 percent range. However, despite stable market interest rates, the Bank of Korea should carefully watch the inflow of foreign capital in carrying out its monetary policy.

Trade Deficit Worrisome

Even though the first-quarter trade deficit is down 11.6 percentage points from last year's deficit of the same period, the deficit of \$3.8 Bil., calculated on a customs-cleared basis, accounts for more than half of the \$7 Bil. deficit target set by the Government early this year. In the first quarter, exports rose 21.5 percent to \$31.8 Bil. while imports outpaced earlier projections and rose 16.7 percent to \$35.6 Bil. As seen in the table below, exports grew faster than imports during this period.

Trading patterns have shown a disturbing trend in that exports were led by heavy and chemical goods to developing countries, while exports of light industry goods and those to developed countries have remained sluggish.

In addition to these trading patterns, the yen factor and money market situation threaten to help widen the trade deficit. The yen-dollar rate, which has a crucial impact on Korea's trade, indicates that Korean products will lose price competitiveness in the international market. Since the end of 1995, the yen has depreciated about 3 percent against the dollar, while the won has only depreciated 1 percent.

Another cause of concern is the expected injection of foreign capital resulting from the opening of Korea's capital markets via measures such as the expansion of the foreign stock ownership ceiling on April 1 from 15% to 18%. The influx of foreign funds into the money market will lead to the won's appreciation, which would hurt exports by making Korean goods more expensive overseas. Thus, many economists are proposing that the timetable for opening the Korean capital markets be determined flexibly, taking into consideration the won-dollar exchange rate. 

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