

WILL THE KOREAN STOCK MARKET BE STRONG AT YEAR-END?

KOSPI Falls to Three-year Low

The Korea Stock Price Index (KOSPI) fell to a three-year low of 729.53 points on November 11th due to a dismal investor sentiment caused by the prosecution's anticorruption drive unveiled over the past couple of weeks prompted by scandals concerning the previous Minister of Defense and city officials combined with pessimism about the future market situation. However, there was a reprieve in mid-month with a technical rebound backed by market-boosting measures by the government. These included: (1) an additional 200 billion won of liquidity financing for security houses to use as marginal loans; (2) provisions of short-term call money loans amounting to 500 billion won to non-banking financial institutions such as security houses to alleviate funding shortages; (3) negotiations with related ministries and appropriate changes in statutes to allow pension funds to expand investment into the stock market; and (4) the allowance of the right to issue \$200 million to Korea Funds as early as the first quarter of 1997.

There are many factors contributing to the fluctuation of the Korean stock market. First of all, there has been an excessive amount of margin loans, reaching up to 2.9 trillion won. The Korean stock market has been suffering severely due to the recent excessive margin loan positions. With margin loans still excessive, especially in comparison with the bleak customer deposits, which had fallen below 2.6 trillion won, the possibility of the KOSPI rebounding may be limited unless a strong trend towards improving the margin positions occurs. Although some security houses extended the maturity on margin loans on November 16th,

the margin position will not decline within a short-term period. The other factors in the market concern the movement of interest rates and its effect on the KOSPI. The Korean government is adamant about lowering market interest rates to the level of other developed nations. In order to achieve this, it announced two cuts in the reserve ratio requirement at commercial banks. As a result, banks and other financial institutions have cut lending and deposit rates. However, the market interest rates have not shown the kind of elasticity hoped for by the government. The representative 3-year corporate bond yield has continued to hover at the 12-percent level and the one-day call rate has reached the 14-percent level.

No Uptrend in December

Generally, the prevalent view is that the Korean stock market became bullish because many investors wanted to have dividend incomes. It is not expected, however, to be bullish at the end of this year. It will be a box trading of 720~750 points amidst a slightly bearish mood. The primary reason is that the big investors want to evade taxes on unearned income. They will yield a dividend if they still have stocks by the year-end, so they will sell their shares by December of this year. Therefore, demand will be weak in the Korean stock market, producing no major turnaround.

Technically, there was already a warning sign when the daily moving average experienced a downturn from 25 to 75 in mid-month, indicating that the atmosphere in the KOSPI will not be bullish in the near future. **VIP**

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