Letter from the Editor

The Korean economy is still mired in a slump. Once again, exports decreased, dropping 4.9% in February compared to the same period last year, and the trade deficit remained a hefty $2.11 billion in February, although both of these were a slight improvement over January's figures (8.2% and $3.48 billion, respectively). Despite the revision of the controversial labor bill, labor-management relations still remain uneasy, as witnessed by the brief one-day strike by bus drivers in late March.

To address this worrisome situation, the Kim Young Sam Administration has announced that it will provide some policy prescriptions to soothe the ailing economy. Everyone, including the opposition, agrees on the need for economic recovery; the economy cannot remain bogged down by the political fallout of the Hanbo scandal.

The area of greatest concern is the financial sector. The bankruptcies of the Hanbo and Sammi Groups has weakened Korea's credit worthiness in the international financial market. The won continues to depreciate in spite of the Bank of Korea's efforts to stem the tide, and the KOSPI stock market index dipped to below 620 before bouncing back up to the 650-660 range at the end of March. Foreign investors are somewhat hesitant to invest capital in the Korean market and seem worried about Korean firms' debt servicing capacity.

Some are predicting that the current recession will bottom out in the second or third quarter of this year, in accordance with classical business cycle theory. Others, though, feel that the reasons for the economic stagnation are more structural than cyclical in nature, citing the high-cost/low-efficiency industrial structure and the over-dependence on a few select export items and examples. Thus, they predict that the malaise may even last into next year.

The Korean economy's fate will be determined by three factors: the government's policy measures labor management relations, and the political situation, especially since this a presidential election year. Given the fact that everyone seems to realize the importance of reviving Korea's economic competitiveness, overcoming the present difficulties is clearly a task within our ability.

The new Minister of Finance and Economy, Kang Kyong-shik, recently announced that in 1997, the Government would place top priority on curbing the current account deficit and keeping inflation down, even at the expense of reduced economic growth. Toward this end, inflation will be kept between 4 to 4.5%, while the GDP growth rate target was lowered to 5 to 6%. Tax revenues will be decreased, and government spending will be tightened, with the budget increasing by only 9%. Financial liberalization and efficient energy consumption will also be emphasized.

In this month's issue of the *VIP Economic Report,* we take a detailed look at dealing with the current account deficit, highlighted in the Korean media as perhaps the biggest symptom of Korea's present economic woes. In the **VIP Forum** section, we examine foreign exchange risk management, an extremely pertinent topic given the rapid depreciation of the Korean won and the effect this is having on the other aspects of the Korean economy. In our **Industry Analysis,** we take a look at cost strategies of Korean auto makers. Changes in the global auto industry are demanding that Korean companies adopt new strategies to remain competitive.

Some are worrying that Korea might experience a Mexico-style financial crisis. In truth the situations are totally different if one looks at their economic histories and industrial compositions. It is true that slowing down from double-digit to single-digit growth has had a psychological impact on the Korean economy and the latest economic data may not seem too promising. However, the current recession can be seen in a positive light in that such a recession is needed to streamline the Korean economy and make it more efficient. If Korea is able to overcome the current troubles without too much cost, then it will become a nation truly worthy of its OECD membership. VIP