

THE EXCESS DEMAND OF DOLLARS IS TEMPORARY

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Demand and Supply of the Greenback

The Korean Won moved in the 1,330~1,350 won/dollar range in early September. However, by the end of September, the exchange rate had moved up to about 1,400 won/dollar because of the excess demand of the greenback by chaebols and financial institutions to repay their foreign debts and also the decrease in the inflow of foreign funds due to the uncertain economic situation.

The preliminary figure for Korea's total external liabilities aggregated by the Bank of Korea reached \$152.3 billion as of the end of July 1998. This figure for July showed a decrease of \$1.5 billion compared to the corresponding period last month. Long-term liabilities fell by \$1.6 billion, mainly due to the reimbursement of long-term debts by financial institutions, whereas short-term liabilities remained almost unchanged. As a result, the ratio of short-term liabilities to total external liabilities increased slightly from 24.9% as of the end of June 1998 to 25.2% as of the end of July 1998. A similar redemption of long-term external liabilities by financial institutions is scheduled for October as well. In particular, on Oct. 8, the interest on foreign debt some financial institutions will have to repay will amount to \$0.9 billion. The five financial institutions which acquired the five failing banks need more dollars to pay back the bad banks' foreign debt. At the same time, the chaebols and other firms also need dollars to repay their foreign debt.

Second, the inflow of foreign funds has decreased with a reduction in both foreign direct and indirect investment. Despite desperate efforts by both the government and private

sector to lure foreign direct investment, foreign investors are still maintaining a wait-and-see attitude because of the worries about the delay of corporate and financial restructuring. Direct investment in Korea by foreigners declined 18.7 percent to \$4.1 billion during the first eight months of this year. After averaging \$630 million per month in the second quarter and rising to \$1.24 billion in July, foreign investment sharply fell to \$407 million in August.

Excess Demand is Temporary

The excess demand of dollars will be temporary. The recent excess demand was largely caused by the demand for the repayment of foreign debt, not the current account deficit. Although the growth rate of exports has decreased, the current account is still recording a surplus. And the ratio of Korea's external short-term liabilities is at low level, standing at about 25% (\$38.4 bil) compared with 44.3% (\$68.4 bil) at the end of 1997. From a long-term outlook, Korea will have no problem in repaying its external debts considering the current account surplus, the inflow of foreign funds from the sales of corporate assets and the scheduled IMF bailout funds. However, in the short-term, the excess demand of the greenback will continue as corporate and financial restructuring progresses. The Korean Won will continue to move in the 1,350~1,400 won/dollar range in October. The foreign exchange rate will stay high until the uncertainties of the economic situation stemming from the prolonged restructuring are reduced. **VIP**

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