

EXCHANGE RATE WILL RISE WITH YEN'S DEPRECIATION

by Hee-Sik Jeong  
(e-mail:hsjeong@hri.co.kr)

*Won/dollar Rate Rising with Yen's Depreciation*

*"From the experience in the last month, market participants have learned that the government or the BOK is willingly intervening in the market, even indirectly, whenever they feel this kind of move is necessary to protect Korean exports' price competitiveness."*

Since its stable movements within the range between 1,170 won and 1,180 won per dollar as of mid-February, the won/dollar rate has sharply risen above 1,200 won because of yen's abrupt depreciation at the end of the lunar new year holidays. Entering March, the won/dollar rate further moved up to 1,240 won due to the yen's further depreciation and the indirect intervention of the government. It seems that the won/dollar rate is moving along the movements of yen/dollar rate. This is contrary to the previous year's situation, when the won/dollar rate was determined largely by the supply and demand in the exchange market.

Originally, it was expected that the oversupply situation in the foreign exchange market would lead to a stable downward movement in the won/dollar rate throughout the year. However, from the experience in the last month, market participants have learned that the government or the BOK is willingly intervening in the market, even indirectly, whenever they feel this kind of move is necessary to protect Korean exports' price competitiveness. More specifically, it has become widely recognized in the market that 1,000 won per 100 yen is the psychological Maginot line for the policy-

makers. In fact, the won/100yen rate momentarily declined to 990 won in mid-February, but has stabilized in the 1,000~1,020 range at present.

*Exchange Rate Will Bounce up to 1,250*

It seems likely that the exchange rate will bounce up to 1,250. In particular, there are several reasons to expect downward rigidity or upward movement of the won/dollar rate for the time being. These include: the continuously weak yen and ensuing intervention by the Korean government, the shrinking trade account surplus, and the strong U.S. economy, among others. In March, the Japanese government is expected to continuously lower interest rates to support the economy; this will result in the yen's depreciation and accordingly, the won's depreciation. As the prospect of Korea's exports in coming months is not so bright, the trade surplus will decrease compared to last year's statistics. In addition, during the first half of this year, the U.S. economy will not show symptoms of decline, supporting a strong dollar. A rational expectation behavior in the financial market might reinforce the downward rigidity of the won/dollar rate, as well. Anticipating a weak won in coming months, short-term foreign capital inflows into Korean financial market may moderately decrease. **VIP**

<Table> Won/dollar Exchange Rate and Forecasts *(end of period, won)*

Won/dollar	1997	1998	1999			
			Feb	Mar(p)	1st half(p)	2nd half(p)
	1,415.2	1,204.0	1,223.0	1,250	1,300	1,150