

MODERATE INFLATIONARY PRESSURE SEEN AMID ECONOMIC RECOVERY

Seungmyung Lee
(reoon@hri.co.kr)

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The economic recovery in Korea has been stronger than expected. Korea's GDP(Gross Domestic Product) soared 10.7% last year, which was the highest growth since 1987. The characteristics of last year's economy can be summarized as follows.

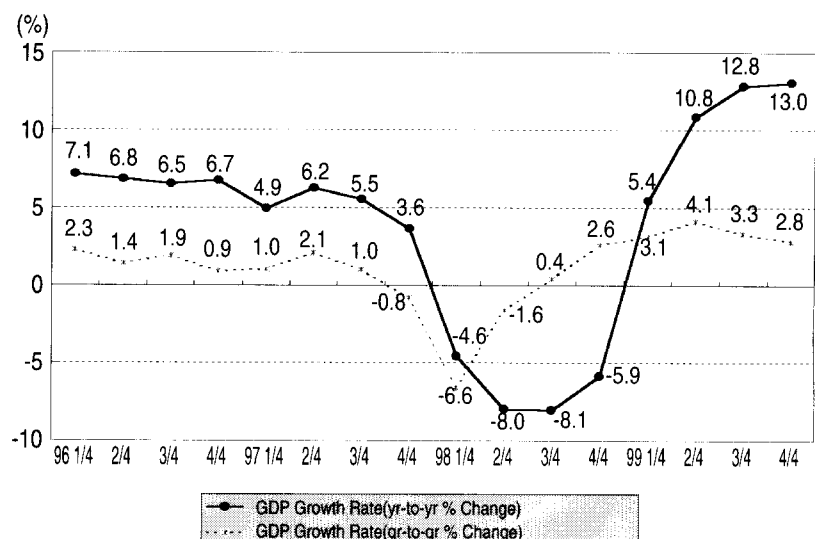
First, the recovery was boosted by a conspicuous rise in domestic demand and export. The main drivers of growth included a 10.3% rise in private consumption and 8.6% surge in exports.

Second, knowledge-based industries such as ICT (information and communications technology) played an important role in bringing about the impressive economic performance. Almost half of the economic growth can be attributed to the surge of the knowledge-based economy including ICT.

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Third, the vigorous economic growth was achieved amid stable price levels. There has not been much sign of inflationary pressure, despite the country's remarkable economic growth and decreasing unemployment rate over most of the year. It is of course too early to judge whether a low and stable price level has been phased in. This may be more of a technical rebound from the price-hike of the

Figure 1. GDP Growth Rate (Quarterly)



previous year and the temporary drop in the won/dollar exchange rate rather than an ever-lasting situation.

This year's economy is expected to continue its expansion, and although the pace may be slower than last year, it is likely to be slightly over 8%. Consumption is likely to slow down but the primary engine of economic growth will be brisk exports and increasing investment. Rising wages and declining unemployment rates are likely to keep consumption on a moderate rising trend. However, external export conditions are likely to be favorable to Korea with the expected recovery of the EU, Southeast Asia and Japan, along with the probable soft-landing of the U.S. economy and the strong Japanese yen against the U.S. dollar.

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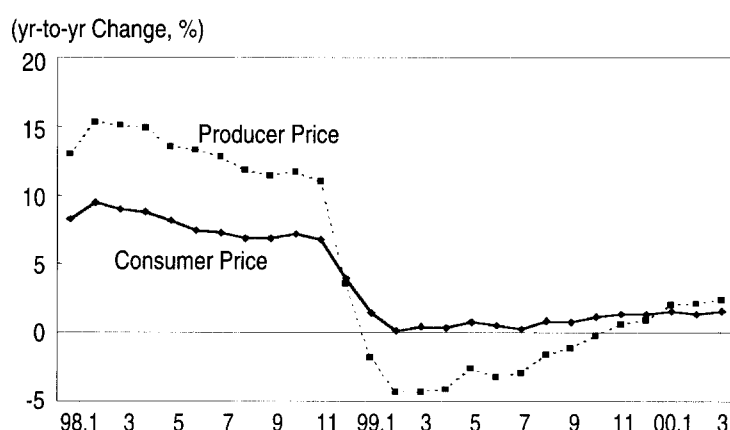
Another key area for growth will be investment. Facility investment is likely to continue last year's increase at double digit rates due to economic recovery and brisk exports. And construction investment will rebound to a rising trend as private housing construction demand picks up in line with the economic recovery.

Still, there are some downside risks for Korea on the horizon. A declining current account surplus, high oil prices, possible wage hikes, all pose threats to the Korean economy. Although February's current account surplus of \$790 million surpassed that of the previous month, it was still far short of last year's average monthly surplus of \$2.08 billion. Consumer prices posted only a slight increase of 0.3% in March from last month and 1.5% for the first quarter compared with the same period last year. The lack of inflationary pressure from demand-pull factors is likely to continue for the time being.

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It is expected that inflationary pressure will mount in the second half of 2000 in large part due to cost-push inflationary factors such as rising prices of international crude oil and raw materials as well as wage hikes. However, the declining won/dollar exchange rate will deter import prices from climbing and hence minimize inflationary

Figure 2. Price Level



pressure. And fortunately, OPEC (Organization of Petroleum Exporting Countries) agreed to supply the world with about 1.7 million barrels a day of additional oil, boosting output by about 7% above current levels of production along with some hope of oil price reduction. The agreement becomes effective April 1.

Some raise the concern that the continued economic growth rate is a sign of overheating that may fuel inflation. Despite the relatively high growth rate, it is too early to worry about an overheating economy, because the pace of economic growth has recently been slowing, and the economy still contains some slack. There are some sectors that are lagging behind, especially construction.

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Therefore, the government does not need to implement contractionary fiscal and monetary policy to cool down the economy for curbing inflation, but should maintain expansionary policy initiatives to continue the current trend of economic recovery, which is not considered too strong. **VIP**

Table 1. Korean Economic Forecast

Category	1999			2000(Estimated)			
	First Half	Second Half	Year	First Half	Second Half	Year	
National Account	GDP Growth Rate(%)	8.2	12.9	10.7	9.3	7.2	8.2
	Consumption(%)	6.9	10.1	8.5	6.8	6.4	6.6
	Private Consumption(%)	8.5	12.1	10.3	7.6	7.2	7.4
	Investment(%)	0.6	9.3	4.1	13.0	11.0	11.9
	Construction Inv.(%)	-10.8	-10.0	-10.3	7.6	7.5	7.5
	Facility Inv.(%)	24.8	51.9	38.0	21.3	16.5	18.7
External Transaction	Current Account(\$ bil)	12.5	12.5	25.0	4.6	5.7	10.3
	Trade Balance (\$ bil, Customs Basis)	11.7	12.3	23.9	3.3	4.9	8.2
	Export(\$ bil)	66.0	77.7	143.7	79.0	82.1	161.1
	(Increase Rate, %)	(-1.7)	(19.1)	(8.6)	(19.7)	(5.7)	(12.1)
	Import(\$ bil)	54.3	37.4	119.8	75.7	77.2	152.9
	(Increase Rate, %)	(15.1)	(42.0)	(28.4)	(39.3)	(18.0)	(27.7)
	Variable	Consumer Price(Avg, %)	0.6	1.0	0.8	2.0	4.4
Yield to Bonds(Avg, %)	8.0	9.6	8.8	10.0	11.0	10.5	
₩/\$ Exchange Rate(Avg)	1195	1183	1189	1100	1080	1090	
Unemployment Rate(Avg, %)	7.5	5.1	6.3	4.7	4.0	4.3	