

CONTRACTION IN DOMESTIC DEMAND AND SLOWDOWN OF EXPORT APPARENT

Macroeconomic Analysis Team

Industrial Activity

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Since the third quarter of last year, the Korean economy started to decline. Domestic demand factors such as the increase rate of consumption contracted, while investment also decreased. In December 2000, the growth rates of production and consumption declined significantly, and facility investment in particular fell for the second consecutive month.

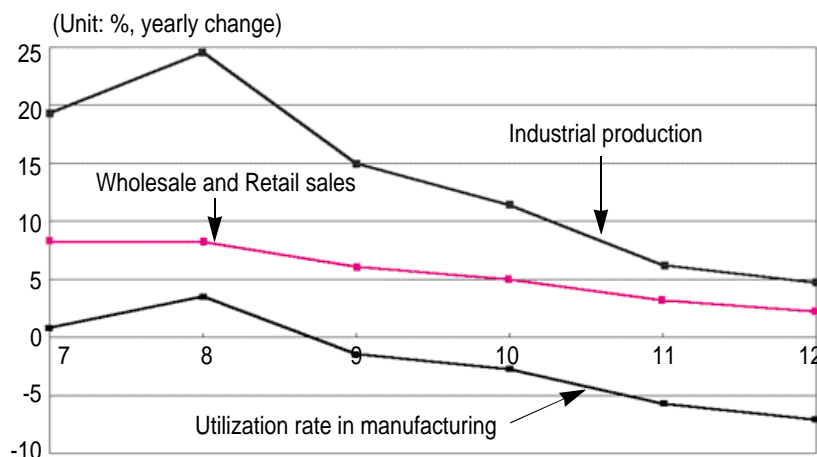
Industrial production decreased in sectors such as textiles, assembled metals, and autos, resulting in a 4.7% fall in the yearly growth rate. Although the growth rate of semiconductor and mechanical equipment production were relatively high, those of textile products (-12.7), assembled metals (-9.4%), and autos (-4.3%), fell.

The increase in wholesale and retail sales, which reflect consumption, fell to 2.2% compared to the same period last year. In the case of domestic consumption forwarding, the growth of durable consumption goods declined further, and even the growth rate of non-durable consumption goods fell 5.9% from the previous year.

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Meanwhile, in the investment sector, the growth rate of facility investment fell rapidly since the first quarter of 2000. In December, facility investment decreased 2.1% from the previous year, due to declines of investment in telecom equipment and

Figure 1. Trends in the Real Economy



transportation equipment. As a result, yearly growth of facility investment fell for two consecutive months since November 2000. In addition, construction investment showed no sign of recovery. The growth rate was similar to the previous year's at -0.1%, and construction orders grew slightly at 0.7% thanks to infrastructure investment.

With the overall contraction of industrial activity, the average utilization rate in manufacturing fell to 74.7%, a decline from 75.8% in November 2000.

External Transactions

In January 2001, exports increased and imports declined to result in a trade surplus of 0.32 billion dollars.

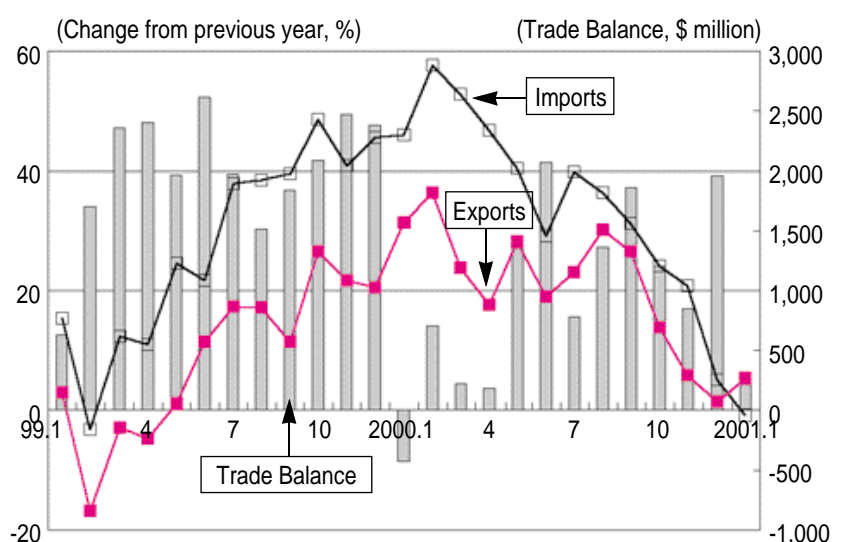
The increase rate of exports in the fourth quarter of 2000 was very low. November's rate was 5.6%, while December's rate was 1.4%, far lower than recorded in the third quarter or the fourth quarter of 1999. However, exports in January 2001 increased 5.2% year-over-year to reach 12.79 billion dollars, a record figure for the month. If we consider that exports were hindered by about 0.9 billion dollars because of the Lunar New Year holidays, it is thought that the real increase rate of exports could have reached 8%.

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Meanwhile, imports for January 2001 decreased by 1.0% from last year to record 12.47 billion dollars. This was the first import decline since February 1999. The reason for the decreased imports include the slowdown of the domestic economy and the decrease in import demand due to the holidays. In addition, oil prices have

Imports for January 2001 decreased by 1.0% from last year to record 12.47 billion dollars.

Figure 2. Exports, Imports, and Trade Balance



become relatively stable.

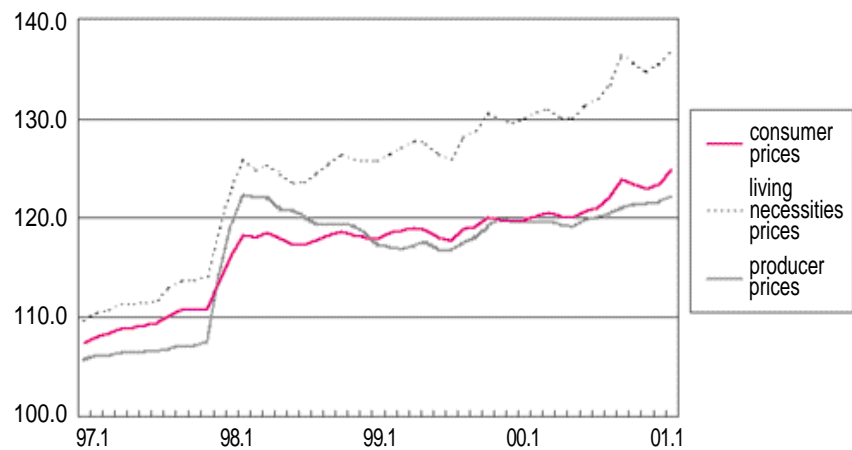
Price Level

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Due to hikes in agricultural goods and medical care charges, consumer prices in January rose 1.13% from December and 4.28% from the previous year. In particular, due to increased holiday demand and a cold spell, agricultural prices rose 2.8% from the previous year, contributing a 0.4% increase to consumer prices. Meanwhile, medical fees increased 9.9%, contributing 0.32% to consumer prices. The CPI for living necessities rose 0.9% from the previous month, and producer prices rose 0.5%.

However, such price increases were due to very special causes, and there is not much worry of inflation.

Figure 3. Key Price Trends (1995=100)



Implications

After the third quarter of 1999, the Korean economy entered a downturn, mainly because of the contraction in domestic demand.

After the third quarter of 1999, the Korean economy entered a downturn, mainly because of the contraction in domestic demand. Although the financial market seems to be recovering, consumer and investor sentiment are severely contracted. To bring a recovery in sentiment, economic restructuring should be completed to reduce uncertainty and improve policy credibility, financial market stability would ease corporate credit, and appropriate policies would improve consumer sentiment.

If such tasks are completed, the length as well as the severity of the economic downturn will be decreased. **VIP**