

## CONTINUING REFORM IN A CHANGING ENVIRONMENT

*The following is an excerpt from a speech by the Honorable Jin Nyum, Deputy Prime Minister & Minister of Finance and Economy made at the East Asia Economic Summit on October 30.*

My goal today is to update you on Korea's recent economic situation before and after the terrorist attack, and share with you our government's vision for future economic reforms.

Korea's reform strategy over the past four years has been to raise the efficiency of the economy through a comprehensive restructuring program and the fine-tuning of macroeconomic policies.

It is a fair assessment that the timely implementation of macroeconomic policies played a key role in attenuating the 1998 recession and laying a foundation for the recovery.

At the same time, Korea was able to make important headway in structural reforms.

However, the rapid recovery of 1999 and 2000 led to a sense of complacency, and public support for many tough initial reforms weakened shortly thereafter.

It was then that the "second economic team" led by me came in to add new momentum to the reforms by taking proper actions against non-viable companies and injecting additional public funds to accelerate the restructuring process.

Recently, our reform focus is shifted away from a downsizing-oriented restructuring to value-creating innovation. Reforms thus far have been past-oriented in nature: repairing the damage of past legacies. From now on, reforms will be future-based with long-term vision and strategy.

We are shifting gears from institution building to an establishment of a environment conducive to self-innovation and accountability.

We are also promoting a market-driven reform, breaking away from the state-led approach of the last four years. In other words, the reforms will be promoted by market forces with the government serving as a system manager or fair umpire.

Some of you may be wondering why the pace of the reforms seems to have slowed down lately. Well, in a situation where market disciplines are not fully working, unless the government intervenes in the process directly, the market-driven reform may take too long a time.

We should but be patient during the transition period until a well-functioning market system speeds up the changes in business practices and the mindset of the market participants.

### **Korea's reform: still on the right track**

Despite some skepticism, Korea's record on corporate restructuring does include a number of significant accomplishments.

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In the corporate sector, a half of the top 30 conglomerates have exited the market, proving “no firm is too big to fail. More recently, Daewoo Motors, one of the largest distressed firms, is about to be sold to a foreign buyer, thus significantly reducing uncertainties in the economy.

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Substantial progress has also been made to reform financial sector, through improving soundness and governance structure of financial and supervisory institutions.

However, our efforts to sell government-owned financial institutions have not borne fruit as of yet. It is rather regrettable that, after considerable preparations for the sale, appropriate partners could not be found. Also, sales negotiations will likely be delayed due to the deteriorating market environment. But, Korean government will continue to make earnest efforts to find appropriate buyers for those institutions.

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Now, let me say a few words about the Korean labor market situation. Despite a few remaining rigidities, labor market flexibility has improved. Over the last two years, the number of labor disputes has been reduced. Even when disputes arise, they are increasingly lawfully resolved without strikes. The peaceful resolution of labor disputes at the Korea Telecom is a prime example.

Reform efforts in public sector have focused on privatization and deregulation. So far, 6 out of the 11 largest state-owned enterprises have been privatized, and almost half of Korea’s business regulations have been abolished. In fact I would like to share with you one particularly encouraging story: Korea Tobacco and Ginseng Corporation successfully issued depository receipts (DR). I believe this sale demonstrates international investors’ confidence in the future of the public enterprises in Korea.

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### **Recent economic developments**

With the world economy slowing down, the Korean economy has also weakened since the fourth quarter of 2000. In particular, with the global demand for IT-related products shrinking, Korea’s exports have fallen since the second quarter of 2001.

Korea’s GDP growth rate, which recorded 8.8% last year, fell to 3.7% year-on-year in the first quarter of 2001, and further to 2.7% in the second. However, compared to other countries in the region, Korea’s GDP performance has been stronger with the exception of China and India.

The reason for this is simple: Korea still has a strong manufacturing industry such as automobile, steel, and shipbuilding sectors. Also, consumer sentiment has helped up so that the Korean economy is able to rely more on domestic demand.

For the rest of this year, the Korea’s GDP may slow down, but it is expected to stay in positive territory, generating an annual growth rate of about 2% for 2001.

As long as the war on terrorism remains somewhat contained and the stimulating effects of concerted policy efforts do materialize, the Korean economy is likely to recover toward the second half of next year.

### **Korea’s policy responses**

However, depending on the duration and severity of the war, the Korean economy could face a further downward pull by unfavorable external condition

already in place.

Considering this downside risk, the Korean government has been formulating and implementing a contingency plan for 3 scenarios based on low-, medium-, and high-impact repercussions of the war against terrorism.

Our basic strategy is to stimulate domestic demand to cushion the impact of falling exports, while maintaining a momentum for structural reforms. Our stimulus package includes four sets of policy measures.

First, we are implementing an expansionary fiscal policy by drafting first and second supplementary budgets of 5 and 2 trillion won, respectively which amounts to about 1.4% of the nation's GDP. The money will go to SOC-related projects and the housing industry. We are also planning a tax cut of about 0.4% of the GDP.

Second, to the extent inflationary pressures are controllable, we are providing monetary stimulus through a series of interest rate cuts and flexible liquidity. We are also taking various measures to stabilize the capital market.

Third, along with these macroeconomic policies, we are taking various measures to revive some of the economy's weaker sectors. For example, we are preparing increased tax and financial incentives for the service and construction industry. Tourism, logistics, and contents industries are expected to be the main beneficiaries.

Fourth, we are streamlining the regulatory system to create a more business-friendly environment. Along with its efforts to improve corporate governance and transparency, the government is deregulating cumbersome restrictions to enhance corporate competitiveness.

We hope these multi-pronged policy efforts will lead to job creation and more resilient domestic demand.

In these times of uncertainty, the anti-terrorist coalition of the international community has not only demonstrated resolve to protect humanitarian interests, but it is also a key to an early economic rebound.

The timely concerted efforts among the G-7 countries, such as cutting interest rates, increasing liquidity and expanding fiscal expenditure, will surely help stabilize the global economy.

Needed now are more concrete, effective measures to stimulate economic growth.

Policymakers should keep in mind the long-term benefits of free trade when tempted to implement trade protectionism in response to the economic shocks. We must aim to resolve issues of trade frictions through dialogue and understanding for a win-win situation, while governments and the private sector make joint efforts to avoid trade dispute altogether.

On a regional level, there is much we can do in terms of cooperation and coordination and aiding in global economic revitalization. Although leading economies like the U.S. will play a large role in pulling the world out of its economic slump, Asian countries can institute appropriate fiscal and monetary policies of their own and get the ball rolling.

In closing, I am confident that as long as we have a vision, a network of cooperation, and willingness to act, we can overcome these difficulties and pave the way for a brighter future for Asia. **VIP**

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