

POLICY AGENDA FOR KOREAN ECONOMY IN 2002

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Recent Economic Trends: Glimpse of an Economic Recovery

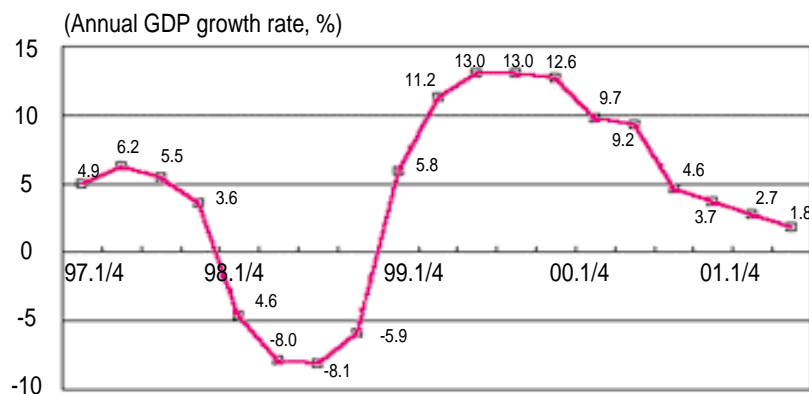
With GDP growth in the third quarter recording 1.8%, higher than the expected 0.5%, many analysts think that the economy may finally be passing its bottom. The cyclical index rose steadily from 96.4 in September to 96.7 in October, while the leading index rose 0.6%, the sixth consecutive month of improvement since May 2001. The slump in investment and exports moderated after the third quarter, while private consumption showed steady growth. The domestic stock market was bullish, and various psychological indicators, such as the consumer expectation index and the business sentiment index for manufacturers increased as well. These indicators support the view that the domestic economy may have bottomed out.

Although the economy seems to be passing its trough, it is still premature to declare a recovery. A U-shaped recovery is expected with growth accelerating by the

Many analysts think that the economy may finally be passing its bottom.

A U-shaped recovery is expected with growth accelerating by the end of the second quarter.

Figure 1. Recent GDP Growth Rates



end of the second quarter. Although some analysts think the trough was passed in the fourth quarter of 2001 and the economy is now ready for an upward trend, this forecast will have to be supported by January and February's figures for the US and Korean economies. With increasing hopes for an early recovery in the US, cautious forecasts are being made for a U-shaped trend in the Korean economy rather than an L-shaped long term recession.

Many observers believe that the world economy will recover from the second half of

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2002. There is a higher possibility for an upturn in the US, with stimulus policies showing some effect, and a recovery of consumption and investment sentiment due to decreased uncertainty in the economy. A recovery in the US will probably lead to improved performance in other economies including those of the EU and Asia, with the possible exception of Japan.

Policy trends and suggestions

The current policy stance in Korea is oriented to macroeconomic stability and continued microeconomic restructuring.

The current policy stance in Korea is oriented to macroeconomic stability and continued microeconomic restructuring. Through measures such as front-loading 65% of spending in the first half of 2002, the government is using proactive fiscal policies to create a stable macroeconomic foundation. In addition, market-led corporate and financial restructuring policies will be maintained in 2002.

Currently, uncertainty lingers about the timing of the economic recovery, and whether restructuring will continue smoothly. In addition, because of the two national elections scheduled for this year, there is a risk of economic policies being used for political advantage. An escape from the recession is not expected until after the first half of 2002, and it is possible that the real unemployment rate (including those who have given up their job search) may exceed 4%. Therefore, stimulus policies should be maintained at least during the first half.

In addition to economic stimulus, measures should be taken to increase the economy's growth potential by creating effective demand while expanding total supply. For example, considering the high shipping costs faced by domestic companies, and Korea's aspiration to become a transport hub for Northeast Asia, efforts should be made to increase infrastructure as well as R&D investment in the transport sector. For economic policies to be effective, different economic authorities should coordinate their efforts, and policies should not be used for political advantage. This would not only help raise policy credibility, but would also allow quick adjustment to changing external conditions.

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Considering the condition of domestic industries as well as industrial linkage effects, Korea should consider investing in industries such as IT, multimedia, alternative energy, and biotechnology as future engines of growth. In addition, efforts should be made to increase the value-added of existing industries, as well as pursue the fusion of cutting-edge technology with existing industries. To strengthen the basis of industrial competitiveness, support systems should be created for technology development, cooperation between industry and academia should be promoted, and networks related to R&D should be established. For venture companies, a foundation for long-term growth should be created through the invigoration of market functions, the merging of relevant policies, joint ventures with large companies, and the creation of specialist networks.

It is thought that the additional input of capital or labor will only result in limited growth for the domestic economy. Korea needs to continue promoting a knowledge-based economy by expanding knowledge resources such as technology, and striving to increase productivity. To strengthen the foundation for a knowledge-based economy, the education system should be reformed to foster new talent, and joint R&D efforts between the government and other sectors should be pursued to create an effective innovation system for science and technology. **VIP**