

RECENT INDUSTRY CONDITIONS AND PROSPECTS

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Prospects for key industries

Industries are expected to undergo adjustment in the first half, and in the second half, recovery may begin in earnest. Due to factors such as accumulated inventory and the continuing war on terrorism, recovery of the world economy has been delayed, and as a result, Korea's main industries are expected to see an adjustment period during the first half of 2002. During the second half, increased production due to inventory adjustment and a gradual upturn in the world economy are expected to lead to a recovery in earnest.

Traditional industries are expected to recover in a form. The shipbuilding and auto industries, which have maintained steady growth while other industries stagnated, are expected to maintain their 2001 performance levels in 2002 thanks to strong price competitiveness and efforts to promote high value-added.

IT industries are hoped to see a rapid V-shaped upturn. Due to recovery in the domestic and world economies, new product releases, and demand for new PCs, the IT industry is expected to see a rapid recovery in the second half of 2002.

Meanwhile, the iron and steel industry and construction are expected to see a U-shaped recovery thanks to the upturn in related domestic industries, such as the auto and shipbuilding sectors, as well as the government's support policies.

The petrochemical industry is expected to see continued stagnation in 2002 due to imbalance in the world market and low competitiveness of domestic petrochemical companies.

The semiconductor industry still faces uncertainty, and is likely to face a W-shaped recovery. While semiconductor prices are on an uptrend and the industry seems headed for a recovery, the industry is undergoing a worldwide restructuring, which may cause some uncertainty in the future.

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Auto Industry

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While exports have fallen due to a slump in the world auto market, the exports of mid-sized and large autos have risen, to result in a mild overall export decline.

Domestically, factors such as reduction of special consumption tax, expectations for economic recovery, the World Cup, presidential elections, and release of new models are expected to induce domestic demand to increase by 6.8%. While exports to North America are forecast to decline in 2002, overall exports are expected to rise by 6.6% due to higher demand for small and mid-sized cars, improved quality and brand image, and hopes that the takeover deal for Daewoo Motors will be completed.

Auto production is expected to increase by 6.9% in 2002 thanks to the increased domestic demand and exports. Exports are expected to rise by 21% due to the introduction of low price models, and active marketing by foreign producers, as well as the entry of Japanese autos after removal of import regulations.

Construction Industry

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Due to a rapid recovery of domestic construction orders in the second half of 2001, orders grew by 12.8% in 2001. In the private sector, the building industry grew by around 50% during November and December, resulting in a 8.7% annual growth rate, while the civil engineering sector grew by 0.6%, resulting in an overall growth rate of 7.2%. Public sector construction grew by 21.0%, with an 19.5% increase in the building sector and 21.8% growth in the civil engineering sector.

Overseas construction in 2001 amounted to \$4.36 billion, a 19.8% annual decrease, and in January 2002, overseas construction amounted to \$0.28 billion, an 11.4% decrease. While orders from the Middle East increase, Asian orders, which account for 40% of overseas orders, fell by 48.6% year over year. In 2001, civil engineering orders fell by 80.5%, while building orders and plant construction orders rose by 238.31% and 107.4% respectively.

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In 2002, domestic construction orders are expected to rise by 3.7% to record about \$7.03 billion. In the private sector, orders are expected to rise by 2.7% to record \$3.89 billion, due to induction of private capital for infrastructure, the abolition of green-belt and military protection areas, and expanded distribution of residential land. Public sector orders are expected to rise by 5.2% to record \$3.14 billion, due to the construction of 400 thousand homes, the injection of 5 trillion won in infrastructure budget, and construction of roads and water pipelines.

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Overseas construction orders in 2002 are expected to increase mildly in the first half and rapidly in the second half, with a forecast total of 4 to 5 billion dollars. As Korea's credit rating improves, corporate ratings are also rising, which will improve conditions for construction companies. Despite the expectations for economic recovery in Southeast Asia and expansion of orders from the Middle East, the domestic firms' lack of financial expertise will make it difficult for them to secure new orders.

Semiconductors

In the domestic semiconductor industry, exports and production declined by 40% in 2001 due to falling prices and decreasing shipments following lack of demand for PCs, and excess supply. However, in late 2001, DRAM prices, which had fallen below the profit level, have been showing a recovery. With the expected recovery in world IT demand after mid 2002, semiconductor exports and production are expected to rise by 14%. Domestic semiconductor exports and production are expected to rise by 14% thanks to the price stabilization of DRAM chips, the industry's main export, as well as a recovery in world IT demand. Imports are expected to rise by about 10% due to economic recovery and export increase and the resulting rise in nonmemory and semimanufactured goods.

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Telecom Equipment

The telecom equipment industry suffered a general slump in 2001, with a contraction in domestic demand and production and an import downturn as well. In 2002 however, the industry is undergoing a rapid recovery, with the upturn in the semiconductor market and IT industry conditions. According to the business sentiment index of the Federation of Korean Industries, the index for the IT industry exceeded 100 for the first time in January, and went on to record 120.3 in February, reflecting a rapid pace of market recovery (the BSI for all industries was 110.7). In January, export of wireless telecom equipment rose by 25.5%, and computer exports came out of their negative growth to record a 3% growth rate. After the second half of 2002, the industry is expected to recover in earnest, due to an upturn in the domestic economy. Demand is expected to gradually increase with the recovery of the domestic economy, introduction of new mobile phone models, and increased demand for new PCs. Exports are expected to see a steep increase due to expanded long term contracts for CDMA devices, and expansion of e-commerce. In particular, exports of IT equipment to emerging markets including China are expected to lead the export growth. Production and imports are expected to increase together thanks to the increase in domestic demand and export.

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Shipbuilding

In 2001, there was a slump in the number of new orders, but production and exports improved. The slump in orders continued into early 2002, with a stagnant shipping market. In January, Japanese shipbuilders received about ten orders, while domestic firms received only two. This seems to be the result of the shock to the world economy after the September 11 attacks and

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the resulting downturn in the shipping market. However, Japan benefitted from a rise in orders from Japanese shipping firms. Marine transport has been recovering since February, and the number of orders for new ships are expected to rise accordingly.

Korea's shipbuilding industry is expected to enter an upturn later in 2002 based on its competitiveness. Competition for new orders is expected to be intense between the shipbuilders of Korea and Japan, who are the two main players in the industry. Orders are expected to increase for Korean firms as their prices are more than 10% lower than that of their Japanese competitors. If the yen/dollar rate rises above 140 and the won/100 yen rate falls below 950, the volume of orders to Korean firms will suffer. With production of most shipbuilders having increased to full capacity, the increases in production and exports are expected to taper off.

Iron and Steel

With the recovery in industries such as shipbuilding, autos, and machinery, domestic demand for iron and steel in 2002 is expected to grow by about 3.1%.

'After the second half of 2000, domestic demand for iron and steel decreased due to the economic downturn', but since the second quarter of 2001, increased production by steel-using industries has led to a recovery in demand. Despite the demand recovery, industry conditions in 2002 are expected to be similar to those of 2001 because of the industry slump in advanced countries, as well as worsening trade frictions. With the recovery in industries such as shipbuilding, autos, and machinery, domestic demand for iron and steel in 2002 is expected to grow by about 3.1%. While demand from developing countries increased, trade pressures from the US and EU may cause not only decreased exports but also export diversion to other markets.

Petrochemical Industry

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The petrochemical industry completed its process of inventory reduction in the third quarter of 2001, and production has increased since December 2001. Production in 2002 is forecast to rise by 3.5% due to expected production increases in related industries such as home appliances, construction, and autos. These industries are expected to recover due to policies such as consumption tax cuts as well as the World Cup. As a result, domestic demand for petrochemical products is expected to rise by 3.0%. Exports are expected to increase by 3.6% due to the rapid growth and tariff reductions by China, a major export market. **VIP**