

## IV. Korean Economy This Week

### *Flagging Exports Are a Troubling Sign*

Korea's exports in the month of July fell a startling -13.7% on a year-on-year basis, the third consecutive month exports have fallen. In addition, exports for the second quarter were down -0.5%, after a respectable 8.6% growth rate in the first quarter. This downward trend is one of the most alarming indicators of the current state of the ailing Korean economy.

Exports have traditionally played a fundamental role in Korea's economic growth, and if and when the Korean economy is to recover from the current depression, exports will undoubtedly have to play a major part. With the huge drops in private consumption and investment, domestic demand is not expected to pick up any time in the near future, and so exports must take up some of the slack. In addition, stronger exports will help to boost Korea's trade surplus and thereby add to Korea's foreign exchange reserves, the shortage of which ignited the currency crisis at the end of last year.

However, exports have been unable to act as a catalyst for economic growth, much to the chagrin of policy makers and firms. There are several obstacles blocking export growth. One main reason has been the overall recession throughout the Asian region. Major export markets such as Japan and Southeast Asia are facing crises of their own and their imports are shrinking rapidly. Another problem has been the drop in export prices of Korea's major export items, such as semiconductors, automobiles and chemical products. A third major factor was the recent appreciation of the Korean won. After hitting almost 2000 won/dollar during the worst of the currency crisis, the won has since stabilized in the 1300 won/dollar range, a level at which exporters claim they lack price competitiveness. In contrast, the currencies of Korea's main export competitors, such as Japan and most of the Southeast Asian countries have all depreciated over the same period, and many are worrying that China will soon follow suit. In addition to these international factors, the domestic financial troubles have also

been hindering exports, as firms are finding it difficult to obtain trade financing as banks try to boost their capital adequacy ratios in the course of restructuring.

### *The Outlook Ahead*

It does not appear likely that the negative factors mentioned above will improve any time in the near future. The other Asian countries are faring no better than Korea in trying to escape from their own crises and demand within the region is expected to remain depressed for a while. Uncertainties still linger about what will happen in Japan and China, and any devaluation of either of their currencies would have a detrimental effect on Korea's export prospects. Advanced nations such as the U.S. and the EU are also beginning to show signs of the effects of the Asian crisis, and exports to those regions will also probably decline as their import demand shrinks. At the same time, there seem to be increasing moves toward protectionism as these nations brace themselves for what they think will be a "flood" of exports from Asia.

Furthermore, restructuring of the financial sector is far from complete, and liquidity still remains tight in the financial markets, paralyzing the trade financing system. Many are worrying that the difficulties in financing will prevent the import of raw materials needed for a sustained export drive.

Under these circumstances, what can the Government do to ameliorate the situation? Of course, the Government has no control over external factors, and the most it can do is prepare for the negative possibilities--for instance, a further appreciation of the won. Some are saying that the exchange rate needs to rise for exports to be competitive, but this would entail difficulties in other areas of the economy. In the end, the Government's best course of action is to facilitate the restructuring of the financial and corporate sectors in as smooth and natural manner as possible. Doing so will stabilize the financial markets and the overall economy and therefore enable exporters to demonstrate their true potential and competitiveness.

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