Ⅳ. Korean Economy This Week

Deteriorating Industrial Base

As of late, the Korean economy has been showing some disturbing trends. Industrial output fell 13.3% in June compared to the same month last year, the largest drop since 1952. In fact, the output growth rate has been negative for every month this year. The overall capacity utilization rate has fallen to under two-thirds, standing at 66.5% as of June, and unemployment has now reached over 7.0%. Domestic demand has also contracted severely, falling -28.9% year-on-year in June.

What is worse, exports are also decreasing. Exports in July only amounted to $10.2 billion, which was -13.7% lower than the same month the previous year--the third straight negative growth rate. And according to preliminary figures for the first 20 days of August, exports have again fallen -11.6% to $4.78 billion while imports have dropped to $4.75 billion, meaning that the trade surplus for this period only amounted to about $0.3 billion.

It does not appear likely that exports will revive anytime in the near future. In addition to the lingering problems in obtaining trade financing domestically, the exchange rate still remains below the 1,400 won/dollar level which exporters feel is the breaking point for maintaining price competitiveness in the world markets, and the prospects for the major export markets show little sign of improvement.

Many are beginning to worry that Korea's industrial base is deteriorating. While the drop in domestic demand is worrisome in itself, the drop in exports, the traditional driving force of Korea's economic growth, is particularly damaging since many were hoping that strong exports could help offset the domestic recession. Continued flagging exports could result in a lasting dent in GDP growth and cause economic contraction both in scale and in scope.

Furthermore, exports have been playing a major role in boosting Korea's foreign exchange reserves and stabilizing Korea's financial situation through the continual monthly trade surpluses. In a worst case scenario, when the current cycle bottoms out, import demand for capital goods and raw materials would rise sharply but exports would remain stagnant. This would mean that Korea's current account would once again worsen and leave open the possibility that the same crisis of recent years is repeated once more.

A New Industrial Policy

To break this potential vicious cycle, a new overall industrial policy is needed to ensure that the Korean economy of the future is less vulnerable to such weak linkages. While it may be premature to aggressively push such a new policy, an overall blueprint which outlines the basic directions for developing a high value-added trade and industrial structure is needed now, particularly as the Korean economy undergoes restructuring.

The key to the new industrial policy will be fostering knowledge-based industries. These include knowledge-intensive industries in which human intelligence, information, and technologies are "intensively" utilized in the manufacturing process to create higher value-added. They also include higher-value-added information service industries such data processing and consulting.

For Korea to be successful in these types of industries, three elements will be needed: a culture which values creativity, ample R&D investment, and future-oriented education which encompasses all of society. Of course, fostering these elements will not be easy, especially since the nation's resources are already being strained under the current crisis. However, these elements are indispensable for securing the nation's future growth potential; this is why a long-term blueprint for growth is needed now--to ensure that Korea's limited resources are channeled in the most effective manner.

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