

IV. Korea Economic Focus

Changes in Korea's External Economic Situation

Over the past year, the Korean economy has undergone some significant changes in terms of its external relations and international situation. To begin with, Korea was the recipient of a substantial amount of financial aid from international organizations including the IMF, the World Bank (IBRD), and also the Asia Development Bank (ADB). Of the US\$35 billion to be borrowed by 2000, Korea has received a total of \$29.015 billion as of the end of November.

This support from these international organizations and the advanced nations has greatly helped in stabilizing Korea's foreign debt and foreign exchange situations. As of the end of October, Korea's total external liabilities (according to IMF standards) amounted to \$153.5 billion, a slight improvement over the \$158.1 recorded at the end of 1997. More importantly, the percentage of short-term debt due within a year has rapidly dropped to 20.2% of total, much lower than the 60% recorded in October last year and the 40% at the end of 1997.

At the same time, Korea's foreign exchange reserves have risen to a record high \$50.02 billion, with usable reserves at \$46.47 billion, in sharp contrast to the low of \$3.9 billion on December 18 and the \$8.87 billion at the end of last year. The won/dollar exchange rate, after flirting with the ₩2,000 mark at one point a year ago, has now stabilized back down into the ₩1,200-1,250 range.

The improved foreign debt and exchange situations have also been aided by the whopping current account surplus this year. After registering a deficit of \$8.17 billion in 1997, the current account has shown a surplus through the end of October of \$34.11 billion, and is expected to hit a all-time high of \$39.5 to \$40 billion this year.

The international community seems to recognize the improvements in Korea's situation. Since May, foreign direct investment has been on the rise, and portfolio investment has been extremely active as of late. The total amount of investment in the first eleven months of the year is up 16.4% over the same period the previous year. At the same time, the spreads on the Korean government's foreign currency denominated bonds, which were as high as 10% at one point in August, have fallen back down to the 4% range, and it is expected

that major credit rating agencies such as Moody's may soon raise their ratings on dollar-denominated bonds to investment grade.

Tasks for the Year Ahead and Beyond

1998 was a hectic year for the Korean economy, and there is little doubt that 1999 will also prove so as well. In light of these dramatic changes, it is essential that the Korean government maintain a clear policy vision to prevent a future outbreak of a similar crisis and to transform the Korean economy into a high-efficiency machine.

Regarding Korea's external relations, the government must continue with its current efforts to add to the current account surplus, lower the overall foreign debt, increase foreign exchange reserves, and keep the exchange rate stable. Top priority must be placed on precluding the possibility of a second currency crisis.

In line with this, the government should focus its efforts in the real economy on boosting exports while simultaneously being aware of and trying to prevent possible trade friction. Already in 1998, some actions have been taken against Korea in the semiconductor and steel industries, and more can be expected in 1999, especially when one considers the size of Korea's trade surplus. Accordingly, Korea should be prepared to actively resort to the WTO to respond to such anti-dumping measures. At the same time, efforts should be made to stimulate the inflow and outflow of foreign direct investment.

In the financial sector, the government should place emphasis on keeping interest rates steady and trying to improve market's role of financial intermediation and supplying the real economy with capital. To raise the sector's effectiveness, it is urgent that financial restructuring is completed as soon as possible. New mechanisms need to be developed or adopted to help financial institutions to properly evaluate or assess credit risks.

From the regional or global perspective, Korea should more actively pursue free trade agreements with other nations or blocs and expand its presence in potential new markets. Korea should also work closely with neighbors like Japan and China to strengthen regional economic cooperation, and help lay down the groundwork for a possible Asian Monetary Fund to improve regional economic stability.

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