EVENT SUMMARY

Korean Perspective on the G-20 Summit

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Updates on the Korean Economy

>> *Slides*

As the numbers on the slides indicate, the Korean economy is not in a grave situation as some suggest. Details of the numbers need to be considered before making hasty, unfair assessment of an economy.

1. Recent Macroeconomic Developments
    - 5 percent GDP growth in recent years. Growth has been slowing down this year—primarily due to lower private consumption (from about 55 percent to 50 percent of GDP). Overall, Korea's economy is not even near recession but is still being managed for a soft landing.
    - Inflation is not a concern; it is below 4 percent, but job creation is a problem that needs to be addressed. The unemployment rate is still around 3 percent, but this follows the ILO's definition, so it excludes all those who are out of the job market because they gave up on finding a job. New job creation has been visibly slow.
    - Trade and the current account situation are still very good despite the global economic turmoil, mainly due to the fact that the composition of exports is very diverse and is equally distributed among different sectors. Also, the export market is diverse in the sense that exports are being made to different countries/continents.
2. Korea's External Position & Financial Strengths
    - Foreign exchange: With foreign reserves of 212 billion USD—the sixth largest in the world—the situation today cannot be compared to the 1997 situation. Also 90 percent of foreign reserves are in bonds of levels above AA; overall they are very liquid.
    - External debts are 39 percent of GDP, but even at that, 12 percent of external debt is in the form of cash advances for shipbuilding contracts and 22 percent is comprised of hedges for shipbuilders' exports and overseas financial investment, which are not exposed to default risk.
    - The banking sector is sound and household debt is not posing a problem either. Due to more rigid regulations on mortgages, implemented in 2006, than in other countries, the loan to value ratio (LTV ratio) is improving and Korea was able to prevent any kind of mortgage-related problems.

- Then why are there such negative perceptions?
  1. Greater capital-market openness and greater trade dependency may explain this. The proportion of foreign shares was 42 percent before foreign investors cashed out recently, which is high compared to 11 percent in the United States. Also the trade dependency is 75 percent, which is considered high.
  2. There are a number of psychological reasons behind these perceptions. People still have a vivid memory of the 1997 Asian financial crisis and this pessimism is creating a vicious cycle of negative perception.

3. **Government Policy Responses**

   Foreign currency is being provided through utilizing foreign exchange reserves, Fed-BOK currency swaps, etc. Also, there already have been fiscal stimulus packages and more will follow. Korea's stimulus packages until now account for 3.7 percent of GDP, which is higher than those of the United States or Japan, but the government is prepared to do more if necessary since it can afford to do so. Korea has maintained a strong fiscal position as yet with a fiscal surplus. Government debt to GDP is only 33 percent, which is much lower than the OECD average. It also has room for further monetary easing, since its current interest rate is 4 percent. Compared to other countries, Korea has a lot more room for further interest rate reduction.

4. **Korean Economic Outlook for 2009**

   With the current prospect of 3 percent GDP growth plus the 1 percent policy effect (through different political means such as fiscal stimulus packages, tax cuts, job creation, and monetary easing), Korea is expecting 4 percent GDP growth in 2009. This may sound ambitious but with the current state, it is not infeasible either.

Question and Answer Session

Q: Could you comment on exchange-rate movements? What's the severity of them and are they going to affect the Asian economies?

A: The G-20 summit started off with 4 agendas; the causes of the current crisis, the actions taken so far, the actions that need to be taken, and where to go from there. Global imbalances were never explicitly mentioned as a cause of this financial crisis. However, trying to reconstruct a global financial architecture without addressing the exchange-rate regime would be wrong. Yes, Korea's Won depreciated almost 50 percent from January 2008 to today. However, it is important that the global economy as a whole deal with this exchange rate volatility.

Q: With President-elect Obama's focus on helping the auto industry, will there be a renegotiation on auto-related agreements (the Korea-US FTA Korea) and what is the progress in the National Assembly of Korea regarding this issue?

A: The current Korean administration and the government are determined to have the bill passed in the National Assembly. The auto deal was a good one on both sides and President-elect Obama knows the importance of the Korea-US FTA. I hope we will be able to get the ratification of measures that are mutually beneficial. Also, judging from the names floating around as the potential US Trade Representatives, the situation looks positive—I don't necessarily see the need for renegotiation.

Q: From looking at the numbers in the slides, Korea does seem to be in a much better state than it was in 1997. Is that due to better bookkeeping or does it reflect a change in the fundamentals of the economy?

A: In the modern days of transparency, we surely do not think that we can change the numbers by changing the bookkeepers. Actually, statistics has been an important area in Korea since the early developing days of the 1970s, which also gave strength to different policies proposals. Policymakers based their decisions on hard data, and these numbers have been reliable for decades.

Q: Looking at the vulnerability of the US car industry and the relative strength of the Korean car industry, do you foresee a greater role for the Korean auto manufacturers in the global market in the future?

A: As a matter of fact, yes. Even GM Korea is doing very well despite GM's domestic turmoil. Korean automakers' plants in the United States such as those in Alabama are also doing well. We expect that people will invest more in the auto companies after the ratification of the Korea-US FTA which will result in more opportunities for growth in the auto industry as well as in other industrial sectors.

Q: The G-20 declaration mentioned that the Financial Stability Forum (FSF) should urgently be broadened by extending membership to key emerging-market countries. Do you think all of the G-20 countries would be included in that forum, because as of now they're considering G-7 countries plus 5 other countries, so if we include all the G-20 countries, it would be a rather big forum. If all of the G-20 countries are not included, which countries do you think should be included as the "key emerging economies"?

A: All G-20 countries would want to be included in the FSF, but it's something that the finance ministries and international financial bodies should work out. Nothing is decided for now. I personally think that Korea should be added, but if you ask someone who thinks that even the G-20 is too big, the emerging economies that they will want to include may be obvious.

C. Fred Bergsten: Our institute came up with a rather objective criterion that might guide this kind of decision, which we call the "Trillion Dollar Club." First of all, we spell "brick" with a "k." There are 6 emerging markets with GDPs of a trillion dollars or more, which are Brazil, Russia, India, China, Korea and Mexico; we believe that this is an objective criterion that suggests enough systemic importance to justify membership in whatever group is at issue. Also, it opens doors for inclusion of more countries as they develop.

Q: It seems that Korea's economy has a better footing that it had in 1997. However, there has been a sense of vulnerability of the corporate sector, especially for the SMEs (small/medium enterprises). They have smaller marginal profits. What actions is the government taking to alleviate this concern?

A: 88 percent of the employment in Korea is done by the SMEs. Therefore, SMEs are important for the Korean economy. The Korean government is paying special attention to the SMEs and they are also included in the most recent special stimulus package. However, this does not mean that the stimulus will be given to all of them; the government will identify viable SMEs through sound objective criteria—those who have strong solvency but are undergoing short-term liquidity problems—and help these firms out. The rest will have to go by the market economy principles.

Q: In the G-20 communiqué, there were no passages regarding the participation of emerging markets. Even the passages that did exist seemed to be there only because some emerging-market leaders were present as part of the process. Could you identify details that have been added or deleted because the emerging markets wanted them or did not want them? Also, what is the constituency structure? Who has the interest or the stake in this? Were the countries that are not members of the G-20 considered?

A: If there was one consensus among the leaders, it was that particular attention was given to the emerging markets. When they talk about IMF resource augmentation, praising the short-term liquidity facility, they had in mind the emerging-market economies, including those not included in the G-20.

Q: There is some evidences that there is a famine going on in North Korea. Are there any measures being worked out by the South Korean government to revive the North Korean economy?

A: The current administration has the initiative of "denuclearization, open, 3000"—which means that when North Korea is ready to open up and cooperate with us, and give up their nuclear program, South Korea will help them increase their GDP per capita to 3000 USD (it is currently less than 500 USD). This agenda is clearly stated and we hope that North Korea will respond positively to this South Korean position.