
COUNTRY REPORT

South Korea

North Korea

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4th quarter 1999

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October 7th 1999 **Summary**

4th quarter 1999

Inter-Korean relations The outlook for inter-Korean relations is positive, thanks in part to the US decision to ease economic sanctions against North Korea. The sixth round of four-party talks took place in Geneva in August, but little was achieved. The construction of two light-water nuclear reactors under KEDO will begin in 2000. Hyundai hopes to build an industrial estate in North Korea.

South Korea

Outlook for 2000-01 The president, Kim Dae-jung, will form a new political party to fight the April 2000 National Assembly election. Although his popularity has fallen, his supporters are likely to do well in the election, partly owing to the stronger than expected economic recovery. Monetary policy will remain accommodating in order to aid corporate and financial sector restructuring. Fiscal policy will tighten modestly. Economic recovery will continue over the forecast period, although the rate of growth will slow to below 5% in 2001 as the technical impact of restocking diminishes. Inflationary pressures will remain muted and the won will appreciate slowly. The current-account surplus will fall to 0.6% of GDP by 2001.

The political scene The government has continued to handle the political dimension of economic reform responsibly. The courts defied the government in late August by ruling that the Federal Supervisory Commission's nationalisation of Korea Life Insurance is illegal. Kim Dae-jung visited New Zealand in September for an APEC meeting and proposed a new policy dialogue, to be called the Seoul Forum. A South Korean defence minister visited China for the first time in late August, upsetting North Korea. Russia's defence minister visited South Korea in September. Relations with Japan have improved.

Economic policy The government has put together a W20trn (\$16.8bn) bond market stabilisation package to cope with the fall-out from the Daewoo crisis. It has also kept nominal short-term interest rates below 5% in order to help both the corporate and financial sectors. The second supplementary budget for 1999, worth W2.7trn, was passed by the National Assembly in August. The cabinet approved a draft budget for 2000 in September. Spending on financial sector restructuring, welfare provision and helping smaller companies will be boosted significantly. A budget deficit of 3.5% of GDP is projected.

The domestic economy

- Real GDP grew by 9.8% year on year in the second quarter of 1999. Private consumption growth during the quarter was surprisingly robust at 9% year on year. Imports of goods and services grew by 27.4% year on year in the second quarter on the back of stronger private consumption and restocking.

- Seasonally adjusted manufacturing production grew by 23.5% year on year in the second quarter of 1999. A strong performance was recorded by the radio, televisions and communications equipment, and motor vehicle sectors.
- The rate of unemployment fell to 5.7% in August; this compares with a peak of 8.6% recorded in February this year. Employment in manufacturing has risen. Wages in manufacturing rose by 13.8% year on year in the second quarter. Consumer price inflation has remained subdued.
- M1 and M2 have both continued to grow quickly. Deposits at local banks have started to rise, as fears about the domestic banking sector subside. Non-performing loans at local financial institutions fell by W2trn from the end-March level to W63.4trn at the end of June. Reverberations from the Daewoo crisis have helped push up bond yields and forced a correction on the stockmarket. External debt levels have remained stable.

Foreign trade and payments Preliminary data show that the merchandise trade surplus (fob-cif) reached \$15.6bn in January-August 1999, a year-on-year fall of nearly 40%. Semiconductors, LCD panel and PC exports have performed particularly strongly. The current-account surplus fell by just over 38% in January-June 1999 to \$13.6bn, mainly as a result of developments on the merchandise trade account. Foreign-exchange reserves rose to \$65.3bn in mid-September.

North Korea

Outlook for 2000-01 The easing of US sanctions in return for a pledge not to test long-range missiles for the time being creates new business opportunities and signals a wider reduction of tensions. Although the Perry plan is bold, it may backfire if North Korea continues to provoke. North Korea's senior deputy foreign minister may visit the US.

The political scene China's foreign minister visited Pyongyang in early October to celebrate 50 years of bilateral ties. North Korea sent its foreign minister to the annual UN General Assembly for the first time since 1992 in September. South Korea has estimated North Korea's population at 22.1m. Ri Jong-ok, one of North Korea's most senior and influential figures, has died.

Economic policy and the economy The lifting of US sanctions against North Korea has opened business opportunities, but there may be few takers. The South Korean central bank estimates that North Korea's GDP fell by 1.1% in 1998. The bank also estimates that North Korea recorded a merchandise trade deficit of \$320m in that year.

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Inter-Korean relations

- The outlook for inter-Korean relations is positive—
- The immediate prospects for inter-Korean relations are positive. The so-called sunshine policy (of positive engagement with North Korea) of the South Korean president, Kim Dae-jung, will be boosted by the US decision to ease economic sanctions against North Korea. Bilaterally, the two crises of mid-1999—the brief Yellow Sea naval battle and the arrest of a South Korean tourist in North Korea (3rd quarter 1999, pages 5 and 6)—were both contained. Hyundai's tours have resumed and have now taken more than 100,000 South Koreans to Mt Kumgang in less than a year. The group's founder, Chung Ju-yung, has met North Korea's leader, Kim Jong-il, for the second time, raising hopes of further business expansion in the north. Civilian north-south contacts are picking up again.
- and a summit is possible—
- Only at government level is North Korea still unwilling to engage South Korea, and even this might change. On September 27th North Korea's foreign minister, Paek Nam-sun, in New York for the UN General Assembly (at which he was unusually active), said that a summit could be held—provided that South Korea accepts North Korea's proposal, which includes withdrawal of US troops and other impossible conditions. Nevertheless, the two governments have talked before, and the signs are that next year they may do so again.
- but much will depend on North Korea—
- As ever, however, the question is whether the thaw will last. This is very much up to North Korea. The hope must be that Kim Jong-il realises that he is never likely to face such tolerant administrations in South Korea and the US again—particularly if the next US president is a Republican—and that the present window may be North Korea's last chance to turn over a new leaf, which above all will mean moving to normalise relations with South Korea. The framework is already there, in the inter-Korean agreement of December 1991—it just needs implementing.
- which may not moderate its hard line
- On past form, however, the usual zigzag course between soft and hard lines cannot be ruled out. A case in point remains the marine boundary dispute off the west coast (3rd quarter 1999, pages 5-6). In September, after the failure of talks at Panmunjom, the Korean People's Army (KPA) unilaterally declared a new border substantially south of the existing Northern Limit Line (NLL), the *de facto* border for the past 46 years. The new line leaves five islands held by South Korea in North Korean waters. Despite much bellicose rhetoric and signs of increased naval exercises, the hope must be that this is just letting off steam. Any new naval clashes could, however, quickly chill the overall atmosphere. Facing a parliamentary election in April 2000, Kim Dae-jung dare not risk looking weak and being accused of appeasement.
- There is little movement at the four-party talks
- The sixth round of four-party talks between the two Koreas, China and the US was held in Geneva in August. As ever, there was little movement, with North Korea still insisting on US troop withdrawal as an important and immediate agenda item. However, the atmosphere was cordial, and sideline meetings between the US and North Korea, in order to discuss fears that North Korea was

about to test-fire a missile, paved the way for the bilateral talks in Berlin in early September which, in turn, produced the breakthrough on this issue and on US sanctions (see below).

KEDO moves forward Although technically a multilateral consortium, the Korean Peninsula Energy Development Organisation (KEDO), set up in order to implement the October 1994 Geneva Agreed Framework between North Korea and the US, has become—as intended—an important forum for substantial, if largely unsung, practical inter-Korean co-operation. This looks set to deepen further in 2000 and beyond, as construction of two new light-water reactors begins at Kumho on North Korea's east coast—not before time, after two years of site preparation. A meeting due to be held in Pyongyang on September 25th—the first of its kind since February—brought together some 30 experts from South Korea, the US and Japan. Among the practicalities on the agenda was the issue of telecommunications. At the moment KEDO maintains site contact with Shinpo via eight lines on Japan's Intelsat, but South Korea would like this switched to its own Mugunghwa satellite.

Hyundai's founder meets Kim Jong-il again Chung Ju-yung visited North Korea again in late September for the third time this year. As usual, he was allowed the rare privilege of directly crossing the demilitarised zone (DMZ) at Panmunjom; and, as once before, his visit was extended to allow the even rarer privilege of an audience with Kim Jong-il. This is a good sign, both for Hyundai and inter-Korean relations overall. Mr Chung's son, the current Hyundai chairman, Chung Mong-hoon, was also present; both will no doubt report back to Kim Dae-jung on their return, thereby creating a *de facto* channel between Kim Dae-jung and Kim Jong-il.

A basketball match is held This visit was part of a large, 80-strong, Hyundai delegation, including 25 basketball players of both sexes, as well as coaches and journalists, who visited Pyongyang—but who had to go the long way round, via Beijing. The basketball matches—both North Korea versus South Korea, and mixed teams—were broadcast live to South Korea, the first such telecast, and were won by the home teams.

Hyundai will build a stadium in Pyongyang— In similar sporting spirit, Hyundai is to build a large, multi-purpose sports gymnasium in Pyongyang. The 12,335-seat facility will cost \$57.5m, of which Hyundai will pay \$34.2m, and will take two years to build, requiring Hyundai engineers to live in Pyongyang during the construction period. Hyundai has hopes of being allowed to take in supplies via Panmunjom, which appears over-optimistic. When built, the new gym will host basketball, volleyball and Korean wrestling, including inter-Korean matches. It is expected to be named after Chung Ju-yung—at North Korea's suggestion.

—and hopes to expand tourism around Mt Kumgang It would be both churlish and otiose to note that one thing Pyongyang is not short of is gymnasia. In the late 1980s North Korea built a whole new street devoted to specialised sports facilities, perhaps in the hope of staging some events of the 1988 Seoul Olympics. As a symbol, however, the new gym augurs well for sustained co-operation. Hyundai also hopes to expand tourism around Mt Kumgang, initially by developing hot springs and improving harbour

facilities. Future plans include two golf courses, three hotels and a ski resort—none of which on the face of it will add to the area's hitherto unspoilt beauty, even as they enhance inter-Korean relations.

Hyundai's hopes for Haeju are the crux of its North Korean operations

All this is puny, however, compared with the most important of Hyundai's plans for North Korea, which is to build a large industrial estate near Haeju in the south-west of the country. The precise hoped-for location has now been revealed as Kangnyong on the Ongjin peninsula, which faces South Korea and is less than 100 km by sea from Inchon. With characteristic ambition, Hyundai wants a site of 66 sq km, of which just under half would be factories, while the rest would be housing for more than 200,000 people—making this in effect an entire new city. The first phase, a more modest 3.3 sq km, would focus on light industry, and encourage small South Korean companies to relocate facilities rendered uncompetitive in recent years by Chinese and South-east Asian competition: for example, in shoes, garments, textiles, television and radio assembly, and food and beverages. Later phases would expand both the scale and types of business, to include heavy industry and larger companies.

\$20bn in exports: is this realistic?

Earlier reports spoke of eventual annual exports from the estate of \$4bn, or six times North Korea's total exports in 1998. The latest version raises this to \$20bn—of which Pyongyang would receive a useful \$2bn for providing the labour. So huge a figure raises doubts about whether this is realistic, or merely rhetoric. Nevertheless, even a much smaller venture such as the planned first phase has great potential: to boost North Korea's economy, while moving on Hyundai's activities from loss-leaders and tribute-bearing into substantial and profitable investments. It also has political resonance, in that if both Korean governments let this go ahead, the improved relations arising from the US's lifting of sanctions will be greatly strengthened. In that light, the fate of this project may be no less important as a guide to Korean futures as William Perry's report on US policy towards North Korea.

Trade unionists play ball—

Hyundai's basketball match was the second inter-Korean sporting exchange this summer. In August the Korean Confederation of Trade Unions (KCTU), the more radical of South Korea's two trade union bodies, sent a team to Pyongyang to play football with what pass for trade unions in North Korea. Again there were both intermixed and North-South matches, and again the atmosphere was cordial. A little too cordial for South Korea's National Intelligence Service (NIS), which, on their return, questioned some of the KCTU team for allegedly endorsing North Korea too warmly. The militants were suitably penitent, claiming (plausibly enough) that their hosts put them under pressure to be fulsome.

—while fellow travellers court arrest

Less usefully, North Korea as usual mounted a "unification festival" at Panmunjom around August 15th, the date on which both Koreas celebrate their liberation from Japan in 1945. As usual, too, a few of the now dwindling band of student and other fellow travellers in Seoul took a circuitous route to Pyongyang to participate in the festival, after which they crossed the DMZ into the welcoming arms of the NIS. They may expect to be jailed, but not for long. There is talk of revising the National Security Law, whose powers to define

“enemy-benefiting activity” are notoriously wide; even if that happens, however, elements like this will no doubt continue to receive the minor martyrdom that they court.

North Korea has received more than \$500m in aid from South Korea—

In response to a parliamentary question, on September 28th an official in Seoul said that a total of \$358m has been given by South Korea (including both government and non-governmental organisations) to North Korea since 1995. Most of this (\$284m) was sent before December 1997, while Kim Young-sam was president; \$31.9m flowed in 1998, and \$42.9m in January-August this year. This does not include the \$174m paid by Hyundai in tourism fees since its cruises to Mt Kumgang began in November 1998.

—and \$1bn from other countries

Over the same period other countries gave a total of \$1bn, either directly or through agencies such as the UN World Food Programme. The US was the most generous, with \$446m. Other donors included the EU (\$160m), China (\$159m) and Japan (\$56m). Japan has suspended aid for the past year, while China probably gave more than this behind the scenes.

Lim Dong-won looks on the bright side

Lim Dong-won, South Korea’s unification minister, likes to be positive. He told a group of visiting Korean-Americans on September 29th that North Korea is becoming “more practical”: noting that inter-Korean trade in August at \$29m was up by 83%, year on year, while in the same month the number of South Korean visitors to North Korea (excluding tourists) reached 769, more than double July’s total of 362.

IMRI will make monitors in Pyongyang

Hyundai is not the only South Korean company whose business in North Korea is expanding. IMRI, a small South Korean company based in Kyongsang province, announced in August that from October it will transfer its assembly line for 17-inch computer monitors to Pyongyang, where it already produces printed circuit boards. By the end of 1999 IMRI hopes to produce what it calls “the first finished electronic product made by a South Korean firm on North Korean soil”, going beyond the assembly operations and “processing on commission” whereby, *inter alia*, LG has had televisions made in North Korea. With the sunshine policy specifically encouraging the northward transfer of plant that is surplus to requirements in South Korea, this is the shape of things to come.

The Unification Church seeks business in North Korea—

The Unification Church (the “Moonies”) has for some years been seeking to do business in North Korea. Although its founder, Reverend Moon Sun-myong, was expelled from North Korea in his youth and is usually seen as strongly anti-communist, in latter years he visited Pyongyang and met Kim Il-sung. The Tongil group, the church’s business arm, competed with Hyundai for the rights to open tours to Mt Kumgang. Neither this nor other rumoured ventures came to fruition, however, and Tongil is widely believed to be in financial difficulties.

—and announces a joint venture in Nampo

On September 3rd, however, Pyonghwa Motors, a Tongil subsidiary, announced a \$5.8m investment in a joint venture with Chosun Yonbong, a North Korean machine manufacturer, for a vehicle repair plant at Nampo. Pyonghwa says that it will invest a further \$300m by 2003 to expand this into

car assembly, with a capacity of 10,000 units per year. What is not clear is where Pyonghwa will find either the technology (it is apparently talking to Fiat, Renault and Mercedes-Benz), or the market.

The circus comes to town

In mid-November the world-class Pyongyang circus troupe will make its first visit to South Korea. The 50-strong troupe will cross the DMZ at Panmunjom, and will give 40 performances in Seoul and elsewhere during its month-long visit. The producers, Kyemyong Co, have reportedly paid Pyongyang \$500,000 for this.

South Korea

Political structure

Official name	Republic of Korea	
Form of state	Presidential system; president and National Assembly are directly elected; National Assembly members are elected in a mixed system of first-past-the-post and proportional representation	
The executive	The president (elected for a single term of five years) appoints the State Council (cabinet) composed of the president, prime minister and between 15 and 30 ministers. The State Council is not entirely composed of members of the National Assembly	
Head of state	Elected president	
Legislature	Unicameral Kuk Hoe (National Assembly) of no fewer than 200 members (currently 299) elected for four-year terms; currently 253 seats are filled by direct election; the remaining 46 are distributed between parties in proportion to their share of the vote	
National elections	April 1996 (National Assembly) and December 1997 (presidential); next elections due by April 2000 (National Assembly) and December 2002 (presidential)	
National government	Coalition of the National Congress for New Politics (NCNP) led by the president, Kim Dae-jung, and the United Liberal Democrats (ULD) led by the prime minister, Kim Jong-pil. Until September 1998 the National Assembly was controlled by the Grand National Party (GNP), the former ruling party, but after opposition defections the government now has a slim majority. As of October 7th 1999 the NCNP had 105 seats, the ULD 55 seats and the GNP 135 seats; there were four independents	
Main political organisations	Government: National Congress for New Politics (NCNP) in alliance with United Liberal Democrats (ULD). Opposition: Grand National Party (GNP), formed by merger of the former New Korea Party (NKP) and the small Democratic Party (DP) towards the end of 1997. The former New Party by the People (NPP) has been absorbed into the NCNP	
Main members of State Council	President	Kim Dae-jung
	Prime minister	Kim Jong-pil
Key ministers	Commerce, industry & energy	Chung Duck-koo
	Construction & transportation	Lee Kun-choon
	Defence	Cho Seong-tae
	Education	Kim Duck-choong
	Environment	Kim Myung-ja
	Finance & economy	Kang Bong-kyun
	Foreign affairs & trade	Hong Soon-young
	Government administration & home affairs	Kim Ki-jae
	Health & welfare	Cha Heung-bong
	Information & communications	Namgoong Suek
	Justice	Kim Jung-kil
	Labour	Lee Sang-yong
	National unification	Lim Dong-won
	Science & technology	Seo Jung-uck
Central bank governor	Chon Chol-hwan	

Economic structure

Latest available figures

Economic indicators	1994	1995	1996	1997	1998
GDP at market prices (W trn)	323.4	377.3	418.5	453.3	449.5
Real GDP growth (%)	8.3	8.9	6.8	5.0	-5.8
Consumer price inflation (av; %)	6.2	4.5	4.9	4.5	7.5
Population (m)	44.5	45.1	45.5	45.9	46.4
Exports fob ^a (\$ bn)	95.0	124.6	130.0	138.6	131.8
Imports fob ^a (\$ bn)	97.8	129.1	144.9	141.8	90.6
Current-account balance (\$ bn)	-3.9	-8.5	-23.0	-8.2	40.0
Reserves excl gold (\$ bn)	25.6	32.7	34.0	21.1	52.0
Total external debt (\$ bn)	81.5	100.3 ^b	131.3 ^b	161.7 ^b	156.7 ^b
Debt-service ratio, paid (%)	6.9	7.3 ^b	8.7 ^b	11.1 ^b	13.8 ^b
Exchange rate (av; W:\$)	803.5	771.3	804.5	951.3	1,401.4

October 6th 1999 W1,203.5:\$1

Origins of gross domestic product 1998	% of total	Components of gross domestic product 1998	% of total
Agriculture, forestry & fishing	4.9	Private consumption	55.7
Mining & quarrying	0.4	Government consumption	10.9
Manufacturing	30.7	Fixed capital formation	29.4
Electricity, gas & water	2.3	Change in stocks	-8.6
Construction	10.1	Exports of goods & services	48.7
Trade, restaurants & hotels	10.6	Imports of goods & services	-35.8
Transport, storage & communications	6.9	Statistical discrepancy	-0.4
Financial & business services	19.6	GDP at market prices	100.0
Government services	8.0		
GDP at market prices incl others	100.0		

Principal exports 1998 ^c	\$ m	Principal imports 1998 ^c	\$ m
Electronic products	25,686	Electric & electronic machinery	18,939
Textiles	15,840	Crude petroleum	11,241
Machinery & equipment	14,783	Machinery & equipment	9,453
Motor vehicles	11,173	Chemicals & chemical compounds	6,117
Ships & floating structures	8,014	Light industry inputs	3,429
Total incl others	132,313	Total incl others	93,282

Main destinations of exports 1998	% of total	Main origins of imports 1998	% of total
US	17.2	US	21.9
Japan	9.2	Japan	18.1
China	9.0	China	7.0
Hong Kong	7.0	Australia	5.0
Taiwan	3.9	Saudi Arabia	4.7

^a Balance-of-payments basis. ^b EIU estimate. ^c Customs basis.

Outlook for 2000-01

- A parliamentary election looms closer
- The main political focus in the coming months will continue to be the election for the National Assembly (parliament), which will take place in April 2000. South Korea's legislative elections, which are held on a separate four-year cycle from the five-yearly presidential elections, often function as a mid-term rebuke for the incumbent president. Having already faced an opposition-controlled parliament at the start of his term, Kim Dae-jung has no wish to repeat the experience. His present narrow majority, gained gradually by luring a few opposition MPs to cross the floor, is, in principle, vulnerable.
- Kim Dae-jung will form a new party—
- Knowing this, Kim Dae-jung—bold as ever—plans to dissolve his party, the National Congress for New Politics (NCNP), and form a new one, more broadly based and therefore more certain of victory. Although the NCNP duly and dutifully voted on August 30th to dissolve itself, this may not prove easy—as has been shown by the postponement of the (as yet unnamed) new party's inauguration until early 2000 rather than later this year.
- but regional antagonism is unlikely to disappear
- Given the regional basis of political allegiance in South Korea, the government's surest way to retain and increase its majority is by alliance with all or part of the Kyongsang provinces in the south-east of the country, thereby in effect splitting the opposition Grand National Party (GNP). It will not be easy, however, to overcome deep hostility, especially that of Kim Young-sam, Kim Dae-jung's predecessor, who remains a force to be reckoned with in Pusan and is implacably hostile to his successor (even though both fought together as democrats against military dictatorship). Ironically, the president's better bet is Chun Doo-hwan, the coup-maker who once sentenced him to death. Such an alliance would be a delicate matter, however, which, despite many rumours, has yet to come to fruition.
- Kim Dae-jung will try to attract new blood to join his party—
- A further aim in founding a new party is to attract high-profile recruits from non-political walks of life. Again, there is no sign of great success here so far, unless it is being done behind the scenes. This prospect also scares NCNP loyalists. It is rumoured that up to half of the party's 105 sitting MPs could be deselected to make way for new blood. Although for many Chollans (in the south-west) loyalty to their local hero, Kim Dae-jung, has long been their guiding principle, there is a risk of disaffection were they to be dropped.
- but many in the ULD may not want to join him
- The NCNP's coalition partner, the United Liberal Democrats (ULD), led by the prime minister, Kim Jong-pil, also cannot be taken for granted. Many in the ULD are unhappy that their leader, under pressure from Kim Dae-jung, agreed to postpone the party's demand—which was the condition of its support for Kim Dae-jung in the first place—for increased powers for the prime minister. They will certainly resist pressure to follow the NCNP in dissolving themselves into the projected new party—which conversely will look weak if the ULD does not join.

Kim Dae-jung should still win the April election

Despite these challenges, the government will probably retain its parliamentary majority. The GNP remains lacklustre, and its leader, Lee Hoi-chang, is weak. The GNP may even split into its component factions, whether or not the ruling camp succeeds in enticing some to change sides. Conversely, although Kim Dae-jung's popularity rating has fallen, the general competence with which the economy is being handled (and its recovery) should suffice to ensure sufficient support—unless some major new scandal or disaster were to break over the next six months.

World economic growth will be robust

According to the EIU's most recent forecast for the world economy, prospects are rosy. World GDP growth is expected to rise from 3% (at PPP exchange rates) in 1999 to average around 3.5% in 2000-01. The US economy is expected to remain strong in 2000, but growth will then slow as interest rates there rise. Japan will emerge slowly from recession. The recovery in the EU will also gather momentum, with output in the member countries growing by some 2.5% in 2000-01. A fairly robust recovery is also well under way in Asia (excluding Japan). World trade growth is expected to rebound, from a low of 3% in 1998 to 6.5% in 2001, providing support for continued growth in South Korea's exports.

South Korea: global assumptions

(% change year on year unless otherwise indicated)

	1998 ^a	1999 ^b	2000 ^b	2001 ^b
Real GDP				
US	3.9	3.9	2.7	1.7
Japan	-2.9	0.6	0.0	1.7
Asia (excluding Japan)	2.6	5.4	5.4	5.4
of which:				
ASEAN	-6.0	2.5	4.2	4.5
EU	2.7	1.8	2.4	2.5
World trade growth	3.0	4.0	5.8	6.5
Oil price (Brent)	-33.3	33.3	6.6	-3.4
OECD consumer prices (av)	1.5	1.5	1.8	2.1
Exchange rate (av; ¥:\$)	131	115	110	109

^a Actual. ^b EIU forecasts.

The yen will remain relatively strong

Interest rates in the US are expected to rise in 2001, before falling back the following year, but the rise will be moderate in annual terms and the fall will be quite sharp, so South Korea's debt-service burden will not be sharply exacerbated. The outlook for exchange rates is benign for South Korea; for the first time since the mid-1990s the yen is expected to enter a period of strength and comparative stability against the dollar. This will help to sustain South Korea's competitive position.

The world inflationary outlook is benign

The outlook for world inflation is also benign. OECD inflation is expected to stay well under control, rising to 2.1% in 2001 from 1.5% in 1998-99. World inflation will stay subdued, at around 3.6%. Oil prices will stabilise again at a new higher level of \$17-18/barrel in 1999-2001, and inflationary pressure from non-oil commodity prices will be quite mild, although prices will be rising in year-on-year terms after a sharp fall in 1996-99. The moderate outlook for

world inflation in a period of fairly robust growth owes much to the fact that a number of countries in Asia, Latin America and Eastern Europe will be on a recovery path in the three years to 2001. There remains much spare capacity in the world economy after the crisis of 1997-98.

South Korea: forecast summary

(\$ bn unless otherwise indicated)

	1998 ^a	1999 ^b	2000 ^b	2001 ^b
Real GDP growth (% change)	-5.8	8.5	6.1	4.5
Unemployment (%)	6.8	7.0	6.8	5.5
Consumer prices (av; %)	7.5	0.9	2.7	2.5
Merchandise exports fob	131.8	138.1	154.2	179.0
Merchandise imports fob	90.6	115.7	142.3	168.6
Trade balance	41.2	22.5	11.9	10.4
Current-account balance	40.0	17.4	4.5	2.8
Exchange rate (av; W:\$)	1,401.4	1,193.0	1,175.0	1,123.0

^a Actual. ^b EIU forecasts.

- Monetary policy will be loose—
- Owing to the fragility of the financial and corporate sectors in South Korea, high value is placed on keeping interest rates as low as possible, despite the strength of the economy. As in many countries, rapid GDP growth is still mainly a matter of catching up with pre-crisis levels of overall output, so there is not much inflationary pressure in the economy. Although interest rates in South Korea may edge upwards, pushed by financial sector difficulties, no dramatic rise is expected over the next two years, and the monetary stance of the Bank of Korea (BOK, the central bank) will remain accommodating.
- while fiscal policy may tighten modestly
- Fiscal policy has been loose. Not only were comparatively expansionary budgets proposed in both 1998 and 1999, but supplementary spending has become habitual as the government has sought to boost domestic demand and provide employment and welfare. The proposed budget for 2000 is mildly expansionary (see Economic policy), but the demands of the financial sector restructuring process will almost certainly ensure that more has to be spent on rescue packages and possibly on welfare. For the time being the government can afford to run a deficit of 3-5% of GDP because it has ready access to the comparatively new domestic bond market and there is ready demand for its paper.
- Private consumption growth will slow in 2000
- Domestic demand is on a recovery path. Private consumption expenditure is expected to record growth of 7.6% in 1999, but it will not recover to its pre-crisis level until next year, when growth will be 5.8%. In 2001 private consumption growth will slow to a more sustainable 4%. Behind the growth in private consumption that is now under way is a more stable labour market. However, as the process of streamlining the corporate and financial sectors gathers some momentum after the National Assembly election in 2000, labour shedding will start again in some sectors.
- Business investment will be subdued
- Private-sector investment demand is still subdued. There is anecdotal evidence of considerable investment activity in some areas, but the picture is patchy.

Encouragingly, lending to small and medium-sized enterprises, previously starved of credit, is rising. The construction sector is still in a state of deep recession, but there are signs of a recovery. We expect gross fixed capital formation to grow by 2.1% in 1999 and for growth then to accelerate modestly to 5.1% in 2001. Construction will return to growth, but the continued overcapacity in swathes of manufacturing will constrain the growth of investment overall.

Stockbuilding will boost growth in 1999-2000

Stockbuilding is contributing to growth in 1999, as South Korean companies replenish inventories depleted at the height of the economic crisis in 1998. Change in stocks will contribute 4.8 percentage points to growth in 1999. This effect will continue into 2000, albeit to a much lesser degree, after which a more normal pattern will resume.

South Korea: economic results and forecasts

(W bn at constant 1995 prices; % change year on year in brackets)

	1998 ^a	1999 ^b	2000 ^b	2001 ^b
Private consumption	206,766 (-9.6)	222,480 (7.6)	235,383 (5.8)	244,799 (4.0)
Public consumption	39,938 (-0.1)	39,139 (-2.0)	39,452 (0.8)	39,847 (1.0)
Gross fixed capital formation	114,618 (-21.1)	117,025 (2.1)	120,887 (3.3)	127,052 (5.1)
Final domestic demand	361,321 (-12.7)	378,644 (4.8)	395,722 (4.5)	411,697 (4.0)
Change in stocks	-27,983 (-5.6) ^c	-8,970 (4.8) ^c	2,000 (2.5) ^c	2,500 (0.1) ^c
Total domestic demand	333,338 (-18.7)	369,673 (10.9)	397,722 (7.6)	414,197 (4.1)
Foreign balance	64,540 (12.2) ^c	62,623 (-0.5) ^c	60,859 (-0.4) ^c	65,130 (0.9) ^c
Statistical discrepancy	435	0	0	0
GDP	398,313 (-5.8)	432,296 (8.5)	458,581 (6.1)	479,327 (4.5)
Exports of goods & non-factor services	174,432 (13.3)	202,515 (16.1)	220,336 (8.8)	242,150 (9.9)
Imports of goods & non-factor services	109,892 (-22.0)	139,892 (27.3)	159,477 (14.0)	177,020 (11.0)

^a Actual. ^b EIU forecasts. ^c Contribution to GDP growth.

Consumer price rises will remain modest

Inflation is currently very mild in South Korea. Now that the currency has stabilised there is little imported inflation, and the recovery of domestic demand is not yet stoking significant inflationary pressure at home. However, there are some signs of asset price inflation, especially in the property market. The rise in some commodity prices and the strength of the yen are putting pressure on producer prices. Utility price rises are likely in late 1999 and the labour market is tight in some sectors. We expect an upturn in consumer price inflation to 2.7% in 2000, after a rise of under 1% in 1999. In 2001 a more subdued growth rate and the impact of financial reforms on prices of some services, as well as slower overall growth, will tend to subdue price rises, and

the goal of an inflation rate comparable to that of other OECD economies will be in sight.

The won will appreciate slowly

The won will appreciate moderately in 2000-01 as a result of strong inflows of foreign direct and portfolio investment and the continuing current-account surpluses. However, periods of volatility are quite probable, for example in the wake of more bad news from the corporate or financial sector, which is highly likely as the slow process of structural reform and opening proceeds. We expect the won to average W1,175:\$1 in 2000 and W1,123:\$1 in 2001.

South Korea: current account

(\$ bn unless otherwise indicated)

	1998 ^a	1999 ^b	2000 ^b	2001 ^b
Goods: exports fob	131.8	138.1	154.2	179.0
Goods: imports fob	-90.6	-115.7	-142.3	-168.6
Trade balance	41.2	22.5	11.9	10.4
Services: credit	24.6	25.2	25.8	26.4
Services: debit	-24.2	-25.5	-26.4	-27.2
Services balance	0.3	-0.3	-0.6	-0.8
Income: credit	3.7	3.8	4.1	4.3
Income: debit	-8.5	-9.5	-11.9	-11.9
Income balance	-4.8	-5.7	-7.9	-7.5
Current transfers: credit	6.8	5.8	6.1	6.3
Current transfers: debit	-3.5	-4.9	-5.0	-5.6
Current transfers balance	3.3	0.9	1.1	0.7
Current-account balance	40.0	17.4	4.5	2.8
% of GDP	12.5	4.3	1.1	0.6

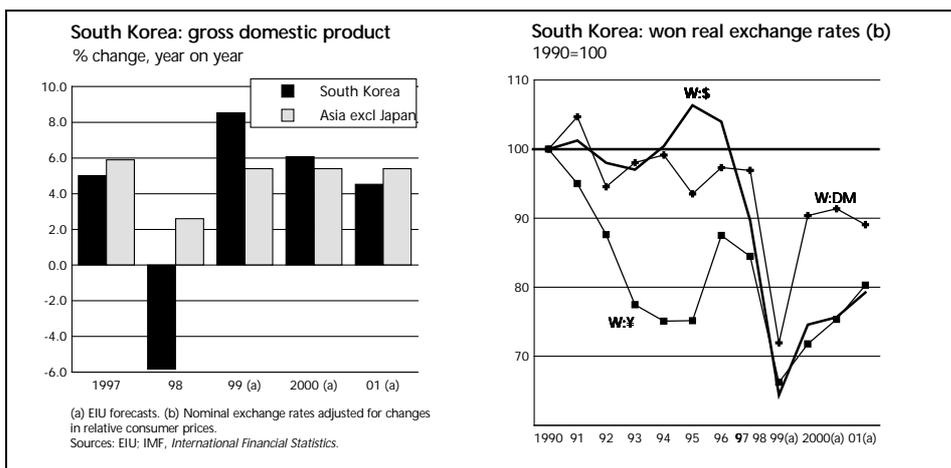
^a Actual. ^b EIU forecasts.

Smaller merchandise trade surpluses—

The recovery of domestic demand, the need to rebuild inventories and some rebound in investment are fuelling merchandise import growth in both volume and value terms; this trend will continue in 2000-01. Merchandise export growth is also likely to be fairly strong; this will, however, also contribute to merchandise import demand, given the high import content of many South Korean exports. We expect growth in merchandise exports in dollar terms to outpace world trade growth as South Korea gains market share in an increasingly narrow export mix, concentrated in information technology. Fast growth in merchandise imports in value terms will, however, reduce the size of the merchandise trade surpluses over the forecast period.

—will help reduce the size of the current-account surpluses

The services deficit will widen steadily in 2000-01, as outward tourism and import-related services both rise in line with the economic recovery. The income deficit will remain high, owing to rising outflows of interest, profits and dividends on the growing stock of foreign-owned assets. As a result of these developments, we expect South Korea's current-account surpluses to shrink steadily over the forecast period, reaching just \$2.8bn in 2001, or 0.6% of GDP.



The political scene

It has been a quiet quarter politically

After the excitements of the May cabinet reshuffle and the series of minor scandals (3rd quarter 1999, pages 15-18), the past quarter was a quiet one politically—if not economically, given the near collapse of the *chaebol* (conglomerate) Daewoo. Relations between government and opposition have remained poor, often obstructing the normal working of the National Assembly (parliament). Like presidents before him, Kim Dae-jung has resorted to railroading bills through the National Assembly, against opposition boycotts and protests. Everyone agrees that this is not healthy for South Korean democracy, but neither side seems prepared to do anything to raise the tone or smoothness of proceedings.

Economic reform continues—

In contrast, the political dimension of economic reform continues to be handled responsibly, with little backsliding and few concessions to populism. One exception is the government's unwillingness to force the closure of Samsung's ill-fated car plant. This is because it is in Pusan, which has the country's highest unemployment rate, as well as being an opposition bastion. The former president Kim Young-sam, whose turf this is, demagogically and unfairly accuses his successor of bias against the region.

—as Daewoo is broken up

However, the (eventually) vigorous handling of Daewoo—in effect breaking it up—is the latest sign that the government's will to reform has not weakened. Attacking the *chaebol* is a populist sport that always plays well in South Korea, but to set about restructuring seriously, as opposed to mere gesture politics, is something new. Most impressive is how the administration has not flinched from letting unemployment shoot up—it has peaked, and is now falling—while explaining to the public why pain is unavoidable.

The unions return to dialogue

This honest approach has served to undermine support for the once-feared militant trade unions. On August 30th the Federation of Korean Trade Unions (FKTU), the larger and more moderate of the two umbrella labour organisations, announced that it will return to the Tripartite Commission—comprising labour,

management and government representatives—which it had boycotted since March this year. This is a positive sign, although the unions, who in any case represent a mere 10% of the workforce, are now so weakened that the commission is of no great importance.

Hyundai is brought to book

Another positive step, politically, was the arrest on September 9th of Lee Ik-chi, the high-profile head of Hyundai Securities, on charges of manipulating the share price of Hyundai Electronics in 1998. Whatever the truth, this should quell mutterings that Hyundai, the largest *chaebol*, which like Daewoo has grown rather than slimmed since the financial crisis, is subject to favouritism because of its important role in advancing Kim Dae-jung's so-called sunshine policy of positive engagement towards North Korea.

The courts defy the government

Yet another good sign is that South Korean courts are daring to become more independent of government, as demonstrated in a ruling in late August that the Financial Supervisory Commission's nationalisation of Korea Life Insurance is illegal. Admittedly this was on a technicality, but in a society where the rule of law has rarely failed to conform to the wishes of whoever holds political power, it is a step in the right direction.

Xenophobic habits die hard—

In the eyes of foreign business, an important touchstone for reform is their own treatment. The old xenophobic stereotypes die hard, with some observers perhaps too hasty to claim evidence of backsliding. Two recent examples are the initial prioritising of Daewoo's local creditors over its foreign ones, and the collapse after seven months of HSBC's deal to buy SeoulBank.

—but the government is trying to change

However, in the former case the government moved swiftly (if not to the satisfaction of all parties) to give foreign creditors a share in both decision-making and collateral. On SeoulBank, there are two sides to the story. The *Financial Times* described the original deal as "a steal", and it was hardly surprising that the government sought to renegotiate it once the rise in the domestic stock-market rendered the original valuations obsolete. Nevertheless, the collapse of the deal looked bad, so the authorities moved swiftly to bring the even longer-running saga of Korea First Bank's sale to Newbridge Capital to a successful conclusion, agreeing after all to take on some potential future liabilities as well as those already known. The lesson is that foreigners may not get all they want on their own terms, but Seoul remains much more sensitive to their importance than before, when foreign businesses were unambiguously second-class citizens.

The government is pressing the press

While Kim Dae-jung's image both at home and abroad remains generally positive, his critics claim that he has dictatorial tendencies. Lee Hoi-chang, leader of the opposition Grand National Party (GNP), made this point a major theme of his little-noticed overseas tour in September. One ongoing episode that has attracted comment, however, concerns the *JoongAng Ilbo*, Seoul's best-selling daily paper, which used to be owned by Samsung, and remains connected to the group by familial ties. The owner of the paper is currently being investigated for alleged large-scale tax evasion. While the government insists that this is a straightforward criminal matter, its predecessors often used tax probes to intimidate their foes, and the *JoongAng Ilbo* had been a thorn in the government's side.

- Kim Dae-jung visits New Zealand—
Kim Dae-jung is keen to cut an active figure on the international stage. During the past quarter his main opportunity came at the Asia-Pacific Economic Co-operation (APEC) meetings in Auckland in September, where his schedule included a high-profile tripartite summit meeting with the US president, Bill Clinton, and Japan's prime minister, Keizo Obuchi. This was originally planned as a top-level joint warning to North Korea not to test another missile, but the news of an apparent breakthrough in Berlin on this issue somewhat took the wind out of its sails. It was nonetheless a useful opportunity for the three leaders to emphasise their common front in dealing with North Korea. (In truth, South Korea's recent sunshine policy is at odds with Japan's new toughness since the missile launch by North Korea in 1998, with the US somewhere in between—albeit closer to South Korea since the recent easing of US sanctions against North Korea.)
- and proposes the Seoul Forum
At the APEC meeting, Kim Dae-jung proposed a new policy dialogue, to be called the Seoul Forum, on how to prevent a recurrence of economic crisis, and to narrow the gap between rich and poor countries. The first meeting is expected in Seoul early next year. He also took the opportunity to visit New Zealand. As usual he was well received, with his easy manner and breadth of outlook perceived as a welcome change from most of his predecessors. In New Zealand, the two governments issued a 19-point joint statement for partnership in the 21st century, to include discussion of a free-trade agreement. South Korea is New Zealand's fifth largest export market.
- The decision to send troops to East Timor is contentious
Kim Dae-jung was also active at the APEC meeting on the East Timor issue and South Korea was quick to commit a contingent to the international peace-keeping force, including combat troops. This proved contentious at home, where the GNP and other critics worried about the risks, including that of the damage to relations with Indonesia. This involvement is very much in character for Kim Dae-jung, as a rare Asian leader who (as when in opposition) is not afraid to raise human rights issues in other Asian countries, albeit selectively.
- A South Korean defence minister visits China for first time—
With China, Kim Dae-jung, like his predecessors, is keen to make up for the lost cold war decades by pursuing ever closer ties. In late August Cho Seong-tae became the first South Korean defence minister to visit China. It was striking to see him taking the salute at an honour guard of the People's Liberation Army (China's army) which lost 400,000 men fighting against South Korea and in 1951 spearheaded the second brief capture of Seoul by North Korean forces.
- upsetting North Korea—
This spectacle will have been a bitter blow to North Korea. The Pyongyang press angrily denounced Cho Seong-tae's "junket", while refraining from criticising his hosts. By allowing this visit—a substantial, week-long affair—China was certainly signalling impatience and insouciance to its old but maverick ally. However, a remaining sensitivity towards North Korea will have been behind China's demurrals at South Korea's offer of joint naval exercises, even while agreeing to other forms of co-operation between the two countries' militaries.

- and raising criticism at home— China's long-term aim in courting Seoul is to wean South Korea away from its dependence on the US. Cho Seong-tae is not the first South Korean minister who while visiting China has shown enthusiasm for moves in that direction. He was criticised at home for apparently saying that the status of US troops in a future reunified Korea would be subject to international discussion (the party line is that this is a bilateral matter between the US and South Korea).
- for his egregious remarks Less commented on was his no less egregious reported remark that one day, it is hoped, South Korea will have military ties with China, Japan and Russia to match those with the US. Presumably he did not mean that these three countries should also have troops stationed in Korea. In general, in the post-cold war era South Korea is naturally seeking to rebalance its ties towards its three powerful neighbours, and away from an excessive dependence on the US. The US will be vigilant for any hint that rebalancing is moving towards neutralism. This will not happen under Kim Dae-jung, who is strongly pro-US.
- Three South Koreans are expelled from China One issue threatening to spoil Sino-South Korean ties is the fate of the North Koreans who cross into China, mostly in search of food. Estimates of the number run as high as 300,000, although many come and go rather than fleeing permanently. All governments involved treat them badly. China sends back those it catches, and North Korea punishes them (including by torture and execution, according to persistent reports). South Korea does little to help them reach Seoul, for fear of upsetting China or precipitating a flood of refugees, which none of the three countries wishes to encourage. Humane help for the suffering is therefore left to civilians: both local Chinese-Koreans who shelter and feed them, and South Korean charities, often Christian or Buddhist, who do likewise. To some extent the Chinese authorities turn a blind eye, but in September they cracked down, expelling two South Korean priests and a businessman. The issue will not go away: public opinion in Seoul is becoming aroused, the more so after China's ambassador told South Koreans that this was none of their business.
- Russia's defence minister visits South Korea Russia's defence minister, Igor Sergeev, visited South Korea in September. As with China, South Korea is keen to deepen normal relations. Unlike China, Russia has no scruples about offering joint naval exercises (if only for search and rescue, rather than military, manoeuvres)—even as it is in the process of formalising a new friendship treaty with North Korea, which pointedly excludes the military co-operation featured in the old, Soviet-era agreement of 1961. South Korea is also to receive Russian submarines in payment of an almost decade-old debt, even though South Korea's navy is not keen.
- Relations with Japan improve— The forging of new friendships by South Korea is not a zero-sum game. Under Kim Dae-jung, old alliances are also being revitalised, none more so than that with Japan, which has often been prickly as Korean memories of the colonial era are slow to fade. In what was a busy period for South Korean diplomacy in late August and early September, both the foreign and prime ministers visited Japan in quick succession. The prime minister, Kim Jong-pil, has long been well-connected in Japan: in 1965 it was he who negotiated the treaty restoring ties between the two countries for the first time since 1945. Some of his

compatriots regard him as too pro-Japanese: he was criticised in Seoul both for giving a speech in Japanese rather than through an interpreter, and for comments in support of an Asian approach to economic problems. The latter is a sensitive issue with the US, which was quick to squash Japanese suggestions at an early stage of the Asian financial crisis of an Asian Monetary Fund.

—but challenges loom The new warmth in bilateral relations will be tested by several issues. The disputed maritime border, involving fishing rights and the Tokdo/Takeshima islet, is on the back burner for now, but could flare up again. Japan's nuclear accident in late September will boost South Korean protests against Japanese ships carrying plutonium coming too close to Korean waters. With a second wave of liberalisation of Japanese cultural imports announced on September 10th, and further rounds planned, the overall relationship should continue to warm.

Economic policy

The Daewoo crisis— As of early October fears of a crisis in November resulting from pressure on investment trust companies (ITCs) exposed to the ailing Daewoo group (see Money and finance) were still putting pressure on interest rates and depressing the stockmarket. In response, the government has put together a W20trn (\$16.8bn at an exchange rate of W1,193:\$1) package with which to buy bonds on the secondary market. It has also pledged, *inter alia*, to support ITCs.

—will force the government to keep interest rates low A rise in interest rates at this stage of South Korea's economic recovery would be most unwelcome. It could force financially unsound *chaebol* (conglomerates), especially those among the 94 that are under "workout" (restructuring) but have so far failed to meet their targets, into bankruptcy, which would itself have an impact on the still vulnerable financial sector. It could also lead to currency volatility—South Korean exporters and the government desire a stable won:dollar exchange rate and want the won to remain weak against the yen in order to boost competitiveness against Japanese products. Every effort will therefore be made to keep nominal interest rates in their current range: the overnight won rate at under 5% and three-year corporate bond yields in single digits.

Support for the financial sector is proving expensive Provision of the necessary support to buoy up ailing ITCs, as well as to continue with the process of restructuring the financial sector, is proving expensive. The W40trn already spent may be only a small proportion of the amount of taxpayers' money that will be needed to create a more robust banking sector. The government is fortunate in so far as the amount of outstanding government bonds remains modest—although it is rising fast; there is therefore room for further borrowing to pay for financial sector restructuring.

The second supplementary budget for 1999 is passed In August the National Assembly (parliament) passed the second supplementary budget for 1999, worth W2.7trn. Most of the additional spending is to be devoted to flood control and prevention. There is also

support for households regarded as poor or middle-class. (See 3rd quarter 1999, page 20, for details of the first supplementary budget, passed by the National Assembly in April.)

South Korea: supplementary budget, Aug 1999

(W trn)

Support for households	0.9
For new businesses	0.3
For those on low incomes	0.5
For the marginalised	0.1
Subsidies to local governments	0.3
Flood recovery & prevention	1.5
Total	2.7

Source: Ministry of Planning and Budget.

The 2000 draft budget proposes a 5% increase in total revenue—

On September 21st the cabinet approved a draft budget for 2000. Excluding government bond issues, revenue is expected to reach W81.4trn, after W75.6trn in 1999, a year-on-year rise of 7.7% based on a slightly higher increase in nominal GDP. Including government bond issues, total revenue is projected at W92.9trn, a 5% rise year on year. Perhaps optimistically, given the need to fund financial sector restructuring in particular, the government expects to issue nearly 11% fewer bonds in 2000 than in 1999.

South Korea: budget proposal

(W trn unless otherwise indicated)

	1999	2000	% change over final 1999 estimate ^a
Revenue			
Tax	62.4	69.0	10.6
Other revenue	8.4	6.2	-26.0
Special account (public-sector loans)	4.8	6.2	28.8
Bond issuance	12.9	11.5	-10.8
Total	88.5	92.9	5.0
Expenditure by main category			
Investment in science & technology, information technology	4.0	4.6	13.5
Education	17.0	18.6	9.3
Promotion of culture & tourism	0.7	0.9	40.1
Investment in environment improvement	2.3	2.8	20.4
Support for venture firms & small & medium-sized companies	2.0	2.3	15.8
Support for agriculture & fishing	8.5	8.9	4.3
Social overhead capital	13.4	14.0	4.7
Expansion of the social safety net	5.1	5.7	11.9
Civil service salaries	14.4	16.3	12.9
Security & national defence	14.9	15.6	4.6
Financial restructuring & debt servicing	6.9	8.6	24.8
Budget balance (% of GDP)	-4.0	-3.5	-

^a Percentage changes calculated on unrounded figures.

Source: Ministry of Planning and Budget.

—and higher spending in key categories—

Spending in key categories—including financial sector restructuring, welfare provision, and supporting smaller companies and corporate start-ups—is set to rise significantly from the 1999 level. Despite efforts to curb the size of the bureaucracy, spending on civil servants' salaries is also set for a substantial increase. Defence expenditure, which accounts for a large share of the total (17%), will rise by 4.7%; however, much of this increase will be accounted for by personnel expenses, as military salary increases are tied to those for civil servants.

—to give a deficit of 3.5% of GDP

The deficit, at W5.6trn, is expected to be held to 3.5% of GDP in 2000, after an estimated 4% in 1999. The 2000 projection is 1 percentage point lower than the government originally forecast under its "Mid-Term Fiscal Plan", which aimed to balance the budget by 2006. As a result of the country's improving economic performance, according to the chairman of the Planning and Budget Commission, Jin Nyum, the government now expects to balance the budget by 2004, two years ahead of schedule.

The domestic economy

Production and demand

The recovery accelerates

Data for GDP in the second quarter of 1999 were surprisingly robust: output grew by 9.8% in real terms, the fastest year-on-year growth for several years. Real GDP rose by 1.7% on its level in the second quarter of 1997.

South Korea: expenditure on gross domestic product
(% change, year on year; constant 1995 prices)

	1998				1999	
	1 Qtr	2 Qtr	3 Qtr	4 Qtr	1 Qtr	2 Qtr
Private consumption	-9.9	-11.2	-10.4	-6.9	6.2	9.0
Government consumption	1.3	-0.7	-0.6	-0.4	-1.7	-2.6
Gross fixed capital formation	-20.6	-23.7	-22.2	-17.9	-4.3	4.9
Exports of goods & non-factor services	25.7	13.2	8.0	8.8	11.9	16.0
of which:						
merchandise exports	27.1	16.5	9.5	11.5	12.7	18.8
Imports of goods & non-factor services	-27.2	-25.5	-25.9	-9.0	27.4	27.4
of which:						
merchandise imports	-27.7	-27.3	-28.7	-14.8	26.3	31.4
GDP	-3.6	-7.2	-7.1	-5.3	4.6	9.8

Source: Bank of Korea, *Monthly Statistical Bulletin*.

Private consumption growth is robust—

The behaviour of private consumption was surprising. Despite continuing uncertainty, and expectations that the process of downsizing and restructuring would cut jobs at *chaebol* (conglomerates), in financial institutions and in the bureaucracy, consumer confidence appears to be recovering. Spending on big-ticket items, such as cars, furniture and personal computers, is reported to be strong.

—as household borrowing rises	Borrowing by the household sector rose strongly in the first half of 1999, stimulated by lower interest rates and more readily available credit, as well as increased confidence among consumers. The total debt of households had risen to W192.6trn (\$161bn at an exchange rate of W1,193:\$1) by the end of June 1999, up by 4.9% on the level a year ago. In the first half of 1999 households borrowed an additional W9trn; borrowing was particularly vigorous in the second quarter, when it rose by W7.1trn.
Government consumption continues to shrink	Government consumption has remained well under control, reflecting the determination of Kim Dae-Jung's government to trim the size of the establishment; it fell by 2.6% year on year, after a fall of 1.7% year on year in the first quarter.
Manufacturing investment grows strongly—	Less startling was the rebound in manufacturing investment in the second quarter of 1999. Within an overall growth rate of 4.9% year on year in gross fixed capital formation, investment in equipment was up by 37.2% year on year, albeit it on a very depressed base; this bodes well for the maintenance of productivity and competitiveness in the future. Construction remained depressed, however, declining by 8.5% year on year in the second quarter.
—but remains below 1997 levels	A survey conducted by the Federation of Korean Industries (FKI, the <i>chaebol</i> lobby group), covering the 200 largest manufacturing companies and reported by the <i>Korea Herald</i> in late September, stated that these companies were intending to invest W12trn in their production facilities in 1999. This is 6.8% above the depressed level of 1998, but represents only 55.4% of the nominal amount invested in 1997, according to FKI data. Encouragingly, the FKI reported, the planned rise in facility investment has risen from 1.9% at the beginning of 1999 as prospects have improved. In July investment was up by 57.8% year on year, according to National Statistical Office (NSO) data, but the spending was 18% down on the same month of 1997 in nominal terms.
The Daewoo crisis may affect investment by smaller companies	Investment by small and medium-sized enterprises has been stimulated by easier access to credit (at the behest of the government), as well as lower interest rates and a stronger domestic economy. However, there are fears that the fall-out from the Daewoo crisis, which has already led to higher interest rates (see Money and finance), could prompt another liquidity squeeze, which would hit smaller enterprises hard. Rising investment remains concentrated in areas of information technology; purchases of personal computers (PCs) and other office machinery that were deferred in 1997-98 are now regarded as unavoidable in light of the approach of 2000 and the associated Y2K problem (the year 2000, a date which will be incompatible with older computing systems—popularly known as the millennium bug).
Export demand is also robust	As well as an improvement in domestic demand, South Korea's economy has benefited from robust demand in export markets during 1999. This has allowed exports of goods and services to maintain year-on-year growth well into double digits in the second quarter, although the rebuilding of inventories and the recovery in investment have kept import growth ahead of exports. In terms of goods alone, the volume of merchandise exports rose by 18.8% year on year, while merchandise imports were up by 31.4%.

South Korea: gross domestic product by industry

(% change, year on year; constant 1995 prices)

	1998				1999	
	1 Qtr	2 Qtr	3 Qtr	4 Qtr	1 Qtr	2 Qtr
Agriculture, forestry & fishing	6.2	-3.5	-7.0	-9.0	-7.4	4.9
Manufacturing	-4.6	-10.4	-9.1	-4.7	10.7	20.1
Electricity, gas & water	4.5	0.3	-4.1	-2.4	2.9	7.1
Construction	-3.9	-6.6	-10.1	-13.3	-14.7	-7.9
Services	-4.5	-7.4	-6.2	-3.4	6.5	10.4

Source: Bank of Korea, *Monthly Statistical Bulletin*.

Supply side data are mixed

On the supply side, it was the strong recovery of manufacturing output that dominated growth: year-on-year manufacturing output growth surged from 10.7% in the first quarter to 20.1% in the second quarter. Agricultural output was boosted by good weather in the second quarter, while growth in utilities and services accelerated, helped by the resurgent manufacturing sector. Construction remained depressed, but the output of the sector declined less sharply than in previous quarters.

South Korea: seasonally adjusted manufacturing production

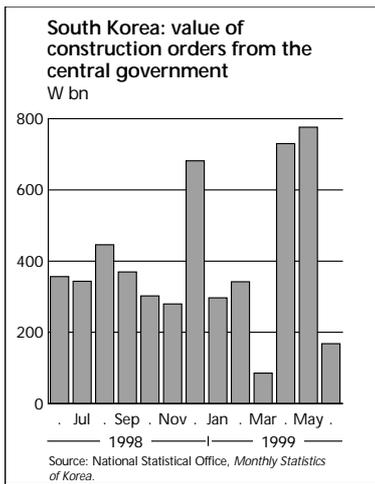
(1995=100; period averages)

	1998			1999		% change ^a
	2 Qtr	3 Qtr	4 Qtr	1 Qtr	2 Qtr	
Food & beverages	92.1	92.2	95.6	96.4	100.7	9.3
Textiles	76.1	73.2	74.7	76.8	79.9	5.1
Clothing	56.4	51.7	53.1	56.4	56.3	-0.1
Chemicals & products	119.8	121.0	127.4	127.2	132.6	10.7
Rubber & plastics products	83.5	81.8	87.7	90.3	99.8	19.6
Basic metals	97.7	97.1	101.3	102.4	106.7	9.2
Fabricated metal products	77.6	77.2	84.0	81.2	84.7	9.2
Non-electrical machinery	72.0	69.5	72.0	77.1	88.9	23.6
Radio, TV & communications equipment	181.6	213.8	258.0	253.0	265.1	46.0
Office, accounting & computing machinery	137.0	140.4	173.0	216.6	294.3	114.9
Electrical machinery	74.3	74.5	81.9	83.0	97.4	31.1
Motor vehicles & trailers	66.8	63.7	88.2	89.3	102.4	53.2
Other transport equipment	204.0	190.5	174.3	205.4	208.8	2.4
Manufacturing	100.6	100.4	114.4	116.6	124.2	23.5

^a 2 Qtr 1999/2 Qtr 1998.Source: Bank of Korea, *Monthly Statistical Bulletin*.

Manufacturing growth is broad-based

The recovery in manufacturing output in mid-1999 was broad-based. Seasonally adjusted manufacturing output rose by 23.5% year on year in the second quarter of 1999. Output in the so-called sunset sectors—clothing, textiles and basic metals—either remained sluggish by the standards of growth set in other sectors or was stagnant. Certain sectors recorded very fast growth in output based on strong export and domestic demand, and the need to



rebuild inventories that were run down sharply in 1997-98. The most rapid rises occurred in information technology, office machinery and motor vehicles, where external demand has boomed during 1999. According to anecdotal evidence, an early recovery in the output of the heavy industrial sectors is now spreading to light industry as well, but this area will be particularly vulnerable to a downturn if monetary conditions tighten.

South Korea: construction indicators, 1999

	Feb	Mar	Apr	May	Jun	Jul
Permits for building						
construction (m sq metres)	2.88	3.98	4.43	6.12	5.27	5.05
% change, year on year	-50.5	-29.6	4.1	47.1	16.8	49.0
Domestic construction orders						
received (W trn)	17.61	23.01	34.20	32.17	37.45	22.67
% change, year on year	-52.0	-51.1	39.4	89.6	-6.2	0.1

Sources: Bank of Korea, *Monthly Statistical Bulletin*; <http://www.bok.or.kr>.

Public works boost domestic construction—

In the second quarter of 1999 the long-awaited recovery in domestic construction began to show through. Permits rose by 22.5%, year on year, in terms of area, and domestic construction orders were worth 27.5% more. The strength of the property market and the fact that industry is now operating at 80% of capacity are boosting the prospects for a sustained recovery in construction. Various large-scale public-sector projects are also under way.

—and overseas construction is buoyant

Overseas construction is buoyant. Higher oil prices have helped to stimulate orders from the Middle East, and the widespread recovery from the Asian currency crisis has boosted demand in the region, to the relief of the *chaebol*. In September the Ministry of Construction and Transportation reported that overseas construction orders in the first eight months of 1999 were worth \$6.3bn, spread among 75 orders. This is a huge rise on the \$2bn in the same period of 1998, but the figure for the year as a whole is unlikely to match the \$14bn recorded in 1997.

South Korean construction companies rank eighth in the world in 1998

South Korean construction and engineering companies, (mainly the *chaebol*) ranked eighth in the world in 1998 in terms of international revenue, according to a report in the US *Engineering News Record*, cited by the *Korea Herald*, in late August. The US was ranked first and the US-based Bechtel Group was the largest single contractor. South Korea's Hyundai ranked 17th, with \$1.7bn in international revenue.

Shipbuilders weather the 1998 recession well—

The shipbuilding sector was among the few areas of South Korean industry to weather the 1997-98 recession virtually unscathed. The collapse of the won in late 1997 helped to boost the competitive position of South Korean shipyards that had been experiencing difficulties in competing against China, and even Japan, in terms of price.

—but the won's strength has eroded their competitive edge

However, the strength of the won in 1999 has eroded much of this competitive edge, and the value of new orders won by South Korean shipbuilders fell by 34.1% year on year in the first seven months of 1999, to 3.8m gross tonnes. As

of the end of July the order backlog stood at 19m gross tonnes, for 305 ships, compared with 19.5m gross tonnes (314 ships) in July 1998. Prospects for a recovery in new orders are considered good, thanks to the buoyancy of the world economy.

Employment, wages and prices

Unemployment is falling— Unemployment (not seasonally adjusted) peaked at 8.6% of the workforce in February and has fallen every month since then, to 6.2% in July (6.4% seasonally adjusted) and, according to press reports, further to 5.7% (5.9%) in August. In July the unemployment rate, according to the National Statistical Office (NSO), would have been 6.6% if measured by OECD standards.

South Korea: employment, 1999

(m unless otherwise indicated)

	Feb	Mar	Apr	May	Jun	Jul
Labour force	20.62	21.21	21.64	21.80	21.96	21.91
Employed	18.84	19.51	20.09	20.39	20.60	20.56
of which:						
manufacturing	3.78	3.87	3.90	3.92	3.95	3.97
Unemployed	1.78	1.70	1.55	1.40	1.36	1.35
Unemployment rate ^a (%)	8.6	8.0	7.1	6.4	6.2	6.2

^a Not seasonally adjusted.

Source: National Statistical Office, *Monthly Statistics of Korea*.

—but at a slower rate The pace of the fall in unemployment has decelerated because public labour programmes have been cut back as a result of economic recovery and demand for agricultural labour has fallen. Employment in manufacturing was up by 5.4% year on year in July and in services by 3%, also year on year. Employment in construction rose by 0.5% year on year, the first rise since November 1997.

The economically active population is falling The NSO attributed the fall in unemployment in August to a decline in the economically active population, rather than a rise in demand for labour. The total number in employment fell from 20.56m in July to 20.53m in August. The economically active population fell to 21.77m in August 1999, from 21.91m in July.

The government expects unemployment to average 6.5% in 1999 The Ministry of Labour (MOL) expects unemployment to average about 6.5% in 1999 as a whole, now that the demand for labour has now stabilised. The fear of provoking unemployment has played a large part in the government's reaction to the Daewoo crisis. A jobless total of about 1.4m is far higher than South Korea has been used to, but the days of unemployment in the 2% range are over; large-scale job losses in the financial sector and among *chaebol* (conglomerates) are in the pipeline.

Wages in manufacturing rise— From the fourth quarter of 1997 until the fourth quarter of 1998 nominal wages in manufacturing fell each quarter in year-on-year terms. A tighter labour market and improved corporate performance prompted a recovery from

the fourth quarter of 1998, which gathered pace in the first half of 1999. In the second quarter wages rose by 13.8%, to an average of W1,416,129 (\$1,187 at an exchange rate of W1,193:\$1) a month.

South Korea: wages in manufacturing industry
(won per month unless otherwise indicated)

	Earnings ^a	% change, year on year
1996	1,261,168	12.2
1997	1,326,241	5.2
1 Qtr	1,287,076	9.9
2 Qtr	1,295,054	9.3
3 Qtr	1,405,427	5.4
4 Qtr	1,319,762	-2.9
1998	1,284,477	-3.1
1 Qtr	1,252,690	-2.7
2 Qtr	1,244,597	-3.9
3 Qtr	1,263,187	-10.1
4 Qtr	1,383,167	4.8
1999		
1 Qtr	1,366,426	9.1
2 Qtr	1,416,129	13.8

^a Period averages.

Sources: Bank of Korea, *Monthly Statistical Bulletin*; <http://www.bok.or.kr>.

—as the gap between the high- and low-paid widens

In 1998, according to the MOL, the gap between the high- and low-paid widened. In an analysis of wages paid by 3,400 companies, the MOL found that the 1998 Gini coefficient (a standard measure of income distribution) had risen from 0.2521 in 1997 to 0.2542. The proportion of low wage-earners with monthly earnings below W500,000 rose to 2.7% of the workforce in 1998 from 2.5% the year before. High wage-earners, with more than W2m a month, rose from 20.4% to 21.2%. The gender gap narrowed somewhat in 1998 (although it is still large), but the gap between those with college education and those without has widened. Larger companies pay more than smaller ones.

South Korea: price indicators, 1999

(% change, year on year)

	Mar	Apr	May	Jun	Jul	Aug
Consumer prices	0.5	0.4	0.8	0.6	0.3	0.9
Producer prices	-4.3	-4.1	-2.6	-3.2	-2.9	-1.6
Export prices (won terms)	-28.6	-19.2	-18.8	-19.8	-16.1	-7.4
Import prices (won terms)	-24.6	-15.4	-14	-14.3	-9.9	-0.2

Sources: Bank of Korea, *Principal Economic Indicators*; <http://www.bok.or.kr>.

Consumer price inflation is very subdued—

Consumer price rises have been very subdued during 1999; weak demand, currency stability and falling interest rates have combined to reinforce price stability. In each month of 1999 year-on-year consumer price inflation has been below 1%. In August, however, prices rose by 1% month on month and by 0.9% year on year. The rise in consumer prices in August was the result of

bad weather, which raised the price of farm products. Higher fuel prices, resulting from higher international oil prices and increased prices for utilities will stoke inflation, but official forecasts expect an overall rise in consumer prices of no more than 3% in 1999.

—but will start to rise in coming months

Producer prices are coming under upward pressure. In the first eight months of 1999 producer prices fell continuously in year-on-year terms, owing both to currency strength and weak demand. From mid-1999, however, some commodity prices, oil in particular, have started to rise quite strongly, thanks to a generally buoyant world economy and, in the case of oil, to the maintenance of OPEC discipline with regard to production cutbacks. The prices of imported raw materials rose sharply in August compared with July; oil products increased by 7.7%. This will feed into consumer prices as the year progresses; according to press reports, the producer price index fell by 1.6% year on year in August, a sharp slowdown in the rate of decline compared with earlier months.

Money and finance

Money supply and savings grow fast

The rate of growth of monetary aggregates continues to be rapid: M1 expanded by 20% year on year in August and M2 by 25.3%, also year on year. Deposits at domestic banks had risen by W8.7trn (\$7.3bn at an exchange rate of W1,193:\$1) to W432.9trn by end-June 1999 from the level at the end of December 1998 (W424.3trn), as people piled their money into savings deposits. This, according to the Bank of Korea (BOK, the central bank), reflected rising confidence in the domestic banking system. Time deposits at commercial banks rose by W23.5trn to W236.7trn at the end of June this year from the end-1998 level, while demand deposits were up by W690bn over the same period. Deposits at money trust accounts fell by W16.3trn to W142.4trn because depositors withdrew their money to invest in the stockmarket.

South Korea: money supply trends, 1999

(W trn unless otherwise indicated; end-period)

	Mar	Apr	May	Jun	Jul	Aug
M1	327.3	331.2	342.9	343.1	331.3	342.7
% change, year on year	16.3	15.0	18.4	22.9	11.6	20.0
M2	2,782.6	2,768.8	2,772.6	2,759.7	2,821.2	2,958.6
% change, year on year	36.3	33.4	27.6	26.4	23.3	25.3
M3	8,207.7	8,292.7	8,345.3	8,328.4	n/a	n/a
% change, year on year	13.1	12.2	12.1	12.0	n/a	n/a

Source: Bank of Korea, <http://www.bok.or.kr>.

Non-performing loans rise slightly at commercial banks—

According to the Financial Supervisory Service (FSS, the executive arm of the Financial Supervisory Commission, FSC), reporting in early September, domestic financial institutions had a total of W63.4trn in non-performing loans (NPLs) at the end of June, W2trn down from the end-March level (3rd quarter 1999, page 28). NPLs at the 18 commercial banks rose slightly to W25.9trn, up from W25.8trn at the end of the first quarter; the total would

have fallen slightly were it not for the implementation of more rigorous classification standards.

South Korea: non-performing loans by type of financial institution, end-Jun 1999

Financial institution	W trn	% change on end-Mar 1999 ^a
Commercial banks	25.9	0.4
Special banks & development banks	11.2	-4.3
Merchant banks	2.1	-25.0
Securities companies	2.3	-4.6
Insurance companies	5.1	-4.5
Mutual savings & loans companies	7.3	-13.1
Leasing companies	6.8	11.3
Credit unions	2.7	-6.2
Total	63.4	-3.1

^a Percentage changes calculated on unrounded numbers.

Sources: Financial Supervisory Service; EIU, derived from press reports.

—but fall at non-banking
financial institutions

NPLs at non-banking financial institutions were valued at W26.3trn, down by W1.5trn compared with the end of the first quarter, representing 21.8% of total lending by these entities. NPLs at brokerage companies fell by W100bn to W2.3trn; NPLs at insurance companies declined by W200bn to W5.1trn; NPLs at mutual savings and finance companies, at merchant banks and at credit unions all fell. The NPLs of leasing companies, however, rose by W700bn, to W6.8trn.

A new NPL classification
will be applied from
December

From the end of December 1999 new and more rigorous classification standards will come into effect, based on forward-looking criteria. However, banks will be allowed to raise their provisions in stages by the end of 2000 in order to meet the new standards. The fall-out from the Daewoo crisis, the Samsung Motors receivership (3rd quarter 1999, page 35) and other, as yet latent, corporate liquidity problems are likely to raise the level of NPLs again. South Korea's banking sector remains highly vulnerable, despite the injection of W37.9trn in public funds since 1997, and many believe that the W12.9trn that the government intends to spend will not be enough to stabilise the situation.

The reverberations from
Daewoo—

The revelation in July that Daewoo could not service some W60trn in total debts has reverberated throughout the already struggling financial sector. Domestic banks have about W23trn outstanding to the Daewoo group. Creditors and the government put 12 Daewoo affiliates under "workout" (the term used for a restructuring programme) in late July, giving them a three-month grace period on debt service. It is believed that the 12 have issued bonds and commercial paper worth W7.5trn under the guarantee of financial institutions. On September 7th creditor banks agreed to put forward another W1.1trn to seven Daewoo subsidiaries in order to provide liquidity.

—include higher interest
rates—

Mainly because of fears about the potential fall-out from the Daewoo crisis, long-term interest rates rose sharply in mid-September; the yield on three-year

corporate bonds rose to 10.5% and that on three-year Treasury bonds reached 9.5%. Long-term interest rates have come under upward pressure because of concerns that, in November, when the Daewoo grace period expires, local investment trust companies (ITCs) with heavy exposure to Daewoo-issued bonds and commercial paper may suffer a serious liquidity crisis when the holders of the paper, which they have guaranteed, can redeem 80% of their certificates. It remains unclear who is responsible for the payment of interest on this type of paper; some creditors argue that the freeze should be lifted and that if Daewoo cannot pay the interest, the Seoul Guarantee Insurance Company (SGIC) should assume the burden. The SGIC refused to meet interest payments on Daewoo bonds on September 10th on which it was guarantor, on grounds of a liquidity shortage. In addition, if banks with direct exposure to Daewoo tighten their corporate lending policies as they seek to comply with Bank for International Settlements (BIS) capital adequacy criteria, a major credit crunch could ensue.

South Korea: financial market indicators, 1999

(end-period unless otherwise indicated)

	May	Jun	Jul	Aug	Sep	Oct ^a
KOSPI ^b (1980=100)	736.0	883.0	969.7	937.9	836.2	835.3
Overnight won rate (%)	4.8	4.8	4.7	4.8	4.8	4.8
3-year non-guaranteed corporate bond (%)	8.4	8.0	9.1	10.2	10.0	9.2
3-year Treasury bond	6.7	7.2	8.3	9.0	9.0	8.5

^a October 6th. ^b Korea Composite Stock Price Index.

Source: Bloomberg.

—prompting government
action—

Fearing that the potential crisis in November could paralyse the bond market, as ITCs dump as much paper as they can in order to hold cash to meet their bond redemption obligations, the government has taken action. One reason for this is the need to provide support to a market on which small and medium-sized companies are coming to depend (see below). In mid-September a package of measures was announced, the main points of which are as follows:

- the FSC has brokered an arrangement under which banks agree to support ITCs by buying government and municipal bonds, and A-grade or higher corporate bonds from them. It is hoped that this will stop the ITCs from dumping bonds on the market;
- the FSC will also try to create demand for bonds by allowing ITCs to sell new financial products, including tax-free savings bonds and short-term mutual funds, and to convert bond-related funds into equity-type investment instruments; and
- a W20trn won bond market stabilisation fund will be created in mid-October to buy bonds that would be dumped by ITCs. Banks and securities companies will provide W10trn on a voluntary basis and public funds will be tapped to raise the remaining W10trn.

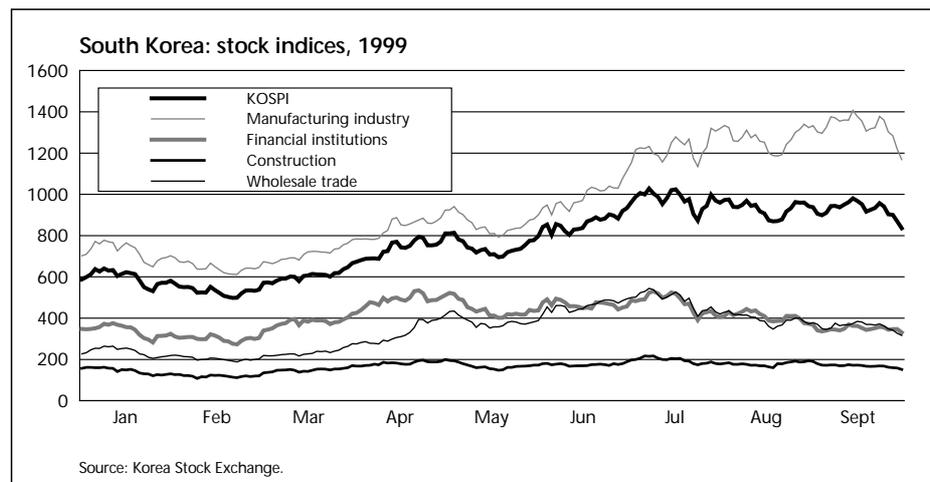
- and a possible increase in funding for the SGIC
- The FSC has also announced that it may provide additional funding to the SGIC to help it meet interest payment on Daewoo bonds. It has been considering easing various prudential requirements for the domestic banking sector; by the end of 1999 domestic banks must provide for 50% of their NPLs. That requirement and the imposition of sanctions on banks that do not meet their BIS 8% capital adequacy ratio by the end of the year may be eased. In response to angry demands from foreign creditors of Daewoo, the government has pledged that they will receive equal treatment during the workout process.
- The measures may not be enough
- There are good grounds to criticise these moves for being too little, too late. On the one hand, in light of the structural balance sheet weakness of many (if not most) South Korean banks, the wisdom of delaying the imposition of tighter prudential requirements is questionable. On the other hand, the W20trn package is small—W20trn against W180trn outstanding in bond-type investment trusts. In one week alone in September there was an outflow of W4trn from these ITC bonds; the bond market stabilisation fund could therefore be exhausted rapidly. A glut of bond issues is expected later this year. State bonds worth some W12trn and corporate bonds worth W15trn are due to be issued before the end of the year, according to the Korea Securities Dealers' Association.
- The chaebol* turn to the banks to raise funds as the Daewoo crisis unfolds—
- With the bond and stockmarkets affected by the Daewoo crisis from late July, the *chaebol* have turned to the banks to raise working capital, according to the BOK. Funds raised through corporate bonds and commercial paper issued by companies fell by W1.1trn and W3.3trn respectively in August from July. Rights issues also fell. This reversed the trend during the first half of 1999, when *chaebol* turned to the stockmarket to reduce their debt/equity ratios. Total borrowing by the top five *chaebol* was worth W148.9trn at the end of June, only W230.9bn lower than in the same period in 1998. According to the FSC, the five largest *chaebol* borrowed W27.9trn from banks in the first six months of 1999, down from W29.5trn in July-December 1998 and W42.1trn in July-December 1997. Their borrowings from non-banking financial institutions fell to W43.82trn from W44.25trn at end-1998 and W47.79trn at end-1997.
- but still dominate the capital markets
- The five largest *chaebol* had W77.68trn in bonds outstanding by the end of June 1999, W1.7trn more than at the end of 1998 and W35trn above the end-1997 figure. In January-August 1999, according to an FSS report in September, the corporate sector raised W29.9trn on the stockmarket, 328.7% up on the same period of 1998. Corporate bond issuance fell, down by 7.5% year on year to W25.4trn. As usual the *chaebol* dominated stockmarket issuance, accounting for 97.9% of the total raised, and the top five *chaebol* accounted for more than half. The bond market was less dominated by the leading five; their issuance fell by 57.3% to W9.38trn. Small and medium-sized companies raised W2.65trn in the first eight months, 1,220% more than in the same period of 1998.
- Debt/equity ratios fall overall—
- The leading five *chaebol* have managed to cut their combined debt/equity ratio to 302.2% as of the end of June 1999, from 386% at the end of December 1998. Their total debt, at W222.7trn at end-June, is somewhat below the W234trn in public debt. The level fell by W2.4trn compared with end-1998 and was

W7.4trn above target. Equity reached W73.7trn, up from W58.3trn and W9.6trn above target.

—but not at Daewoo The exception to this generally favourable picture was Daewoo. Even before it went public with its problems in late July its debt/equity ratio had risen to 588.2% by the end of June, up from 526.5% at the end of 1998 and against a target of 512.4% for the period. The position will have worsened since then, with the value of Daewoo equity eroded and new debts assumed.

Listed companies return to profit In the first half of 1999 the 523 companies listed on the Korean Stock Exchange made net profits of W6.7trn, after losses of W9.7trn in the first half of 1998. However, the majority of companies placed under debt workout programmes failed to meet targets set for the first half of the year. The FSC has said that only 19 of the 93 firms now undertaking workout programmes surpassed sales revenue and net profit targets for the first half, while the remaining 74, or 79.5% of the total, fell short.

Stockmarket performance is volatile The domestic stockmarket delivered a robust performance in the early part of 1999, largely reflecting growing optimism over South Korea's improving economic outlook. By July the benchmark Korea Composite Stock Price Index (KOSPI) had risen above 1,000 points, well up on the end-1998 level of just over 560 points. However, there have been jitters; concerns about Daewoo, for example, weakened the KOSPI in mid-August, sending it below 900 points and prompting a sell-off by foreign investors. Net selling by foreign investors during the 17 trading days after July 19th, when Daewoo's restructuring plan was announced, reached W1.trn, compared with net sales of W1trn in the previous 17 days. In early October the KOSPI stood at just over 835 points.



External debt levels are stable Total external debt data for the end of July 1999 released by the Ministry of Finance and Economy show a broadly stable picture. All \$13.4bn of the short-term loans from the IMF had been repaid by early September. The government still owes \$7.5bn from the long-term stand-by arrangement to the Fund, including \$1.5bn to be drawn down at the end of next year. Total foreign liabilities stood at \$143.5bn at the end of July, and South Korea's foreign assets are expected to outstrip its liabilities before the end of the year. The ratings agencies have yet to react with another upgrade, and South Korea still pays a premium on foreign debt. The rise in short-term debt in 1999 is the result of the recovery in trade.

South Korea: external liabilities, 1999
(end-period; \$ bn)

	Feb	Mar	Apr	May	Jun	Jul
Public sector	34.1	34.2	33.4	33.5	32.1	31.0
Domestic financial institutions	56.9	56.1	53.8	52.6	52.2	52.6
Long-term	45.7	44.4	44.5	43.1	42.6	41.7
Short-term	11.1	11.7	9.3	9.5	9.6	10.9
Branches of foreign banks	13.1	13.4	12.8	13.4	13.5	14.1
Long-term	6.0	5.9	5.2	5.1	4.9	4.8
Short-term	7.1	7.5	7.6	8.3	8.6	9.3
Domestic corporations	41.4	41.8	42.7	43.3	43.6	45.8
Long-term	29.1	29.2	29.3	29.6	29.7	30.9
Short-term	12.3	12.7	13.4	13.7	13.9	14.9
Total	145.4	145.5	142.8	142.8	141.4	143.5

Source: Ministry of Finance and Economy, <http://www.mofe.go.kr>.

The won is stable

The won has recently stabilised around W1,200:\$1, thanks to the strength of the external payments position and the buoyancy of the economy. Downward pressure on the won arising from the Daewoo crisis has not been prolonged or acute. The appreciation of the yen against the dollar is a welcome development for South Korean exporters, despite the fact that it will raise import costs.

FDI inflows are strong

Foreign direct investment (FDI) commitments in the first eight months of 1999 totalled \$7.8bn, 89.5% up on the same period of 1998. Although FDI is rising rapidly, South Korea's FDI/GDP ratio remains low, at 6.7% in 1998, compared with other Asian countries, such as Singapore (72.4%) and China (24.7%), according to government data. Further efforts to improve the climate for FDI are to be made, despite opposition from those who argue that South Korean assets are being sold cheaply and that the FDI flows are no longer necessary in large amounts now that the economy is recovering and the external payments position is healthy. In the first eight months of 1999 investment from the EU rose by 169% year on year to \$4.3bn, investment from the US fell by 16.7%, while investment from Japan rose by 42.1%. The services sector took 53.3% of the total in the first eight months, while manufacturing accounted for 46%.

KFB has been sold successfully

After months of negotiation the terms for the sale of Korea First Bank (KFB) to Newbridge Capital of the US were finally agreed. Newbridge will pay W500bn for 51% of KFB. KFB's equity/asset ratio will be 3% and its capital adequacy ratio will be 10%. Newbridge has pledged to invest W200bn in KFB over the next two years in order to modernise it. Newbridge will not be exposed to any current NPLs or any that may arise over the next two years, including KFB's exposure to Daewoo. These generous terms were doubtless considered all the more necessary in the aftermath of the failure of protracted negotiations for the sale of SeoulBank to HSBC. These have now been abandoned, and the government has decided to inject W4.5trn into SeoulBank to make it viable again.

Sectoral trends

- Semiconductors dominate With exports worth \$10.6bn in the first seven months of 1999 alone—a 14% increase year on year—the role of semiconductors has become crucial to South Korea's economic performance. The country's rise to prominence in this field has been a mixed blessing for both the national economy and the companies involved—Samsung, Hyundai and LG (which has been taken over by Hyundai)—given the wild swings in prices of memory chips. Fortunately for South Korea's economic recovery, after a long period of low unit prices (partly caused by South Korean oversupply of 64-megabyte dynamic random access memory, or DRAM, semiconductors), these have now bounced back from a low of \$4.6 in late June to exceed \$10 in early September. South Korea's total export earnings in this sector are now expected to exceed \$20bn this year, up from the \$18.6bn originally targeted. South Korea also gains from initially high prices of 256-megabyte DRAM chips (although these, in their turn, will fall over time), as well as from the strong yen and the recent Taiwan earthquake, each of which is a blow to competitors.
- Samsung begins mass production of Rambus DRAM chips Several large Japanese companies—Hitachi, Fujitsu, Mitsubishi, Toshiba and NEC—have either pulled out of memory chips in whole or part, or scaled down operations, leaving South Korea with 45% of global 64-megabyte DRAM production (compared with 20% in the US, 15% in Japan, and 10% each in Europe and Taiwan). Knowing well that this is a wasting asset, in September Samsung became the first company worldwide to start mass-producing Rambus DRAM chips, operating at up to 1.6 gigabytes per second. Samsung hopes for sales of \$250m and a 60% share of the global Rambus market this year, rising next year to \$2bn—but on a 20% market share, as competitors rush to the market.
- The car industry is recovering— After a period of lean sales and drastic consolidation—Hyundai bought Kia, Daewoo bought Ssangyong and is now itself in difficulties, Samsung stopped production when it had barely started—the vehicle sector has recovered in 1999, with both domestic sales and exports healthy. The Samsung Economic Research Institute (SERI) expects domestic sales, always the mainstay, to grow by 32.3% year on year in the second half of 1999 (admittedly from the low baseline of last year's plunge in sales), while exports should grow by 5%.
- but overcapacity is a concern Two looming issues, however, are overcapacity and unequal exchange. Change of ownership has so far led to almost no plant closures, yet capacity is far above what markets—local and global—can support. This economic problem is also a political one, given the continuing difficulty that foreigners have in penetrating the Korean market. As the economy recovers, so the US trade representative and the EU are returning to the attack. European trade organisations claim that South Korea exports 280 cars for each one that it imports, and that both tariff and non-tariff barriers persist. The row is likely to intensify. One possible way forward would be mergers and acquisitions, or strategic alliances, above all between Daewoo and General Motors (GM), who were partners in the past. Despite much speculation, however, there is no sign of a remarriage yet.

Foreign buyers are buying component makers	One encouraging trend, however, is the sale of South Korean component manufacturers to foreign buyers, often for global platform use. Components have been the sector's weak point, with too many companies chasing too small a local market and quality problems which have hurt the carmakers (for example, Hyundai in North America). Recapitalisation in foreign hands will be a boon. A case in point is Halla Climate Control, in which Ford now has a 35% stake. On top of a \$200m contract in 1998 to supply air conditioners for three GM models, Halla Climate Control announced in September a further \$120m deal with GM over the next four years.
South Korean computers corner the US low-end market—	In computers, South Korea's long (if unsung) experience in original equipment manufacture (OEM) has partly given way to own-branding. LG still makes Compaq notebooks and Apple's iMac, and recently secured new long-term contracts from IBM and Gateway. Export performance this year has been boosted above all by TriGem's success at the cheapest (below \$600) end of the US home personal computer (PC) market, with its eMachines joint venture. In July alone eMachines took 46% of the market, leaving Compaq second with 26%. It now has 19% of the overall US PC market, in which the weight of the low-cost segment rose from 5% in March to 37% in July. Its eOne model was also the best-selling PC in Japan in July.
—and TriGem aims to become the world's second largest computer maker	On the strength of this performance, TriGem expects to become the world's second largest computer maker in 1999 with 3.4m units, second only to Acer of Taiwan with 5.5m. This is a remarkable comeback for both South Korea and TriGem. Competition from Taiwan had reduced South Korea's PC exports to a mere \$158m in 1996, from a peak of \$973m in 1989. In the first half of this year the total was \$757m, and the full year's total is expected to exceed \$1.5bn.
LG leads in TFT-LCD screens	As with semiconductors, in some specific areas South Korean companies are now prominent or even dominant, not only in global market share but also with cutting-edge technology. For example, Philips's \$1.6bn joint venture with LG (in which each company has a 50% stake) in thin-film transistor (TFT) LCD screens is the largest single inward investment in South Korea to date. South Korean makers only entered this industry, hitherto a Japanese monopoly, as recently as 1995: their market share rose from 9% in 1996 to 27% in 1998 and an expected 35% this year. Ironically, only one year ago LG and the other Korean makers of LCD panels, Hyundai and Samsung, were seriously considering cutting back or even quitting the sector owing to weak global demand and falling unit prices. Both have since recovered, however, and exports for January-July 1999 at \$1.529bn were half as large again as the total of just over \$1bn for the whole of 1998.
The shipping industry has full order books for now, but prospects are uncertain	Compared with this electronic high-tech, ships may seem to be a relic of South Korea's earlier metal-bashing stage—just as garments bespeak the even earlier era when South Korea was starting out in light industry. Nonetheless, South Korea now rivals Japan as the global number one: it expects to launch a record total of 10m gross tonnes this year. South Korea also boasts the world's three largest ship manufacturers in Hyundai, Samsung and Daewoo, since Japanese manufacturers are more numerous and smaller (Japan is urging them to merge).

Ships, like chips, are a cyclical market, though the cycles (of vessel replacement) are counted in decades rather than years. Currently Korean order books are full for the next two or three years, but prospects thereafter are less certain. Daewoo, in particular, is seeking a buyer, but rumours of Japanese interest—an idea which would have been sacrilege until recently—have been denied in Tokyo. With the onset of cheaper Chinese competition in the low-end very large crude carrier (VLCC) segment, South Korean makers such as Samsung are trying to move upmarket into more specialist niches, such as oil rigs and ancillary vessels.

Overall trends are favourable

A recent survey by the SERI paints a mostly favourable picture of sectoral prospects. Semiconductors, telecoms and shipbuilding are all seen as booming, thanks both to home demand and exports (with the proviso for shipbuilding about new overseas orders). Three further sectors—cars, household electronic appliances and machinery—are recovering satisfactorily after last year's slump. Another trio—steel, petrochemicals and textiles—are experiencing mixed fortunes: demand at home is recovering, but export prospects are less good for various reasons (for example, in the case of steel, a combination of lower demand in Asia and import restrictions by Western countries).

Foreign trade and payments

The merchandise trade surplus is falling

According to preliminary data from the government, in the first eight months of 1999 the merchandise trade surplus (fob-cif) reached \$15.6bn, down from a surplus of \$25.5bn in the same period of 1998. Merchandise exports have strengthened in dollar terms as the year has progressed, growing by 17.8% year on year in August, but merchandise imports have grown even more strongly, as parts of South Korean industry have restocked and as commodity prices have risen.

Semiconductors, LCD panels and PC exports are strong—

South Korea's merchandise export base is narrowing. Partly as a result of the 1997-98 recession and the subsequent rise in the value of the won, merchandise exports are being increasingly concentrated in those areas where the relevant *chaebol* (conglomerates) are able to compete and to invest in staying competitive. In the first half of 1999 exports of semiconductors, liquid crystal display (LCD) panels and personal computers (PCs) together accounted for 23.1% of the total value of exports, compared with 12.6% in the first half of 1998.

—partly owing to the Y2K problem

The strength of international demand for these products is associated with the Y2K problem (the year 2000, a date which will be incompatible with older computing systems, popularly known as the millennium bug), which has prompted businesses and individuals to overhaul their computing equipment. Semiconductor exports consist mainly of dynamic random access memory (DRAM) chips and prices of 64-megabyte chips have risen back to \$10 a unit, from a recent low of \$4.6 in late June. The recent severe earthquake in Taiwan will disrupt production of DRAM chips, at least temporarily, which may drive prices higher, so prospects for the branches of Samsung and Hyundai (which has absorbed LG Semicon) that export these items are good.

Car and machinery exports are doing well

Unit prices for LCD panels have also risen and demand is strong; exports in January-July rose by 268% year on year. Samsung is building a large new plant which will produce 30,000 units/month of large-sized LCDs; LG and Hyundai will begin to build new production lines this year. In the PC market, LG has become a global original equipment manufacture (OEM) supplier to PC makers. Exports of passenger vehicles and machinery and precision instruments have also performed strongly; in the first six months of this year, the latest period for which the EIU has data, exports of these products rose by 11.4% and 15%, respectively. Car exports have benefited from continued strong demand in the US, while exports of machinery and precision instruments have been boosted by stronger than expected demand in Japan.

South Korea: exports of selected commodities, Jan-Jun

(\$ m unless otherwise indicated)

	1998	1999	% change, year on year
Food	1,348	1,333	-1.1
Crude materials & fuels	4,158	3,137	-24.6
of which:			
petroleum & derivatives	2,488	2,149	-13.6
Clothing	2,108	2,194	4.1
Fabric	4,175	3,776	-9.6
Yarn	869	695	-20.1
Rubber tyres & tubes	789	754	-4.4
Chemicals & chemical products	4,656	4,242	-8.9
Metal goods	5,918	4,976	-15.9
Machinery & precision instruments	4,883	5,616	15.0
Electronic products	16,740	20,246	20.9
of which:			
semiconductors	7,999	9,029	12.9
Passenger cars	3,740	4,168	11.4
Ships	3,830	3,253	-15.1
Total incl others	67,110	66,234	-1.3

Source: Bank of Korea, *Monthly Statistical Bulletin*.

Imports surge in the first six months of 1999

Imports were severely compressed in 1997-98, but are now rebounding in most categories. In the first six months of 1999 imports of consumer durables rose by 30% (albeit from a very low base), boosted by the return of consumer confidence and by the removal of barriers to Japanese products. It was, however, imports of capital goods, up by 24.9% year on year to \$21.7bn, and of certain vital inputs such as semiconductors, chemicals and metallic ore, that pushed the growth in imports to 15% in the first half of the year. Higher prices for oil and other commodities and a stronger yen are likely to boost the import bill further in the second half of the year.

South Korea: imports of selected commodities, Jan-Jun

(\$ m unless otherwise indicated)

	1998	1999	% change, year on year
Food & consumer goods	6,011	7,328	21.9
of which:			
cereals	1,407	1,133	-19.5
consumer non-durables	561	628	12.1
consumer durables	2,969	3,859	30.0
Industrial materials & fuels	23,778	25,226	6.1
of which:			
crude petroleum	5,990	5,704	-4.8
minerals	1,494	1,749	17.0
light industry inputs	1,909	2,026	6.1
chemicals & chemical compounds	4,111	4,560	10.9
iron & steel products	1,909	2,083	9.1
non-ferrous metals	1,720	1,831	6.5
Capital goods	17,408	21,740	24.9
of which:			
machinery & equipment	5,405	6,051	11.9
electric & electronic machinery	10,424	14,154	35.8
of which:			
semiconductors	5,864	7,613	29.8
transport equipment	1,083	1,029	-5.0
Total	47,196	54,294	15.0
For domestic use	25,321	28,783	13.7
For export	21,875	25,511	16.6

Source: Bank of Korea, *Monthly Statistical Bulletin*.

The current-account surplus is falling

Developments on the merchandise trade account dominated the performance of the current account in January-June 1999; the merchandise trade surplus fell by 28.8% year on year, to \$15bn (fob-fob). The deficit on the income account also rose, reflecting outflows associated with the rising level of foreign assets in South Korea. The current-account surplus fell by 38.2%, to \$13.6bn. The services account also fell into deficit during the period, after recording a surplus in the same period of 1998, mainly as a result of increasing outward tourism on the back of rising consumer confidence.

South Korea: current- and capital account balances, Jan-Jun

(\$ m unless otherwise indicated)

	1998	1999	% change, year on year
Merchandise exports fob	67,081.1	67,578.9	0.7
Merchandise imports fob	-45,906.0	-52,504.1	14.4
Trade balance	21,175.1	15,074.9	-28.8
Services balance	788.8	-122.9	-115.6
Income balance	-1,967.6	-2,381.5	21.0
Current transfers	2,044.8	1,044.9	-48.9
Current-account balance	22,041.1	13,615.4	-38.2
Capital & financial account balance	3,172.9	-953.8	-130.1

Sources: Bank of Korea, *Monthly Statistical Bulletin*; National Statistical Office, *Monthly Statistics of Korea*.

Foreign-exchange reserves continue rising

Despite the repayment of the supplementary reserve facility (SRF) to the IMF, usable foreign-exchange reserves rose by \$500m from the end of August to \$65.3bn as of September 15th, according to the Bank of Korea (BOK, the central bank). Repayment of local banks' foreign-currency borrowings from the central bank contributed to this recent rise, as did the continuing current-account surplus. Usable reserves have risen from \$48.5bn at the end of 1998 to \$60.4bn at the end of June, and now provide ample cover for imports and short-term debt.

North Korea

Political structure

Official name	Democratic People's Republic of Korea	
Form of government	One-party rule, based on the ideology of <i>juche</i> (self-reliance)	
The executive	Constitutional revisions in September 1998 abolished the Central People's Committee, renamed the State Administration Council as the cabinet, and reaffirmed the National Defence Commission (NDC) as the highest state body, albeit nominally under the Supreme People's Assembly (SPA)	
Head of state	As of September 1998 Kim Il-sung (who died in 1994) is dubbed "eternal president". The president of the SPA Presidium performs the formal duties of the head of state, but the ultimate executive power holder is the chairman of the NDC	
National legislature	Unicameral 687-member SPA, directly elected for five-year terms. Its Presidium, formally the Standing Committee, substitutes when the SPA is not in session	
Regional legislatures	Each province, city, county or district elects people's assemblies or committees. These committees elect local officials to carry out centrally decided policies	
National elections	The tenth SPA was elected on July 26th 1998, more than three years late. The next SPA election is due by 2003. These are communist-style elections, with a single list of candidates and claimed turnout and "yes" votes approaching 100%	
National government	The Korean Workers' Party (KWP) controls all arms of the state. Since the death of Kim Il-sung, military figures have had a growing influence	
Main political parties	Government: the KWP is nominally in coalition with the Social Democratic Party and the Chondoist Chongu Party	
Key holders of state & party positions	National Defence Commission chairman First vice-chairman Vice-chairmen SPA Presidium President Vice-presidents Prime minister Vice-premiers Key politburo members	Kim Jong-il Jo Myong-rok Kim Il-chol; Ri Yong-mu Kim Yong-nam Yang Hyong-sop; Kim Yong-dae Hong Song-nam Jo Chang-dok; Kwak Bom-ki Kye Ung-tae; Chon Byong-ho
Key ministers	Agriculture Commerce Defence Finance Foreign affairs Foreign trade Light industry Metals & machinebuilding Public security	Ri Ha-sop Ri Yong-son Kim Il-chol Rim Kyong-suk Paek Nam-sun Kang Jong-mo Ri Yon-su Jon Sung-hun Paek Hak-nim
Chairman of the State Planning Commission	Pak Nam-gi	

Economic structure

Latest available figures

Economic indicators	1994	1995	1996	1997	1998
Real GDP growth ^a (%)	-1.8	-4.6	-3.7	-6.8	-1.1
Rice production ^b ('000 tonnes)	n/a	n/a	1,340	n/a	n/a
Population (m)	23.1 ^b	23.5 ^b	23.6 ^a	23.9 ^a	22.1 ^c
Exports ^a (\$ m)	840	740	730	910	560
Imports ^a (\$ m)	1,270	1,310	1,250	1,270	880
Trade balance ^a (\$ m)	-430	-570	-520	-360	320
External debt (\$ m)	9.8 ^d	n/a	n/a	n/a	n/a
Exchange rate (av; Won:\$)	2.17	2.15	2.15	2.20	2.20 ^e

October 7th 1999 Won 2.20:\$1

Origins of gross domestic product 1994 ^a	% of total
Agriculture, forestry & fishing	29.5
Mining	7.8
Manufacturing	23.6
Electricity, gas & water	4.8
Construction	6.3
Services	27.9
Total	100.0

Main destinations of exports 1995 ^f	% of total	Main origins of imports 1995 ^f	% of total
Japan	27.9	China	32.6
South Korea	20.8	Japan	17.2
China	5.2	Russia	4.7
Germany	4.0	South Korea	4.3
Russia	1.2	Germany	2.9

^a Bank of Korea (Seoul) estimates. ^b UN Food and Agriculture Organisation (FAO) figures. ^c National Statistical Office (Seoul) estimate. ^d Including rouble-zone debt, at pre-1990 values. ^e EIU estimate. ^f Cited in a book by Marcus Noland, *The North Korean Economy*, Institute for International Economics, Washington DC, 1995.

Outlook for 2000-01

- The prospects in and for North Korea are good
- At the risk of cliché, at the turn of the millennium the chances that things may improve in and for North Korea are better than they have been for a long time. The lifting of US sanctions in September, in exchange for a pledge that North Korea will not test long-range missiles for the time being, not only creates new business opportunities, but also signifies a wider easing of tensions, which had risen in mid-1999 as fears of such a test grew.
- A range of scenarios is possible
- A range of scenarios is now possible. The best would be if this limited and tacit promise by North Korea proves the first step in a larger and more formal process, leading eventually to a comprehensive curtailment of the several security threats posed by North Korea: not only missiles, but also nuclear weapons and the so far unaddressed issue of chemical and biological weapons. The US would gradually ease further sanctions and move to formalise diplomatic relations. Japan, which had moved in the opposite direction by imposing sanctions after North Korea fired a rocket over its territory in August 1998, will be under pressure to follow suit and ease the sanctions. All this will please and boost South Korea's president, Kim Dae-jung, since it conforms with his own so-called sunshine policy of positive engagement towards North Korea.
- The Perry plan is bold—
- Despite the lack of any published written undertaking from North Korea, the US would not have taken so firm—and politically risky—a step as lifting decades-old sanctions without good reason to expect real changes in North Korean behaviour. The context here is the Perry report on overall US policy towards North Korea, which has been long in the making. The ex-defence secretary, William Perry, was commissioned to review policy towards North Korea in November 1998. He visited Pyongyang in May this year, and his 20-page report was finally delivered to Congress and US allies in September. The report itself is classified—although it is to be distributed in confidence to South Korean MPs, which guarantees that it will leak to the Seoul press—but its general thrust has been widely canvassed.
- offering carrots and sticks—
- Mr Perry proposes a step by step approach of relationship-building by mutual concessions, of which the missile test suspension for lifting sanctions is the first step. The hope is to add further steps over time, with the ultimate aim of verifiably and permanently ending worries about North Korea and weapons of mass destruction: specifically nuclear weapons and missiles. The process is reversible: if Pyongyang goes back on its word, the US will reimpose sanctions.
- but has been criticised as appeasement
- It is significant that Mr Perry, who was chosen because he commands bipartisan respect in Washington, has opted for a path that critics condemn as appeasement. In support of this approach, he made what is the first high-level official admission of how close the US and North Korea came to war in 1994 over the nuclear issue: at one point the US came within 24 hours of ordering an evacuation of US civilians from South Korea. To avoid a repetition, step by step containment by offering inducements is seen as a better way—indeed the only way.

- It may backfire— Realistically, however, on past form there is no guarantee of success. For one thing, a similar situation was reached with the Geneva Agreed Framework (AF) of October 1994. Unlike what seems to be a mere tacit understanding this time, that was a formal, written, public agreement, intended not only to defuse the nuclear issue—which it did—but also to improve relations with the US and South Korea more widely—which it has not. By comparison, what North Korea has apparently agreed to now is much more limited, and leaves many loopholes. Not testing weapons is one thing, but what about developing and selling missiles? (Proliferation being a key US concern.) Furthermore, this applies only to long-range missiles—so is Pyongyang still free to sell its existing short-range Rodong missile (a modified Scud) to the likes of Iran and Pakistan?
- if North Korea continues to provoke Above all, Bill Clinton's administration risks being severely embarrassed—at a time when elections loom—should North Korea, as is its habit, stir up trouble elsewhere. One worry is the unilateral declaration by the Korean People's Army (KPA) of a new marine border in the Yellow Sea, far south of the existing Northern Limit Line (NLL), and including five islands held by South Korea. This may be only bluster, but the inter-Korean naval battle in June (3rd quarter 1999, pages 5-6) shows the risks. Any new North Korean provocation would force the US to reimpose sanctions, and strengthen those—in the US, Japan and South Korea—who are terminally fed up with North Korea as an inveterate rogue state, and regard sticks as more appropriate than carrots. This could lead to a further chill, and to serious tensions if the AF were to unravel.
- Kang Sok-ju may visit the US One touchstone will be mutual visits. When in Pyongyang earlier in 1999, Mr Perry invited Kang Sok-ju—North Korea's senior deputy foreign minister, who negotiated the AF and is said to be close to the country's leader, Kim Jong-il—to visit Washington. It is thought that Mr Kang may accept, and the visit could take place in late October. Ironically, Mr Kang's nominal superior, the foreign minister, Paek Nam-sun, spent much of September in the US—for the UN General Assembly. Evidently, however, he is not North Korea's point man for negotiations with the US.

The political scene

- China's foreign minister will visit China's foreign minister, Tang Jiaxuan, led a ten-strong delegation to Pyongyang for five days from October 5th. This was to celebrate half a century of bilateral ties, and follows the visit to China in June by a much larger North Korean party, led by Kim Yong-nam, the former foreign minister who, as chairman of the Supreme People's Assembly (parliament) Standing Committee, acts ceremonially as head of state in lieu of the reclusive Kim Jong-il. Details of Mr Tang's schedule were not announced in advance, so it was not clear if he was to meet the "dear leader"—who has himself been rumoured for many months to be about to visit China. The delay may continue, since North Korea is not best pleased with its old ally (and last remaining friend) for fêting South Korea's defence minister, Cho Seong-tae, in August.

- Active diplomacy at the UN— For the first time since 1992 North Korea sent its foreign minister to the annual UN General Assembly meetings. By September 22nd Paek Nam-sun had met his counterparts from Denmark, Singapore, Iran and Uganda, while his deputy, Choe Su-hon, had talked with his Finnish equivalent. Finland currently chairs the EU, towards which Pyongyang has been putting out feelers. These were rebuffed while there were fears of a new missile launch, but with that out of the way there may be progress.
- includes feelers to US-Korean business As well as a packed diplomatic schedule, Mr Paek was liberal with interviews, including with the radio station Voice of America. He also took a boat cruise around Manhattan with a dozen leaders of the US-Korean business community—pointedly excluding those known to be pro-North Korea. Presumably this was to try to drum up business from those most likely to be interested in taking advantage of the new opportunities opened up by the easing of US sanctions.
- The IAEA is still unhappy Even as the Korean Peninsula Energy Development Organisation (KEDO) moves ahead, the International Atomic Energy Agency (IAEA) is not happy about North Korea. The IAEA's concern, reiterated at a board meeting on September 20th, is that Pyongyang is not implementing safeguards at its now mothballed Yongbyon site that would eventually enable its nuclear history to be reconstructed in full. The October 1994 Agreed Framework allowed this to be postponed until at least 2003, after new light-water reactors are built, and the IAEA fears (correctly) that in practice North Korea may never be called to account for having almost certainly siphoned off plutonium in the early 1990s.
- The NSO estimates North Korea's population at 22.1m— On August 27th South Korea's National Statistical Office (NSO) published estimates of North Korea's population. Although there has been less of a shortage of demographic figures than other data, thanks to a published (but problematic) census in 1993 and earlier figures given to the UN, gaps and ambiguities remain—not least regarding the impact of famine since 1995. The NSO estimates North Korea's current population at 22.1m, 47% of South Korea's. It anticipates a much slower rate of increase than in the past, to just 22.2m next year and 23.5m by 2010. For normal reasons of demographic transition, although lagging South Korea, North Korea's population growth rate had fallen from an annual average of 2.2% in 1970-75 to 1.3% during 1990-95. For 1995-2000, however, the rate is expected to plunge to just 0.6%, well below South Korea's 1%.
- as famine takes its toll The reason for this reversal is famine, as reflected not only in deaths to date, but also in the reduced will or ability to have children under such duress. The NSO's figure of 270,000 deaths from hunger or malnutrition during the four years 1995-98 is lower than some other estimates, which reach as high as 3m. If the latter is true, or the reality lies in between, then the long-term demographic consequences for North Korea will be even more severe. Life expectancy, once among the highest in Asia, has already fallen to 59.8 years for men and 64.5 for women: down by 3.8 and 4.8 years respectively on the figure in 1993. The NSO reports that women outnumber men by 435,000, but this may be an artefact of Pyongyang's seeming exclusion of the military and certain other categories from its own statistics.

Ri Jong-ok dies at 83 Ri Jong-ok, one of North Korea's most senior and influential figures, died on September 23rd aged 83. His most recent position was as vice-president, from which he retired only last year and as which, despite his age, he travelled widely, particularly in developing countries. Before that he served as prime minister (1977-84), and in a wide range of economic ministries and other posts. His first cabinet post, as minister of light industry, came as long ago as 1951, during the Korean War, when he was just 35. Later he negotiated North Korea's post-war economic agreements with the Soviet Union and China, and he is credited, if that is the word, with spearheading Pyongyang's fateful push to prioritise heavy industry above all else.

Economic policy and the economy

The easing of sanctions by the US brings fresh opportunities—

The easing of US sanctions announced on September 17th is primarily a political gesture, but is not without potential economic import. It is by no means total. For example, as North Korea remains on the State Department's list of countries said to sponsor terrorism, trade in products with potential military applications remains banned, as do international loans and financial transactions between North Korea's government and US individuals or companies. North Korea's assets in the US, some \$14m in bank accounts, remain frozen by the Trading With The Enemy Act. The areas now opened up include:

- US imports of North Korean goods;
- the sale of most US consumer goods and financial services to North Korea;
- US investment in North Korean agriculture, mining, energy, lumber, transport and tourism;
- direct financial help by US citizens to relatives or other individual North Koreans;
- US transport of ordinary cargo to and from North Korea, by ship and plane; and
- commercial flights between the US and North Korea.

—but there may be few takers

Less clear is whether there will be many, or indeed any, takers. That which is now legal is not necessarily lucrative. The main beneficiaries are likely to be Korean-Americans, who can now send money to relatives or invest in North Korea fairly freely. Some had already found ways to do this, usually through China or Hong Kong, but it will be easier now. These apart, it is possible that a few large corporations—Coca-Cola, for example—will see symbolic value in setting up an operation in North Korea, as a gesture and a foot in the door rather than an immediate source of profit. Not that a population of around 22m is a negligible market, but, as currently organised, there is little chance to convert real need into purchasing power.

The pace of economic contraction slows—

On August 26th the Bank of Korea (BOK, South Korea's central bank) announced its latest estimates for North Korean economic growth, covering 1998. Although other analysts have in the past questioned the BOK's

methodology, in the absence of any coherent figures from North Korea these data are useful for trends and orders of magnitude, even if the apparent precision of decimal points may mislead.

—as real GDP falls by just 1.1% in 1998

The BOK estimates that North Korea's GDP fell in 1998 for the ninth successive year, but by much less—1.1%—than the falls of 6.8% in 1997 and 3.7% in 1996. This raises hopes that the plunge is bottoming out at last. By sector, agriculture in fact grew by 4.2% year on year, but manufacturing fell by 3.3%, while construction plummeted by 11.4%. In nominal South Korean won, the BOK estimated North Korea's GNP in 1998 at W17.6trn, barely 4% of South Korea's W443.1trn (in nominal terms) in the same year (an extremely bad year for Seoul). The gap in income per head is about 1:12; in dollar terms, North Korea's figure is just \$573.

North Korea records a trade deficit of \$320m in 1998

The BOK also gave figures for North Korea's trade in 1998, although as usual it excludes inter-Korean trade (South Korea is the north's third largest partner). On this basis, North Korea's merchandise trade fell sharply, by more than one-third, to just \$1.4bn in 1998 from \$2.2bn in 1997. Merchandise exports were \$560m and merchandise imports \$880m, giving a trade deficit of \$320m (the figures are presumably rounded). Inter-Korean trade also fell by 28% year on year to \$222m, although the balance improved. South Korea's financial and economic crisis hit imports of goods and raw materials from North Korea, while aid from Seoul and Hyundai's tourism project (see below) increased flows from south to north.

JETRO data show that merchandise exports plummeted in 1998

The Japan External Trade Organisation (JETRO) has offered its own trade figures, compiled from the statistics of 53 partner countries—and including South Korea. These give a year-on-year fall of 21.7%, from \$2.3bn in 1997 to \$1.8bn in 1998. Merchandise exports fell by 32% year on year to \$644.2m, while imports fell by half as much to \$1.2bn. China, Japan and South Korea (in that order) remained North Korea's leading three partners, but their aggregate share of overall trade shrank by 4.4% as trade with all three contracted.

Overall trade levels in 1998 are lower than in 1981 or even 1974—

Whatever the exact figures, the long-term trend is dismal and perhaps unique. JETRO noted that this is the first time that North Korea's total merchandise trade has fallen below \$2bn since 1981. Other studies suggest that in 1974 Pyongyang recorded more trade than in 1998, at \$2bn. Comparisons with South Korea simply go off the graph: South Korea trades twice as much in a week as North Korea does in a year.

—and 1999 may be even worse

Early figures suggest that this year's performance may be even worse. According to the Korea Overseas Trade Association (KOTRA), South Korea's equivalent of JETRO, North Korea's trade with its two main partners fell substantially again in the first half of 1999. Trade with China fell by 19.3% and with Japan by 24%. Exports to Japan fell by 16.8%, to \$87.4m, while imports from Japan plunged by 31.7% to \$64.5m. If this continues, total trade with Japan this year could fall below \$300m: again well below the norm in the 1980s, let alone the 1990s, and entailing a loss of hard-currency earnings, which Pyongyang can ill afford. Part of this, however, may be the effect of sanctions imposed by the

Japanese government after North Korea's rocket launch in August 1998. If these are now lifted in line with US policy, there could be some improvement in trade with Japan from 2000.

MOFAT shows that overseas earnings in 1998 total \$850m—

South Korea's Ministry of Foreign Affairs and Trade (MOFAT) told a parliamentary committee in Seoul on September 28th that, according to its estimates, North Korea's overseas earnings in 1998 totalled a modest \$850m. Of this, \$560m were from "normal" exports, \$100m from tourism earnings and \$50m from weapons sales. A further \$50m was sent by Chongryun, the pro-North Korea organisation of Koreans in Japan, while drugs and other criminal activity brought in \$100m.

—but revenue from weapons sales looks low

Clearly, many of these figures are to some extent guesswork. Other sources have given much higher figures—up to \$1bn annually in either case—for both weapons sales and Chongryun's remittances, although both of those probably err wildly on the high side. However, MOFAT's figure for arms sales seems very low; or conversely, if true, one may wonder why the US is so concerned by this minuscule trade. What is clear, however, especially once aid donations are included (see Inter-Korean relations), is that outside subventions—such as Hyundai's \$174m tourism fees in the first ten months of Mt Kumgang tours—now form a significant proportion of North Korea's hard-currency revenue.

Rajin-Sonbong may be losing out to Russia—

In one of the few fields where North Korea's sole declared special economic and trade zone (ETZ) has clear potential—namely for transit trade and as a regional entrepot—Rajin-Sonbong risks losing out to a rival just along the coast. Russia's Primorskii region has been upgrading the port of Posyet and improving its transport links, including a new rail line to China. Having already opened a sea route to the South Korean port of Sokcho in June, in August another route was announced: a triangular container service to Akita in Japan and Yangtse in China. A further link to Tonghae in South Korea is planned.

—and suffers from poor infrastructure

Almost eight years after being designated as a free zone (the word free was later withdrawn), Rajin-Sonbong has yet to tarmac its side of the main road to China used by trucks—which on the Chinese side has been upgraded with new flyovers and tunnels. No doubt North Korea is short of funds, but even so, without minimal investment in infrastructure, the zone will never be able to fulfil its potential.

A casino half-opens

Rajin-Sonbong's largest single investment is a casino/hotel by Hong Kong's Emperor Group, worth \$180m. The full project is still under construction, but the facility partly opened in July, using what will eventually be staff quarters to house punters. Hopes of luring big-spenders from across the border in China, or even further afield, are not facilitated by the practical difficulties of getting to the zone. Although a helipad exists, a company that has been trying to launch helicopter services into the zone for several years has not yet been cleared for take-off.

Nine foreign investment laws are partly revised—

The paucity of foreign investment in North Korea contrasts with the abundance of laws and regulations on the subject introduced during the past decade. According to Jin Gil-sang, a professor at the pro-north Korea University

in Tokyo, North Korea revised nine such laws earlier this year. In most cases the changes are to conform to constitutional revisions enacted in September 1998, and are in that sense formal: for example, adding mention and responsibility of the cabinet, as opposed to its predecessor, the State Administration Council.

—perhaps to rein in
Rajin-Sonbong

Some, however, seem more significant. For example, the former free zone law allowed the local authorities in Rajin-Sonbong to approve foreign investments worth up to W20m (about \$9m at the official exchange rate). Now, the role of local government is merely to be a postbox for the Central Trade Guiding Organ, or CTGO (formerly the Central External Economic Organ, or CEEO), which makes the decision. CTGO and CEEO are generic terms, but the actual bodies have also changed, with the former Committee for Promotion of External Economic Co-operation (CPEEC) being absorbed into the new Trade Ministry—whose Economic Co-operation and Control Bureau (ECCB) now controls Rajin-Sonbong.

Further ETZs are unlikely
to be established

It is hard to see this other than as an attempt to curb the relative autonomy of the ETZ, whose local government has also been reorganised, as in the rest of the country, by merging the formerly separate Administrative and Economic Committee into the People's Committee. On the other hand, official preference for foreigners to go to the ETZ rather than anywhere else in the country has been strengthened, although joint ventures outside the zone are allowed "if necessary". There seems to be no more talk of establishing further ETZs, although *de facto* Hyundai's Ongjin operation (see Inter-Korean relations) will become such if it gets off the ground.

Arbitration is on
Pyongyang's terms

Also perhaps ominously, the dispute resolution provisions in six different laws now simply state: "In case a dispute is not solved by negotiations, it will be settled by arbitration or court procedure defined by [North Korea]". In a related issue, on July 21st the Supreme People's Assembly Presidium adopted a new External Economic Arbitration Law, the 43 articles of which make it clear that North Korea regards arbitration as essentially an internal matter. Only one clause (Article 19, paragraph 4) allows that an arbiter may be "a foreigner experienced in economic affairs, if needed". True, Article 7 declares: "The State pays respect to international treaties and practices ...". Unfortunately it does not. A consortium of creditor banks obtained judgement against North Korea in the International Court of Arbitration several years ago, and Pyongyang took not the slightest notice. For as long as such insouciance persists, there are likely to be few investors.

Tax levels are now set by
the cabinet

Another change is that the revised laws no longer specify rates of taxation in various heads—personal, property, inheritance, business and vehicle—but simply state that this is decided by the cabinet. However, Mr Jin was assured in Pyongyang in mid-1999 that the cabinet has no plans to alter the existing tax rates "for the time being".

Quarterly indicators and trade data

South Korea: quarterly indicators of economic activity

		1997			1998				1999	
		2 Qtr	3 Qtr	4 Qtr	1 Qtr	2 Qtr	3 Qtr	4 Qtr	1 Qtr	2 Qtr
Industrial production	Monthly av									
General, seasonally adj	1995=100	115	117	116	103	101	104	115	117	124
Construction										
Permits issued ^a	'000 sq metres	10,659	8,251	11,263	5,871	4,309	2,987	3,822	3,179	5,273
Employment										
Employed	'000	21,319	21,336	21,070	19,710	20,179	20,049	19,924	19,105	20,362
Unemployed	"	550	470	561	1,182	1,485	1,597	1,588	1,748	1,435
Wages & prices										
Monthly earnings	1995=100	115.2	125.0	117.4	111.6	110.7	112.4	123.1	121.6	n/a
Consumer prices:	"	108.9	110.0	111.6	117.5	117.8	117.7	118.3	118.3	118.5
change year on year	%	4.0	4.0	5.1	9.0	8.2	7.0	6.0	0.7	0.6
Producer prices	1995=100	106.0	106.8	109.6	121.2	121.2	119.6	119.0	117.0	117.2
Share prices	"	78.6	78.5	53.2	55.1	40.3	34.5	47.5	62.1	n/a
Retail sales										
Constant value	1995=100	116	113	119	103	102	97	108	107	110
Money	End-Qtr									
M1, seasonally adj:	W bn	36,987	34,852	31,967	29,134	28,491	32,157	32,407	33,920	n/a
change year on year	%	5.1	-7.5	-11.8	-20.1	-23.0	-7.7	1.4	16.4	n/a
Foreign trade	Qtrly totals									
Exports fob	\$ m	35,532	34,182	36,727	32,232	34,878	30,481	34,723	30,342	36,060
Imports cif	"	37,362	35,688	34,517	23,655	23,541	21,462	24,624	25,571	28,739
Exchange holdings	End-Qtr									
Gold ^b	\$ m	84.1	79.4	77.0	96.0	97.2	93.5	95.9	93.6	89.4
Foreign exchange:										
Bank of Korea	"	33,316	29,654	19,710	29,677	40,764	46,904	51,963	57,089	61,630
other banks	"	33,793	34,912	32,749	41,925	38,478	37,239	34,310	33,441	n/a
Exchange rate										
Market rate	W:\$	888.1	914.8	1,695.0	1,383.0	1,373.0	1,391.0	1,204.0	1,227.0	1,157.6

Note. Annual figures of most of the series shown above will be found in the Country Profile.

^a 32 cities and 90 towns. ^b End-quarter holdings at quarter's average of London daily price less 25%.

Sources: Bank of Korea, *Monthly Statistical Bulletin*; IMF, *International Financial Statistics*.

South Korea: foreign trade

(\$ m)

	Total		US		Japan		China		Australia	
	Jan-Dec 1997	Jan-Dec 1998								
Imports cif	6,480	4,597	1,932	1,430	135	65	1,128	758	567	485
of which:										
cereals & preparations	2,028	1,716	975	988	1	1	534	388	150	150
Hides, skins, leather & mnfrs	2,018	1,014	832	515	35	21	143	63	24	6
Rubber & mnfrs	888	577	98	56	180	120	12	7	1	1
Wood & mnfrs	2,376	912	325	118	32	9	174	87	51	21
Pulp	1,161	974	533	403	23	28	1	0	1	2
Ores, slag & ash	1,744	1,712	74	26	4	2	76	45	612	648
Mineral fuels	27,381	18,196	798	403	279	148	1,239	728	1,287	1,310
Chemicals ^a	13,466	9,447	3,282	2,219	4,161	2,973	670	509	111	62
Textile fibres, yarns, cloth & mnfrs	4,623	3,016	516	452	581	362	1,272	856	244	169
Iron & steel & mnfrs ^b	7,541	4,164	944	515	2,532	1,658	1,510	460	169	117
Other metals & mnfrs ^b	5,459	3,796	608	430	857	601	375	330	468	406
Machinery & transport eqpt of which:	49,104	31,505	15,650	10,624	14,798	8,443	1,720	1,575	392	198
electrical & electronic eqpt	24,322	19,425	8,124	7,047	7,438	5,329	1,246	1,034	33	22
road vehicles & tractors	1,926	814	505	200	490	335	30	7	17	10
other transport eqpt	2,567	1,454	1,550	748	208	95	30	235	3	4
Clothing	1,309	484	53	11	61	16	643	264	6	1
Scientific instruments etc	6,836	4,060	1,965	1,013	2,993	1,521	124	115	47	30
Non-monetary gold	6,517	4,512	482	753	21	35	0	0	1,739	1,032
Total incl others	144,614	93,281	30,135	20,274	27,906	16,631	10,117	6,300	5,894	4,611

continued

	Total		US		Japan		China		Hong Kong	
	Jan-Dec 1997	Jan-Dec 1998								
Exports fob										
Food	2,667	2,428	150	144	1,500	1,456	146	117	141	124
of which:										
fish	987	941	26	19	735	677	112	92	2	16
Mineral fuels	5,349	4,595	140	222	1,709	1,189	1,565	1,150	759	677
Chemicals ^a	11,367	10,853	710	808	1,177	939	2,837	2,833	1,090	930
Hides & skins, leather & mnfrs	2,278	1,724	232	221	214	169	830	624	421	277
Rubber & manufactures	1,893	2,004	282	377	50	42	84	73	71	52
Paper & manufactures	1,531	1,726	112	227	53	60	457	508	429	356
Textile fibres, yarn, cloth & mnfrs	14,386	12,062	995	964	508	336	2,555	1,922	2,398	1,752
Iron & steel & mnfrs ^b	7,568	8,790	1,053	1,760	1,757	1,325	963	1,116	460	719
Other metals & mnfrs ^b	2,623	3,094	322	411	444	580	340	381	344	465
Machinery & transport eqpt	68,864	65,585	14,526	14,187	4,546	3,825	3,072	2,597	3,312	3,054
of which:										
electrical & electronic eqpt	34,049	31,820	8,379	8,264	3,514	2,818	1,512	1,420	2,625	2,465
road vehicles & tractors	12,328	11,434	2,273	2,051	125	91	80	110	82	63
other transport eqpt	7,935	9,446	534	544	137	222	76	56	154	147
Clothing	3,994	4,478	1,657	2,021	875	924	91	90	78	85
Footwear	982	810	211	175	218	176	188	149	47	29
Scientific instruments etc	2,437	2,931	533	533	485	364	123	71	140	149
Non-monetary gold	6,159	6,695	22	1	300	88	19	5	1,772	392
Total incl others	136,151	132,302	21,850	22,987	14,771	12,237	13,572	11,944	11,725	9,261

^a Including crude fertilisers and manufactures of plastics. ^b Including scrap.

Source: UN, *External Trade Statistics*, series D.

South Korea: structure of trade

(\$ m)	Jan-Dec 1994	Jan-Dec 1995	Jan-Dec 1996	Jan-Dec 1997	Jan-Dec 1998	Jan-Jun 1998	Jan-Jun 1999
Imports cif							
Food, beverages & tobacco	5,110	6,460	7,929	7,178	4,904	2,513	2,858
of which:							
cereals	2,256	2,852	3,835	3,101	2,520	1,408	1,133
Crude materials, inedible	9,405	11,713	10,965	10,424	7,275	3,558	4,014
of which:							
minerals	3,081	3,801	3,536	3,861	3,146	1,495	1,749
Mineral fuels	15,415	19,013	24,284	27,381	18,195	9,689	9,210
of which:							
crude petroleum	8,878	10,809	14,432	17,772	11,241	5,990	5,704
Chemicals	9,763	13,156	13,231	13,110	9,240	4,800	5,396
Manufactured goods	15,936	21,270	20,947	19,249	11,112	5,811	6,725
of which:							
iron & steel products	5,081	7,120	7,188	6,256	3,319	2,109	2,083
non-ferrous metals	3,210	4,796	4,319	4,664	3,347	1,720	1,831
Machinery & transport eqpt	37,408	49,437	54,675	48,722	31,216	15,500	19,618
of which:							
electric & electronic mach	17,199	23,258	26,474	28,592	21,583	10,425	14,154
transport equipment	5,193	6,030	6,655	3,964	2,138	1,083	1,029
Miscellaneous manufactures ^a	8,165	10,803	12,062	11,561	6,479	3,295	3,830
Total incl others	102,348	135,119	150,339	144,616	93,282	47,196	54,294
Exports fob							
Food, beverages & tobacco	2,396	2,803	2,918	2,841	2,580	1,260	1,259
Crude materials, inedible	1,430	1,790	1,608	1,780	1,541	813	706
Mineral fuels	1,746	2,472	3,866	5,349	4,595	2,485	2,165
Chemicals	6,339	8,944	9,148	10,666	10,235	5,275	4,899
Manufactured goods	22,949	27,568	26,959	29,097	28,584	15,080	13,442
of which:							
fabrics	8,109	9,203	9,330	9,580	7,850	4,175	3,779
metal goods	7,713	9,951	8,544	9,943	11,119	5,918	4,976
Machinery & transport eqpt	47,068	65,546	67,584	68,110	65,090	31,842	34,736
of which:							
electric & electronic products	25,189	35,017	34,021	36,745	34,284	16,741	20,246
passenger cars	3,839	6,551	8,255	8,635	8,167	3,740	4,132
ships	4,945	5,533	7,127	6,520	8,014	3,830	3,252
Miscellaneous manufactures ^a	13,504	13,382	12,237	12,032	12,421	5,871	6,715
of which:							
clothing	5,681	4,969	4,226	4,194	4,653	2,108	2,194
Total incl others	96,013	125,058	129,715	136,164	132,313	67,110	66,161

^a Including clothing and scientific instruments.

Sources: National Statistical Office, *Monthly Statistics of Korea*; Bank of Korea, *Monthly Statistical Bulletin*.

South Korea: direction of trade

(\$ m)

	Jan-Dec 1997	Jan-Dec 1998	Jan-Jun 1998	Jan-Jun 1999		Jan-Dec 1997	Jan-Dec 1998	Jan-Jun 1998	Jan-Jun 1999
Exports fob					Imports cif				
US	21,625	22,805	10,982	13,143	US	30,122	20,403	10,141	12,147
Japan	14,771	12,238	6,113	6,813	Japan	27,907	16,840	8,452	10,501
China	13,573	11,944	6,236	6,341	China	10,117	6,484	3,291	3,787
Hong Kong	11,725	9,261	5,033	4,254	Australia	5,894	4,642	2,262	2,342
Taiwan	4,613	5,140	2,463	2,830	Saudi Arabia	7,153	4,384	2,398	2,077
Singapore	5,797	4,065	2,020	2,188	Indonesia	4,107	3,058	1,586	1,792
UK	3,984	4,179	1,923	2,035	Germany	5,824	3,345	1,812	1,724
Germany	4,753	4,009	1,853	1,962	Malaysia	3,283	2,211	1,130	1,395
Malaysia	4,356	3,602	1,606	1,842	Taiwan	2,421	1,671	788	1,321
Philippines	2,601	2,832	1,346	1,419	UK	3,365	1,763	916	1,123
Indonesia	3,541	1,784	897	1,160	Singapore	2,417	1,713	775	1,085
Total incl others	136,164	132,313	67,110	66,161	Total incl others	144,616	93,282	47,196	54,294

Source: Bank of Korea, *Monthly Statistical Bulletin*.

North Korea: direction of trade

(%)

	Jan-Dec 1995		Jan-Dec 1995
Exports		Imports	
Japan	27.9	China	32.6
South Korea	20.8	Japan	17.2
China	5.2	Russia	4.7
Germany	4.0	South Korea	4.3
Russia	1.2	Germany	2.9

Source: Institute for International Economics, Washington DC, *The North Korean Economy*.

Country Profile: North Korea, July 2007. North Koreans were living in the South. This number contrasts with only nine living there in 1990, 41 in 1995, and 312 in 2000.Â Health: North Korea has a national medical service and health insurance system.Â There were no reported human immuno-deficiency virus/acquired immune deficiency syndrome (HIV/AIDS) cases as of 2007. However, it is estimated that between 500,000 and 3 million people died from famine in the 1990s, and a 1998 United Nations (UN) World Food Program report revealed that 60 percent of children suffered from malnutrition, and 16 percent were acutely malnourished. October 4, 1999 Web posted at: 10:36 p.m. EDT (0236 GMT). In this story: Sanctions also high risk.Â CNN's Jamie McIntyre reports on the decisions that could have led to another armed conflict with North Korea. Real. 28K.Â U.S. analysts believed the North Koreans took one main lesson from the 1991 Persian Gulf War: Don't give the United States time to mass its forces. Perry told Clinton all the options were unpalatable, but that not to pick one of them would be disastrous. 11th hour call from Jimmy Carter. "My recollection is that before the president got to choose -- was asked to choose -- the door of the room opened and we were told that there was a telephone call from former president Carter in Pyongyang and that he wished to speak to me," Gallucci remembered.