The Korean Economic Crises: Road to Recovery

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Ambassador of the Republic of Korea to Ireland
1. Where Korea Stands Now

2. The Financial Crisis of 1997

3. The 2008 Global Financial Crisis & the Korean Experience
Geopolitical Importance of Korea

- **Land Area**: 100,140km² (30% larger than Ireland)
- **Population**: 49 million (South)
- **Capital City**: Seoul
61 cities with population over 1 million within 3 hours

- Northeast Asia is home to 1/3 of the world’s population.
- Region’s purchasing power will be larger than that of US

Strategic Location of Korea: East Asia Business Hub

- Test Market
- High Tech, Mid Labor Cost

KOREA

- Large Market
- Low Labor Cost

CHINA

JAPAN

- Sophisticated Market
- High Technology

Vladivostok (2 ½ hrs)
Beijing (1 ½ hrs)
Shanghai (1 ½ hrs)
Hong Kong (3 ½ hrs)
Taipei (3 hrs)
Manila (3 ½ hrs)
Tokyo (2 hrs)
<table>
<thead>
<tr>
<th>Company Name</th>
<th>Company Name</th>
<th>Company Name</th>
<th>Company Name</th>
<th>Company Name</th>
<th>Company Name</th>
</tr>
</thead>
<tbody>
<tr>
<td>Samsung Electronic</td>
<td>LG</td>
<td>SK Holdings</td>
<td>Hyundai Motors</td>
<td>POSCO</td>
<td>GS Holdings</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Hanwha</td>
<td>Samsung Life Insurance</td>
<td>KoGas</td>
<td>S-Oil</td>
<td>Doosan</td>
<td>Samsung C&amp;T</td>
</tr>
<tr>
<td>Hyundai Heavy Industry</td>
<td></td>
<td></td>
<td></td>
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<td></td>
</tr>
</tbody>
</table>
### Global Context

#### South Korea

<table>
<thead>
<tr>
<th>Category</th>
<th>Rank</th>
<th>Score</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overall</td>
<td>15</td>
<td>83.28</td>
</tr>
</tbody>
</table>

#### Scores & Rank by Category

<table>
<thead>
<tr>
<th>Category</th>
<th>Rank</th>
<th>Score</th>
</tr>
</thead>
<tbody>
<tr>
<td>Education</td>
<td>23</td>
<td>Korea South: 87.93</td>
</tr>
<tr>
<td>Health</td>
<td>29</td>
<td>Korea South: 77.02</td>
</tr>
<tr>
<td>Quality of Life</td>
<td>3</td>
<td>Korea South: 73.02</td>
</tr>
<tr>
<td>Economic Dynamism</td>
<td>19</td>
<td>Korea South: 61.72</td>
</tr>
<tr>
<td>Political Environment</td>
<td>11</td>
<td>Korea South: 54.52</td>
</tr>
</tbody>
</table>

**Source:** Newsweek (August 2010)

<table>
<thead>
<tr>
<th>Category</th>
<th>Score</th>
</tr>
</thead>
<tbody>
<tr>
<td>Education</td>
<td>97.9%</td>
</tr>
<tr>
<td>Health</td>
<td>71 yrs</td>
</tr>
<tr>
<td>Quality of Life</td>
<td>31.6%</td>
</tr>
<tr>
<td>Economic Dynamism</td>
<td>$28.0K</td>
</tr>
<tr>
<td>Political Environment</td>
<td>79.0</td>
</tr>
</tbody>
</table>
From Rule-Taker to Rule-Maker

- The first non G8 country to host a G20 Summit
- Korea’s Initiatives:
  - Global Financial Safety Nets
  - Development Issue

Aid: From Recipient to Donor

- Joined OECD Development Assistance Committee (DAC) (Nov. 2009)

- Increasing Official Development Assistance (ODA)

<table>
<thead>
<tr>
<th>Year</th>
<th>ODA/GNI</th>
</tr>
</thead>
<tbody>
<tr>
<td>2008</td>
<td>0.09%</td>
</tr>
<tr>
<td>2012</td>
<td>0.15%</td>
</tr>
<tr>
<td>2015</td>
<td>0.25%</td>
</tr>
</tbody>
</table>
Korea is the only country that will conclude FTAs with two thirds of world markets or almost half the world’s population.

**Building Global FTA Networks**

Korea-EU FTA to come into Provisional Effect in July 2011
Background to the Crisis

The Side-Effects of Rapid Economic Growth

Government
- Alleged Unhealthy relationship with the private sector ("crony capitalism")
- Liberalization without adequate monitoring
  - Opening of the short-term financial market
- Government’s over-confidence with policy making

Corporate/Financial Sector
- Expansion oriented
  - Seeking to increase market share and diversify into various areas
- Over-reliance on foreign capital
- Establishment of multiple secondary financial institutions

Populace
- Growth of interest groups
- Increase in labour costs
<table>
<thead>
<tr>
<th>Unsustainable Current Account Deficit</th>
<th>Weak Economic Fundamentals</th>
<th>Unstable Financial Market</th>
</tr>
</thead>
<tbody>
<tr>
<td>- China’s abolition of its dual exchange rate regime (1994) - effective devaluation of Chinese currency</td>
<td>- Excessive investment → Excess capacity → Low capital efficiency → hindered overall growth</td>
<td>- Influx of short-term liquidity without adequate regulatory regime</td>
</tr>
<tr>
<td>- Decrease in External Competitiveness - Increased current account deficits</td>
<td>- Low profitability of businesses → increase in non-performing loans</td>
<td></td>
</tr>
</tbody>
</table>

- Financial Crisis in Southeast Asia
- Refusal of Bilateral Assistance - US, Japan
- IMF Bailout
Economic Index during the Crisis: 1. GDP Growth Rate

SOUTH KOREA GDP ANNUAL GROWTH RATE

source: TradingEconomics.com; Bank of Korea
## 2. Unemployment, Bankruptcy, Exchange Rate

<table>
<thead>
<tr>
<th>Date</th>
<th>Unemployed (per thousand Persons)</th>
<th>Unemployment Rate</th>
<th>No. of Bankrupt Companies</th>
<th>Ratio of Bankruptcy (%)</th>
<th>Exchange Rate (USD/KRW)</th>
</tr>
</thead>
<tbody>
<tr>
<td>September 1997</td>
<td>469</td>
<td>2.2</td>
<td>1,235</td>
<td>0.31</td>
<td>909</td>
</tr>
<tr>
<td>October 1997</td>
<td>451</td>
<td>2.1</td>
<td>1,435</td>
<td>0.43</td>
<td>922</td>
</tr>
<tr>
<td>November 1997</td>
<td>574</td>
<td>2.6</td>
<td>1,469</td>
<td>0.38</td>
<td>1,030</td>
</tr>
<tr>
<td>December 1997</td>
<td>658</td>
<td>3.1</td>
<td>3,197</td>
<td>1.49</td>
<td>1,501</td>
</tr>
<tr>
<td>January 1998</td>
<td>934</td>
<td>4.5</td>
<td>3,323</td>
<td>0.53</td>
<td>1,693</td>
</tr>
<tr>
<td>February 1998</td>
<td>1,235</td>
<td>5.9</td>
<td>3,377</td>
<td>0.62</td>
<td>1,618</td>
</tr>
</tbody>
</table>

Source: Bank of Korea
The Key Pillars of Recovery

Restoring External Competitiveness Through Forced Devaluation
- Massive Trade Surplus

Success in Rescheduling Debts with Creditors
  - Roll-over of Debts and Return of Foreign Capital

Right Policy Responses
- Restructuring of Economy and Liberalization of Markets
- Expansionary Monetary and Fiscal Policies
- Enhancement of Social Safety Net

National Support: Gold Collection Campaign (1997)
- 3.5m people
- 160 tons of gold (US$2 bn)
- Enormous symbolic Importance
Policy Responses: Reforms

**Corporate Sector Reform**
- Objectives
  - To enhance competitiveness
  - To concentrate on core businesses
- Streamline business structure
  - Big deals (swapping of business lines among Chaebols)
- Invite Foreign Participation (FDI)

**Financial Sector Reform**
- Objectives
  - To strengthen the financial system
  - To prevent a future financial crisis
- Restructuring: recapitalization/winding down
- Setup of Korean Asset Management Corporation
- Creation of consolidated regulatory agency

**Public Sector Reform**
- Reorganization of Government ministries and agencies
  - Transfer of some of functions of MOFE → National Budget Administration, Financial Supervisory Commission
  - Establishment of MOFAT
- Large-scale privatization
- Enhancing productivity of Public Sector

**Labour Market Reform**
- Establishment of the Tripartite Commission (Jan. 1998)
- Legalizing layoffs for managerial reasons
- Basic rights of workers restored
Financial & Corporate Sector Reform

Restructuring of Financial Institutions

<table>
<thead>
<tr>
<th></th>
<th>At the end of 1997 (A)</th>
<th>Closed or Merged (B)</th>
<th>(B/A)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Banks</td>
<td>33</td>
<td>16</td>
<td>0.48</td>
</tr>
<tr>
<td>Non-bank financial institutions</td>
<td>2,070</td>
<td>897</td>
<td>0.43</td>
</tr>
<tr>
<td>Total</td>
<td>2,103</td>
<td>913</td>
<td>0.43</td>
</tr>
</tbody>
</table>

Reorganization in the Automobile Sector

Before the crisis
- Hyundai
- Kia
- Samsung
- Daewoo
- Ssangyong

After the reform
- Hyundai-Kia merger
- Samsung → Renault Samsung
- Daewoo → GM Korea
- Ssangyong → sold to Mahindra
Policy Responses: Monetary and Fiscal Policies

Austerity Measures
(IMF prescribed)
- Increase in interest rates
- Recession in real economy
→ generated public criticism of the IMF

Enhancement of Social Safety Net
- Enhancing public assistance program
- Public works program/Vocational training/Government-paid internships

Government’s refusal to follow the prescription of the IMF

Expansionary Policies

Early Graduation from the IMF
- The Current Account turned into a large surplus (1998)
- Rapid economic recovery

Social Integrity
### Background to the Crisis

#### Abundant Liquidity and Inadequate regulation
- Intrinsic vulnerability of financial market (‘Financial instability hypothesis’ by Minsky)
- Globalization and liberalization of the financial market
- Financial engineering and development of new financial products (Operating outside of normal framework)

#### Structural Imbalance in World Economy
- Seriously unbalanced trading system
  - US suffering from chronic trade deficit ↔ China, Germany accumulating large surpluses
  - Dependence on an unsustainable expansion in US demand
- Unstable international financial market
  - Emergence of G-20 Summit

#### Other elements
- Greed
- Moral hazards

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**Global Financial Crisis**
Impact on the Korean Economy & Policy Responses

Impact on the Korean Economy

Severe Credit Crunch
- Sudden Capital Outflow
- Stock Market Plunge

Decline in FX Reserves
- Attack on Korean FX market
- Rapid depreciation of Korean Won

Battered Industrial Sector
- Rapid reduction of export demand
- Difficulty in maintaining stable balance sheet

Early Exit from the New Crisis

Bank Recapitalization Fund
- Slash of Interest Rate → Expansion of Domestic Liquidity

FX Liquidity Provision (USD 550 bn)
- Currency Swap Agreement with US, China and Japan
- Restored Confidence with International Investors

Increased export through aggressive marketing
- Recovered output
Fast Recovery from the Crisis

V-shaped GDP Growth after Crisis

Increase of FX Reserves

Asian Financial Crisis

Global Financial Crisis

* Projection of 2010 and 2011: Mosf

* Source: Ministry of Strategy and Finance
Contributing Factors behind the Fast Recovery

Robust Economic Fundamentals
- Positive effects of the Restructuring of Financial and Corporate Sectors following the 1997 Crisis

Pre-crisis Strong Policy against Speculation in the Real Estate Sector
- Timely preventive measures

Prompt Policy Responses

Positive Thinking of the Korean People
- “Crisis is opportunity”

Expansion of Exports and FX Reserves
- Improved External Competitiveness through Devaluation
- Expanded Investment, Improved Employment
Challenges Facing the Korean Economy

To Search for New Engines of Growth
- Green Industry / High Technology / High-value Added Services

To Redress Imbalances in the Domestic Economy
- the Gap between large corporations and SMEs
- the Gap between the rich and the poor

To Create Jobs
- Easing of unemployment for young people
- Support to the Service Sector

To Play a Leading Role in the Global Market
- Establish a more favorable trade and business environment
Learning from the Crisis

**Embracing Flexibility and Change**
- Need to change mindset to reflect dynamic nature of economy
- Pursue fresh ideas and identify appropriate models

**Winning over Competition**
- Improve productivity and reduce costs
- Secure new markets ahead of competitors

**Building a Robust Domestic Economy**
- Boost local enterprise and invest in key SOCs
- Avoid over-reliance on external assistance

**Social Consensus for Painful Decisions**
- Social unity in pursuit of an early exit from crisis
- Equitable burden sharing (Government, corporate, public)
Thank you!