

# Ten Years After the Crisis

## Lessons from Korea



**Doo Yong Yang**  
**Korea Institute for International Economic Policy**

# CONTENTS

- ◆ 1. Recent Economic Performance .....
- ◆ 2. Economic Changes since the Crisis .....
- ◆ 3. Challenges and Opportunities from the crisis .....
- ◆ 4. Implication for Regional Monetary and Cooperation .....

# Recent Economic Performance

2. Economic Changes since the Crisis

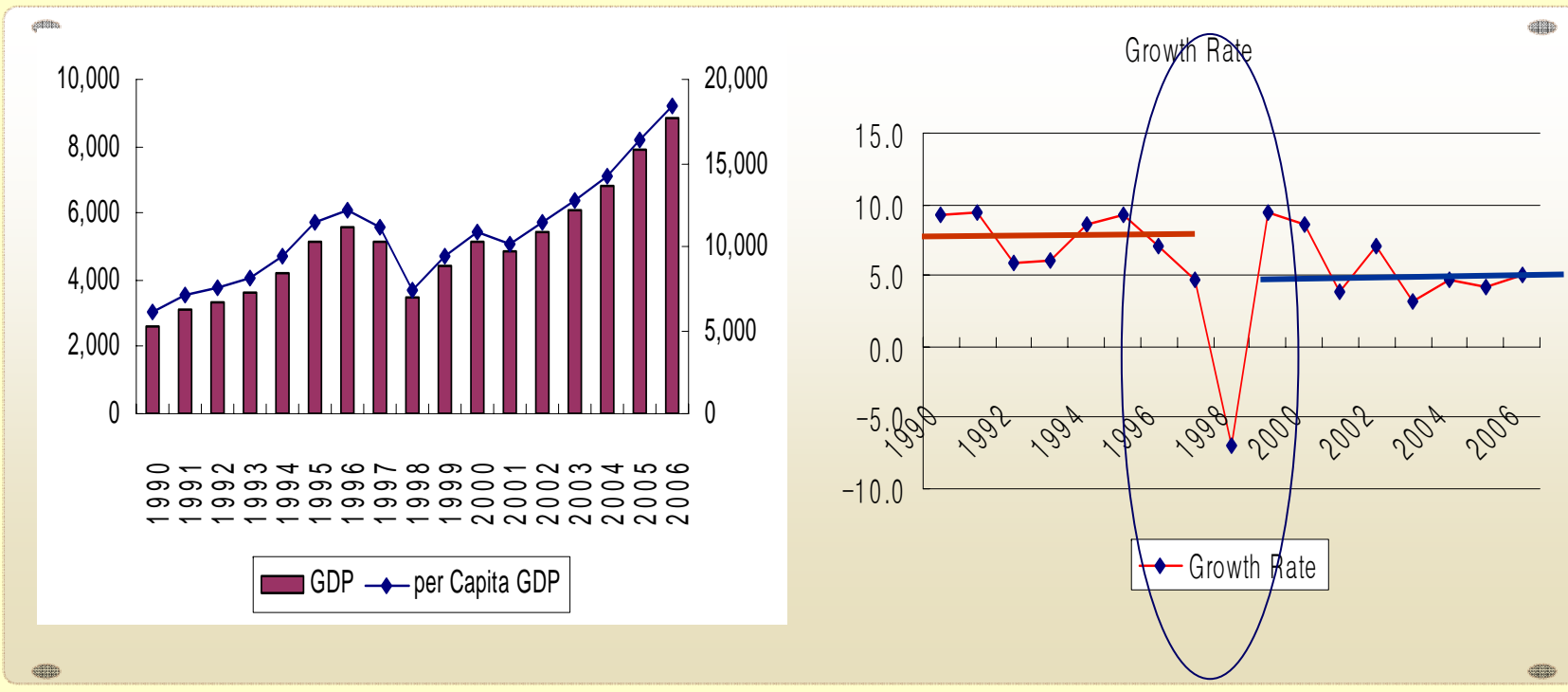
3. Challenges and Opportunities from the crisis

4. Implication for Regional Monetary and  
Cooperation

# Economic Performance

## ◆ Economic Growth

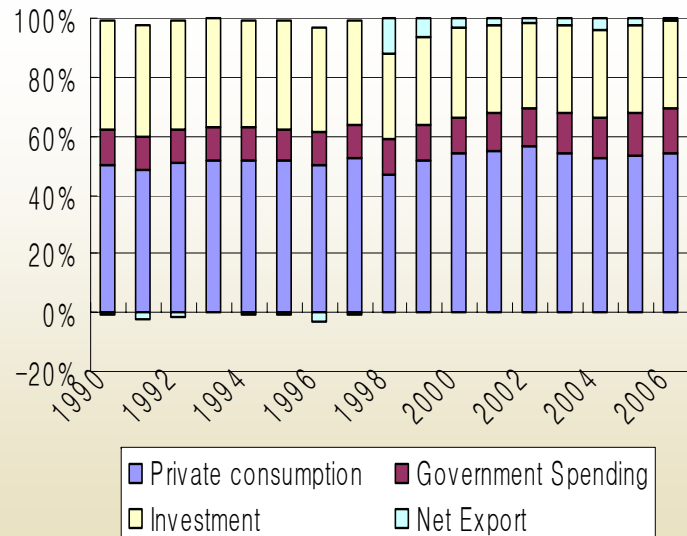
- GDP recorded \$887.4 billion in 2006
- Per Capita GDP reached over \$18,000 in 2006
- GDP growth rate was 5% in 2006



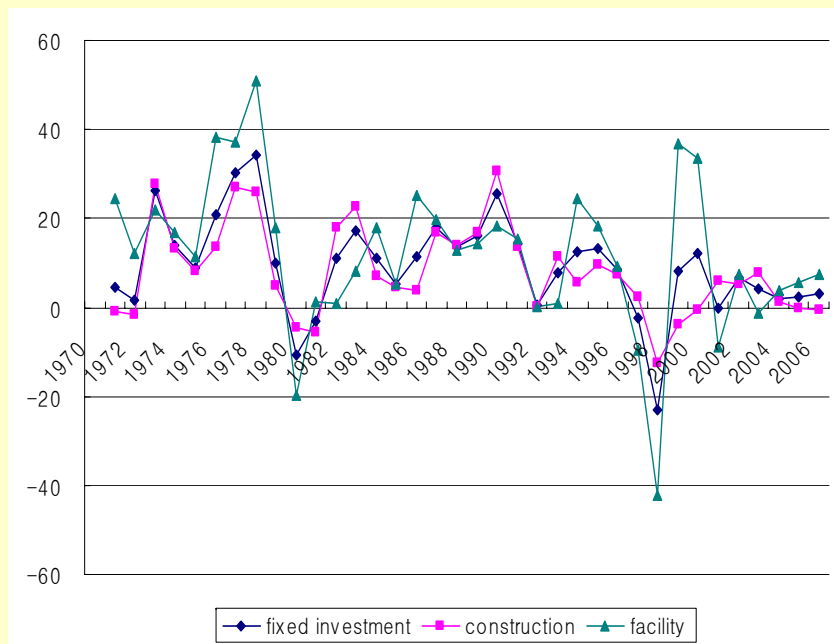
# Growth Components

Share of Consumption to GDP is slightly increasing since 1998

Investment is decreasing since the crisis

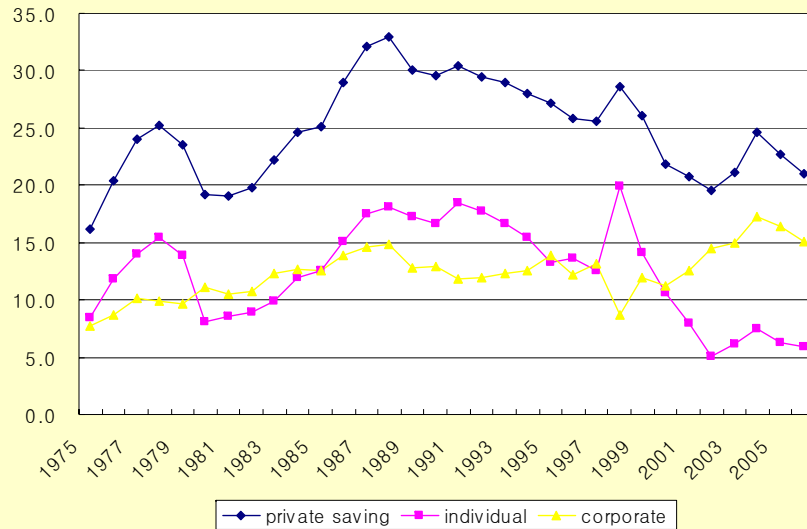


But investment is slightly picking up in 2007



# Growth Components

Saving has been declining, but corporate saving is increasing since the crisis

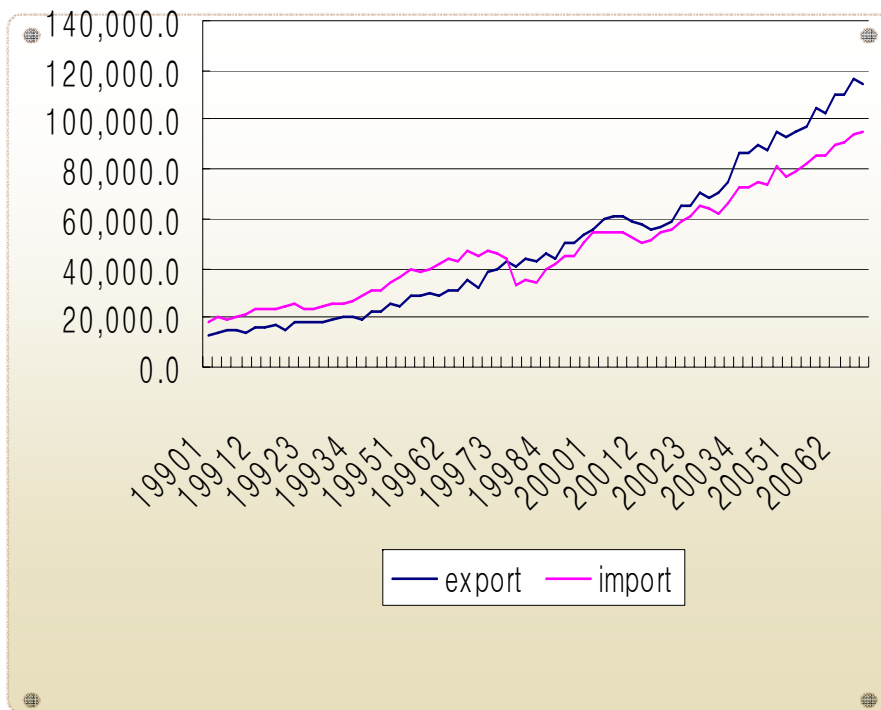


Labor productivity is gradually decreasing

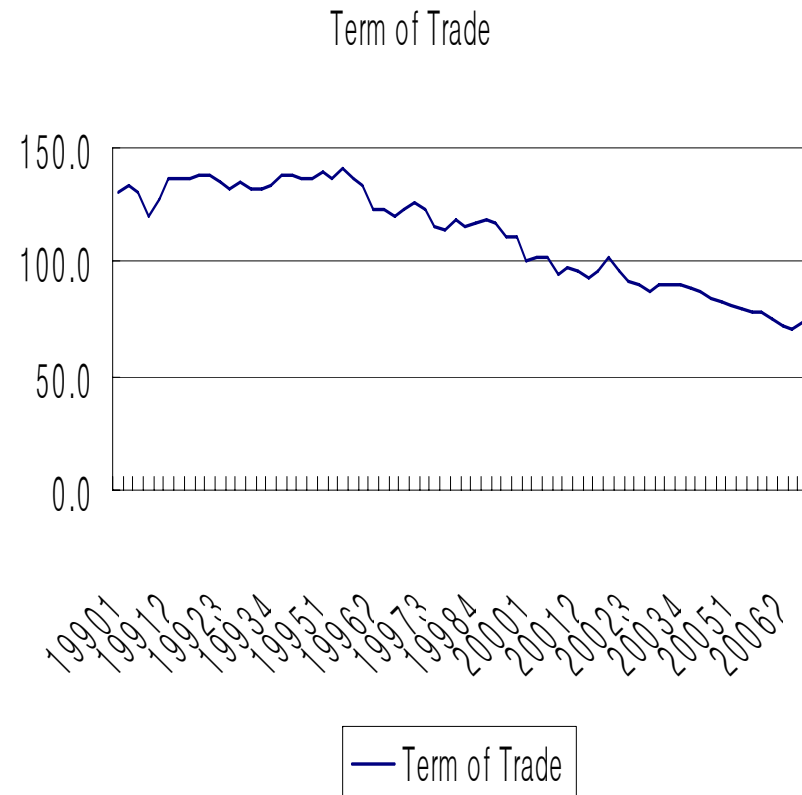


# Growth Components

Export increase supported by robust global demand

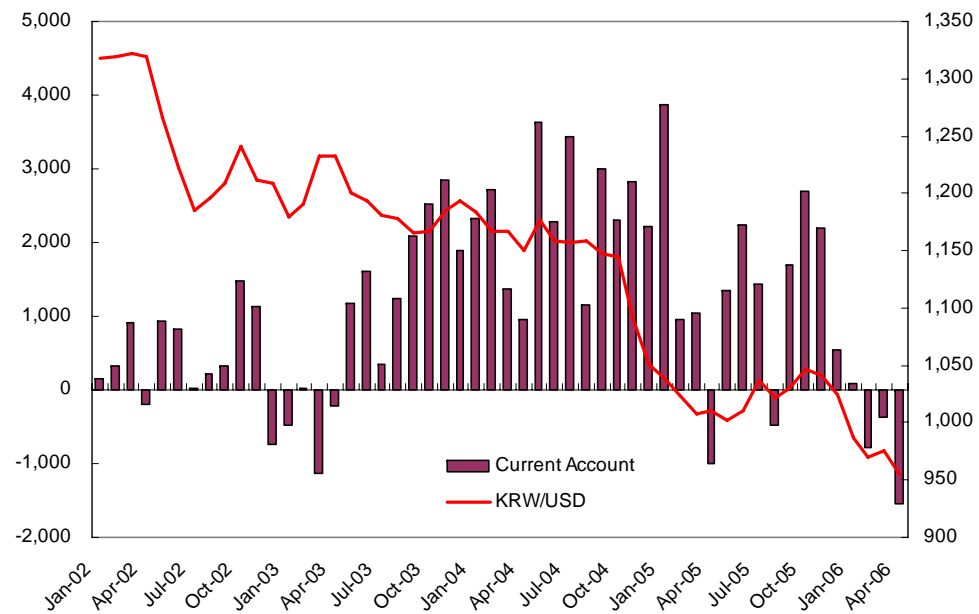


Term of Trade deteriorate since the middle of 1990s



# Won-dollar exchange rates

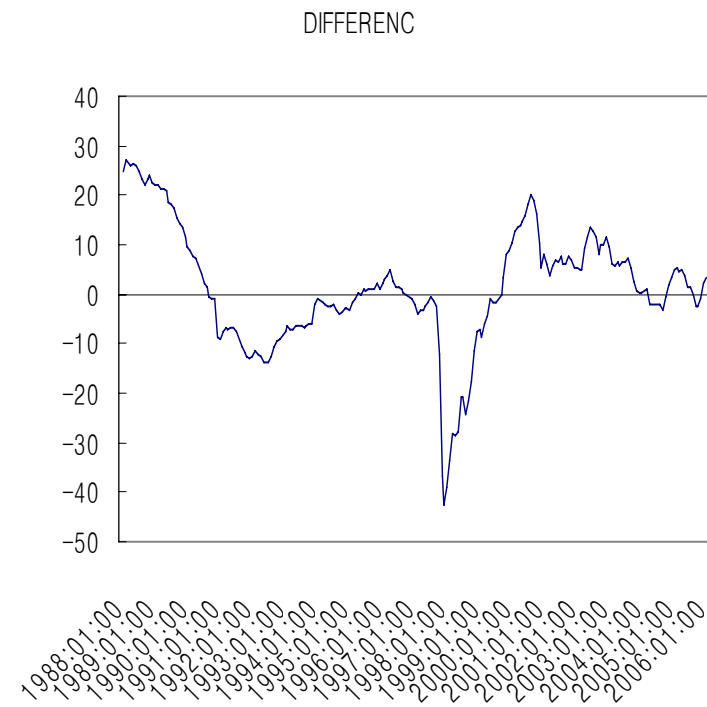
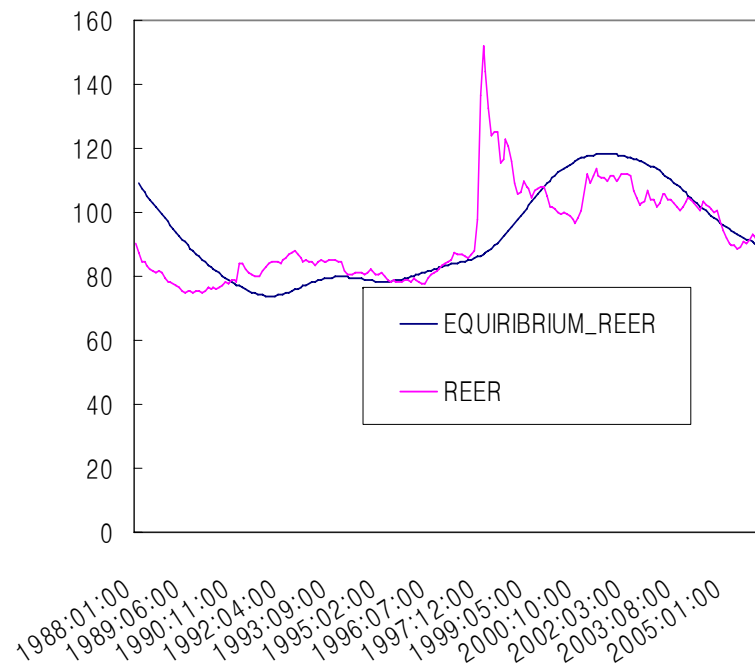
Won/dollar rates are closely related with the current account balance





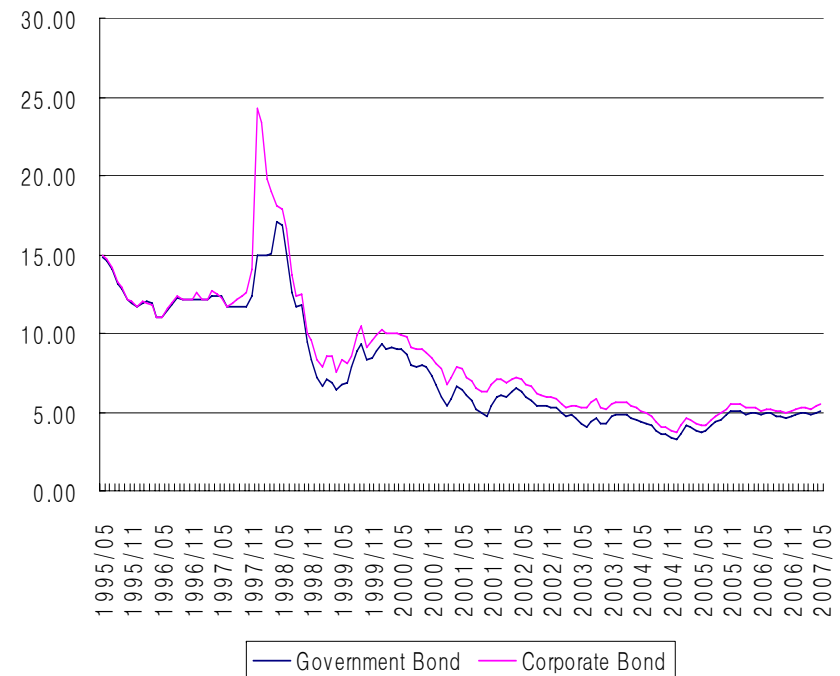
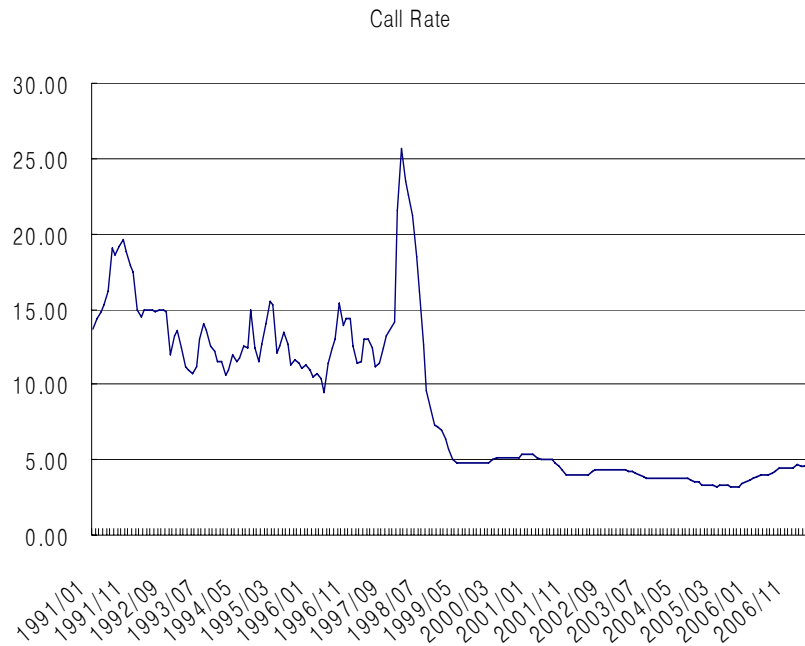
# Won-dollar exchange rates

Won/dollar exchange rates reached almost long-run equilibrium level

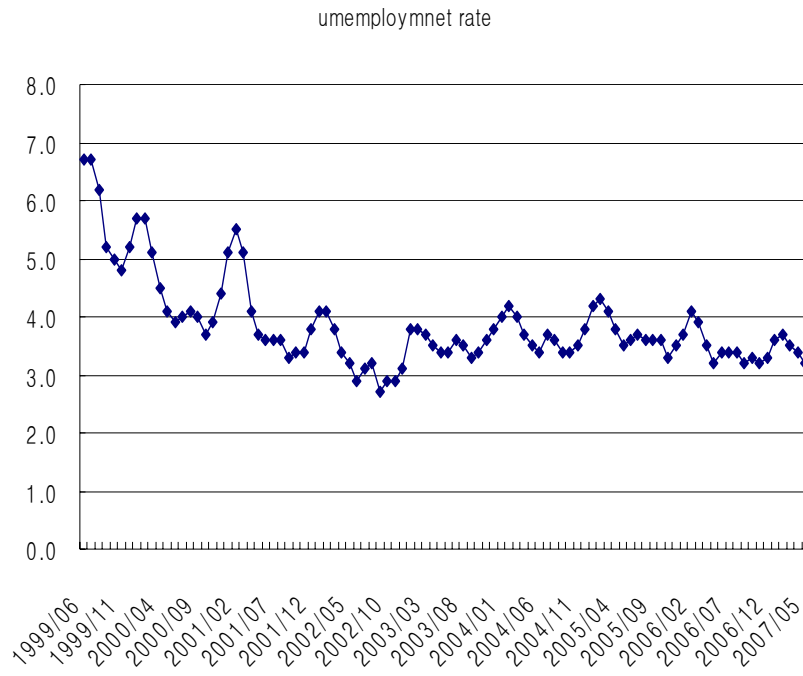


# Interest Rates

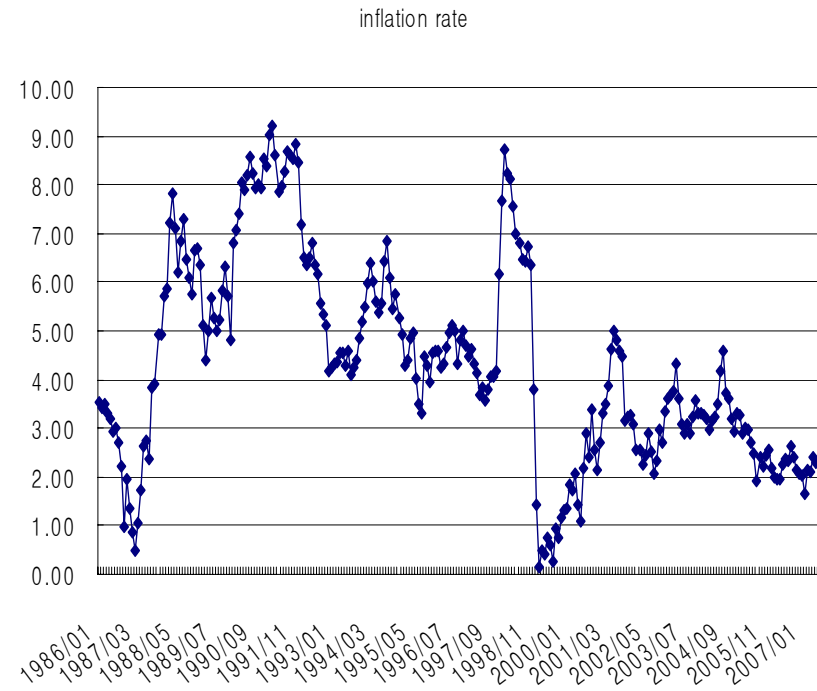
Interest rate has been lower since the crisis, and the risk premium has reduced, but prevailed



Unemployment rate is stabilized  
in lower level, but out of labor force  
increased



Inflation rate is lowered



# CONTENTS

1. Recent Economic Performance

## Economic Changes since the Crisis

3. Challenges and Opportunities from the crisis

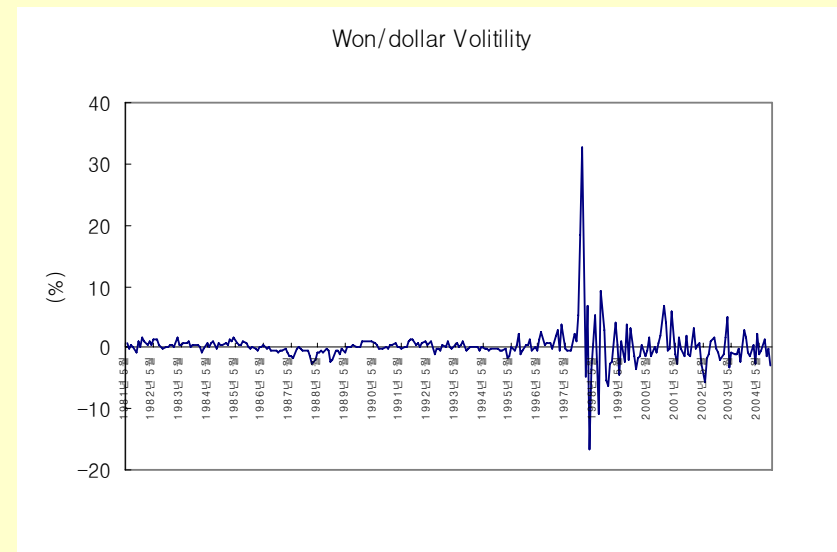
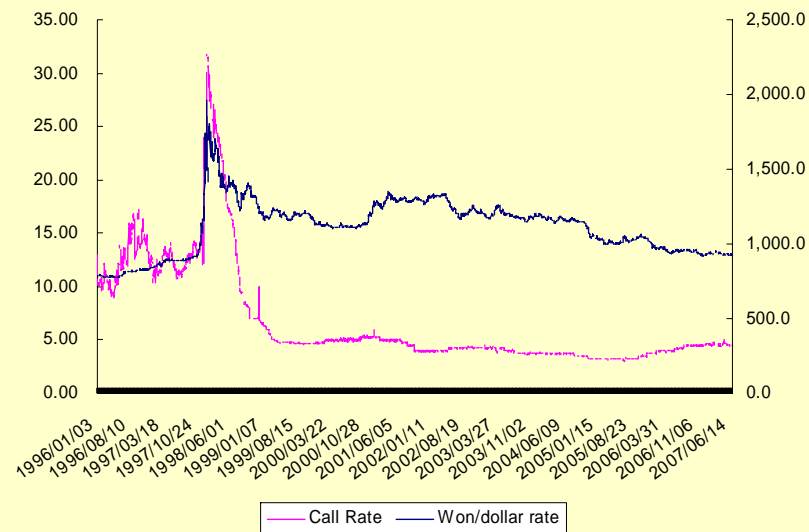
4. Implication for Regional Monetary and  
Cooperation

# Economic Changes since the Crisis

## Macro Economic Policy

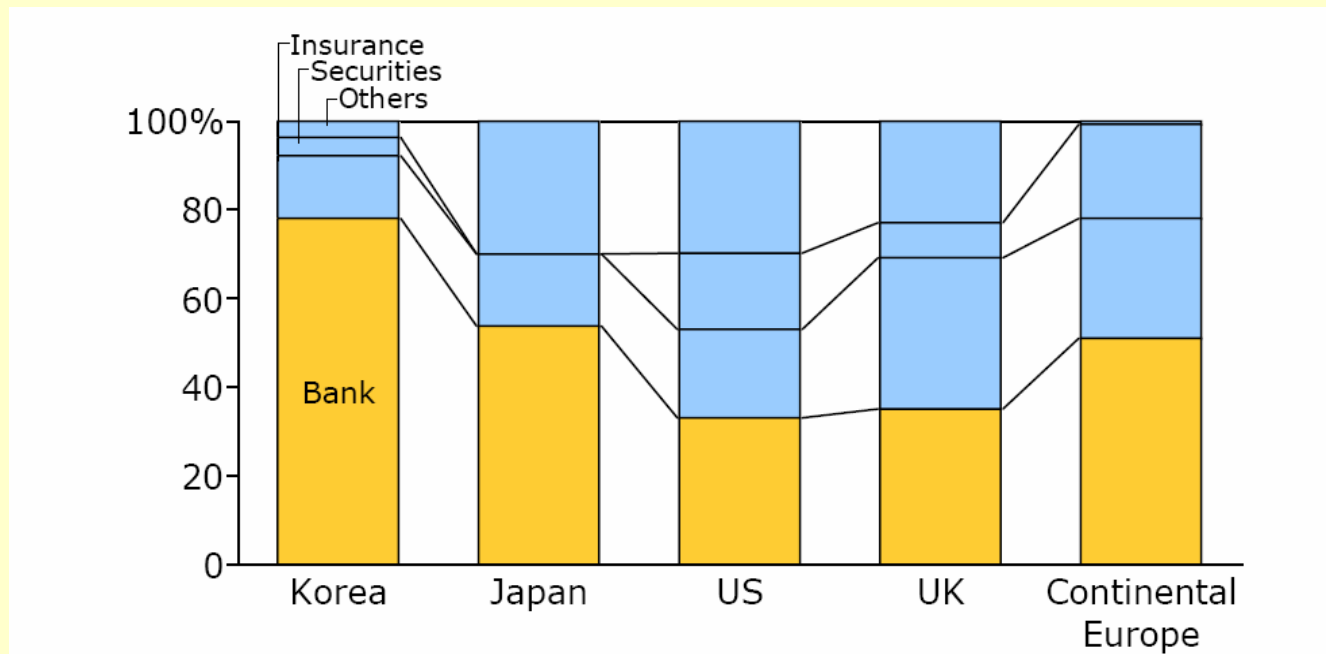
### Inflation Targeting and Flexible Exchange Rate Regime

- Since 1998, Korea adopted inflation targeting with free floating exchange regime, However, in the early stage, the level of target is too high (9% of CPI), In 1999, the target range lowered to 3% of core inflation. Currently 3%  $\pm$  0.5 of three years' average CPI
- However, there is a potential conflict between inflation targeting and exchange rate



## Financial Market Development

1. Government-led financial market restructuring
2. Bank-focused capital clean-up
3. M&A of financial institutions by government



## The banking sector is healthy

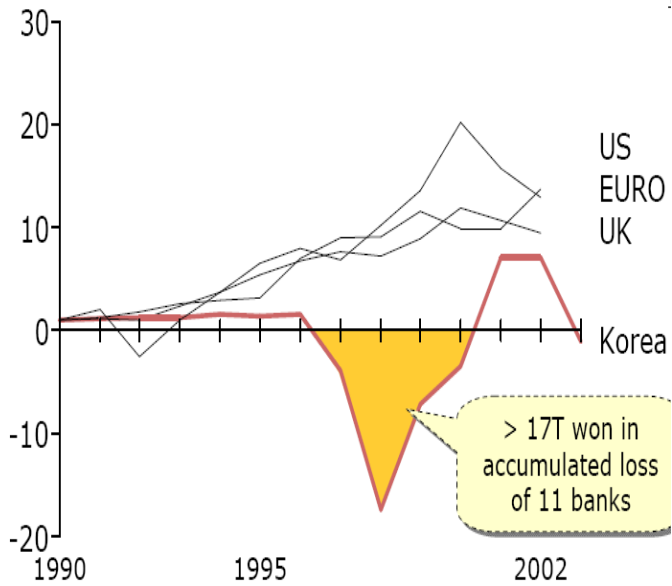
Nation-wide banks, in trillion won

	1998	2001	2002	2003	2004
Before-tax profits					
Net profits	-3.2	9.0	9.0	10.7	12.8
Net profits minus loan loss provisions	-10.1	3.6	3.7	0.3	6.0
After-tax profits	-10.1	3.4	2.9	0.2	5.9
Return on equity (per cent)	-48.63	16.30	10.95	0.87	18.23
Return on assets (per cent)	-2.99	0.79	0.56	0.04	0.89
Total loans (A)	263.9	353.2	432.2	463.9	473.0
Substandard loans or below <sup>1</sup> (B)	19.0	11.7	10.6	13.1	9.4
Ratio to total loans (%) (B/A)	7.2	3.3	2.4	2.8	2.0
Loan loss reserves (C)	12.1	8.8	8.8	10.7	9.1
Reserves to substandard loans or below <sup>1</sup> (%) (C/B)	63.8	75.3	83.5	82.1	96.6
Capital adequacy ratio (B/S ratio)	8.22	10.81	10.46	10.34	11.31
Number of branches	4,164	4,052	4,304	4,345	4,333

1. Includes loans classified as substandard, doubtful and estimated loss.

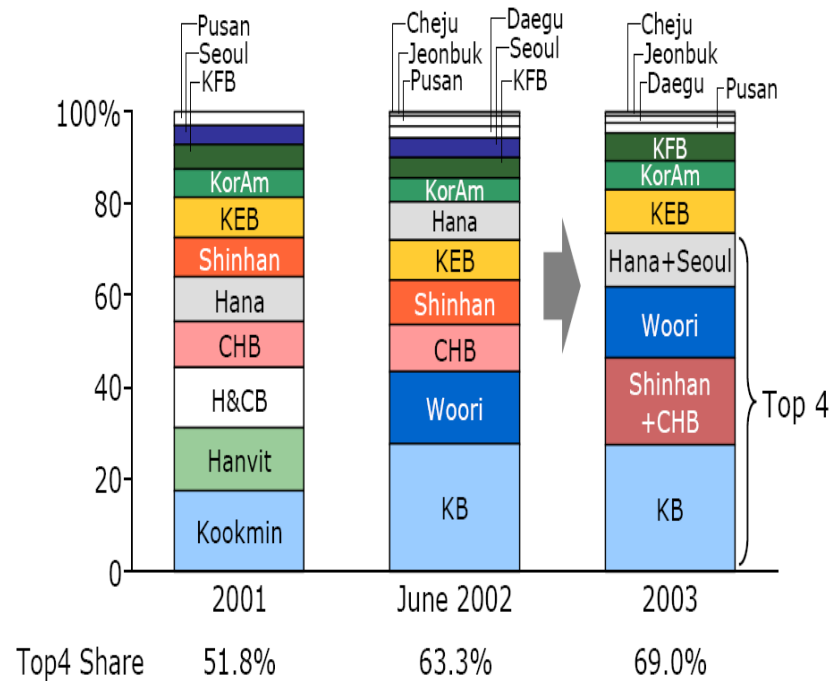
# Economic Changes since the Crisis

Annual earnings (indexed to 1990)  
(Net income/loss)



Note: Indexed to 1990

Market Share  
(based on Asset Size)





## Corporate Sector

There are fundamental changes in corporate sector since the crisis

1. Economic criteria is major factor in determining the bankruptcy rather than previous non-economic criteria
2. Corporate restructuring market has developed since the crisis. KAMCO, CRC, CRV, CRF, PEF
2. Rehabilitation procedures are improved but heavily concentrated in the financial restructuring rather than operational restructuring
3. Despite the improvement in financial statement, overall profitability remained weak because of large interest burden and lack of operational restructuring, but recently increasing due to lower debt/equity ratio

# Economic Changes since the Crisis

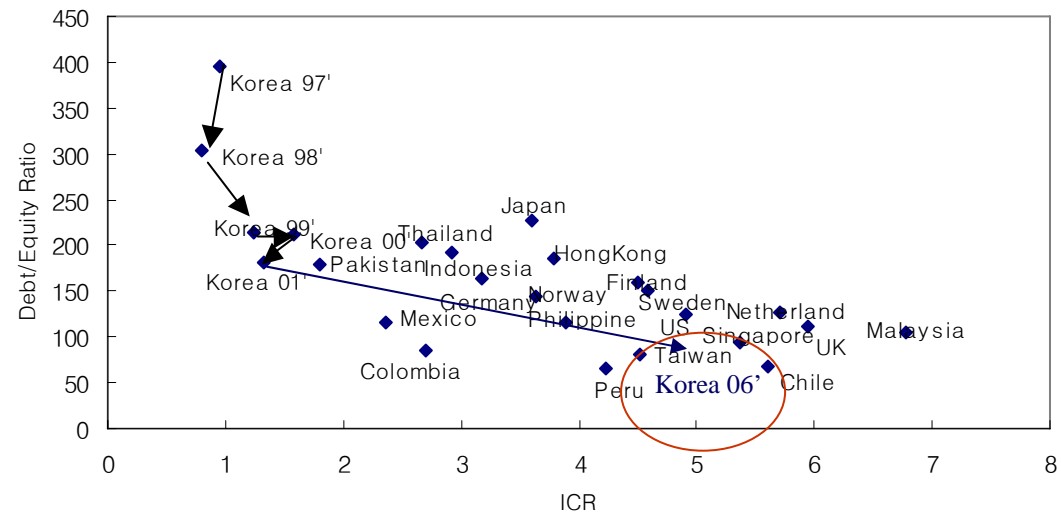
**There has been a marked improvement in the health  
of the corporate sector**

**The manufacturing sector**

	1997	1999	2000	2001	2002	2003	2004
<b>Financial indicators</b>							
Debt-equity ratio	396.3	214.7	210.6	182.2	135.4	123.4	104.2
Total borrowing-assets ratio	54.2	42.8	41.2	39.8	31.7	28.3	24.0
Current ratio	91.8	92.0	83.2	97.9	106.1	109.8	117.0
Asset turnover ratio	0.90	0.82	0.96	0.98	1.08	1.10	1.20
<b>Profitability indicators</b>							
Operating profit-sales ratio	8.3	6.6	7.4	5.5	6.7	6.9	7.6
Labour cost-sales ratio	11.4	9.8	9.7	10.0	10.1	10.3	9.7
Labour cost-total operating cost ratio	13.6	11.5	11.5	11.7	11.9	11.8	11.3
Ordinary profit-sales ratio	-0.3	1.7	1.3	0.4	4.7	4.7	7.8
Financial expense-sales ratio	6.4	6.9	4.7	4.2	2.6	1.9	1.3
Average interest rate	10.6	11.5	10.5	9.4	7.7	6.8	5.9
Interest coverage ratio <sup>1</sup>	129.1	96.1	157.2	132.6	260.3	367.1	575.8

1. The ratio of operating profits to interest expenses.

# Economic Changes since the Crisis



# CONTENTS

◆ 1. Recent Economic Performance .....

◆ 2. Economic Changes since the Crisis .....

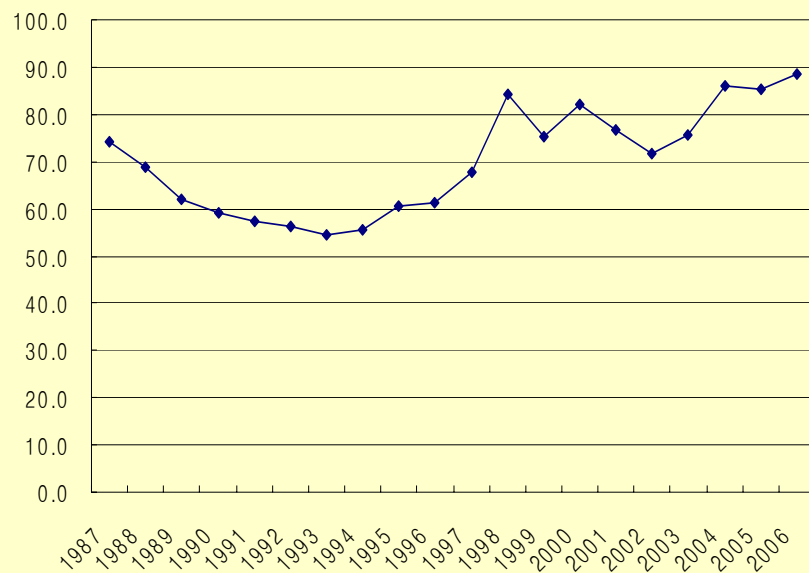
**Challenges and Opportunities from the crisis**

◆ 4. Implication for Regional Monetary and Cooperation .....

## 1. More Open Economy

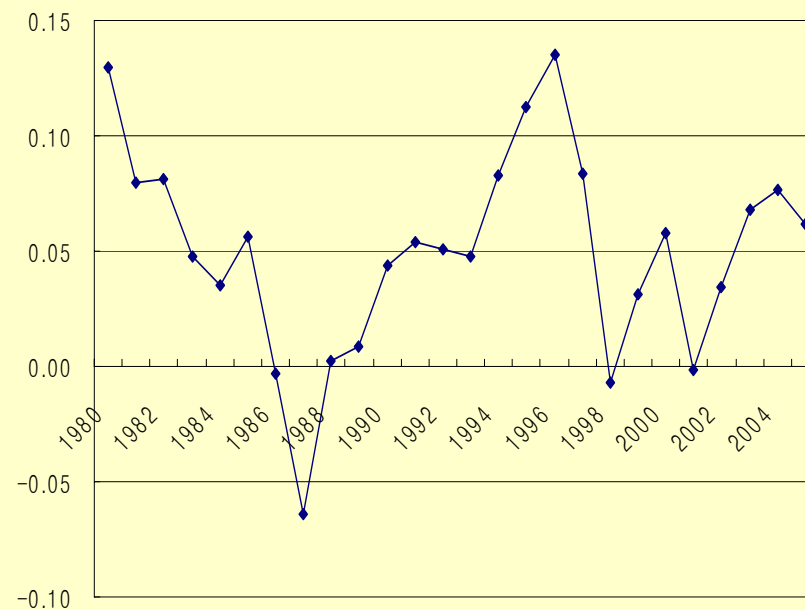
### Real sector

(Export+Import)/GNI



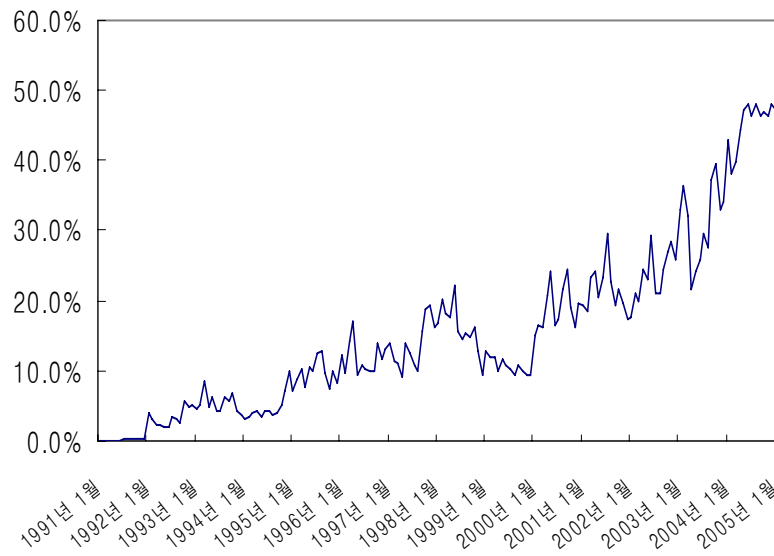
### Capital flows

(inflow+outflow)/GDP

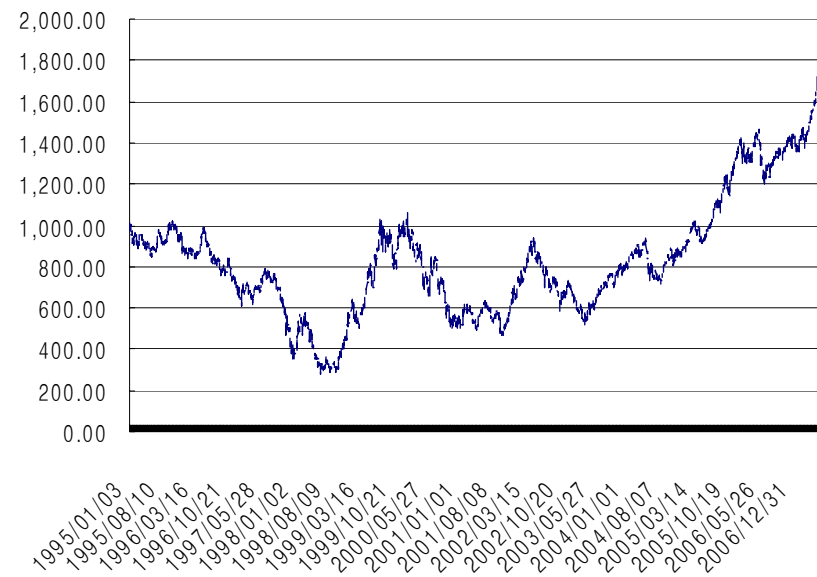


## Foreign equity investment has increased dramatically

Share of foreign investment in equity market

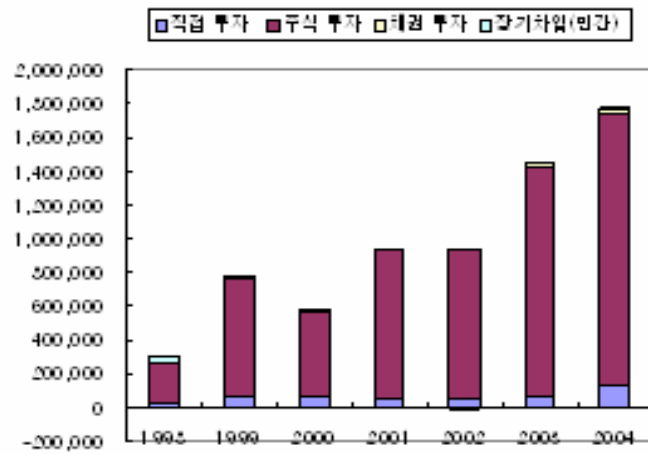


KOSPI



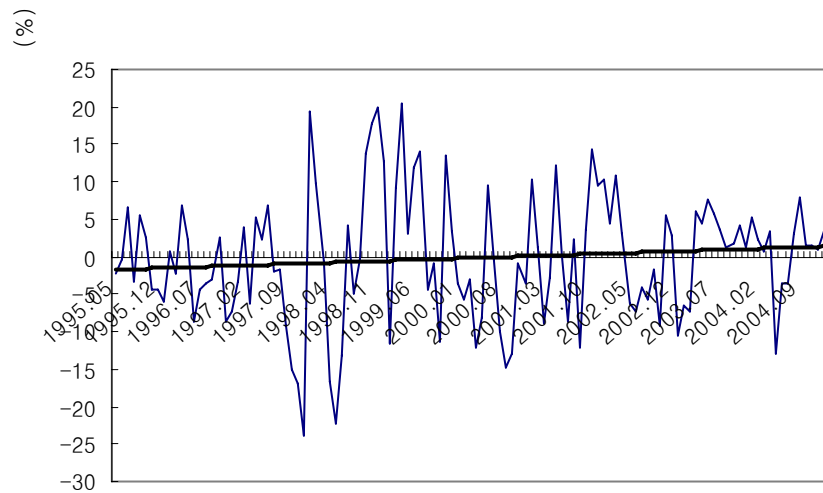
# Challenges and Opportunities from the Crisis

Most foreign capital inflows are concentrated in equity market



	FDI	Equity	Bond	LT-borrowing
1998	10.3	74.7	3.2	11.8
1999	7.6	90.0	1.5	0.9
2000	11.3	86.2	1.2	1.3
2001	5.8	94.4	0.5	-0.6
2002	5.5	94.8	0.7	-1.0
2003	4.3	94.2	1.2	0.3
2004	7.6	90.2	1.8	0.5

## Equity premium turn into positive



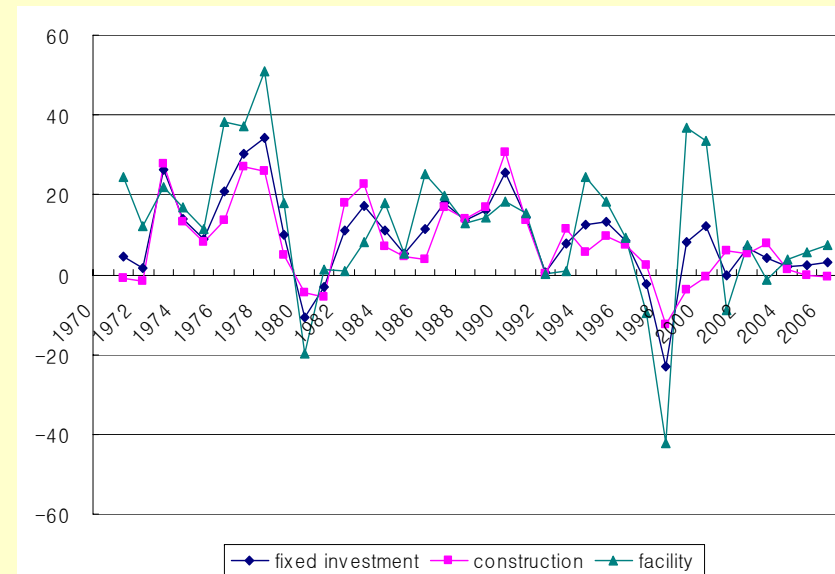
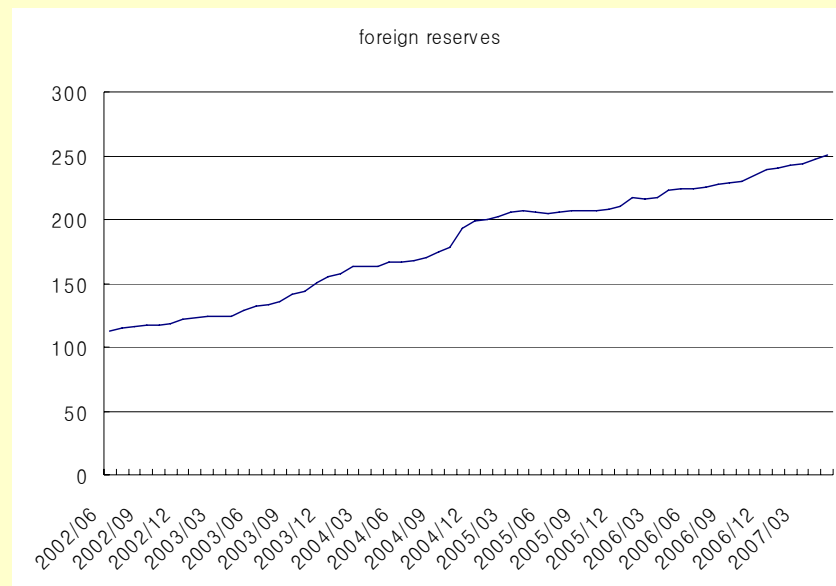


## 2. More Risk Averse

### - Global Imbalance

More prudent in public sector: increasing foreign reserve

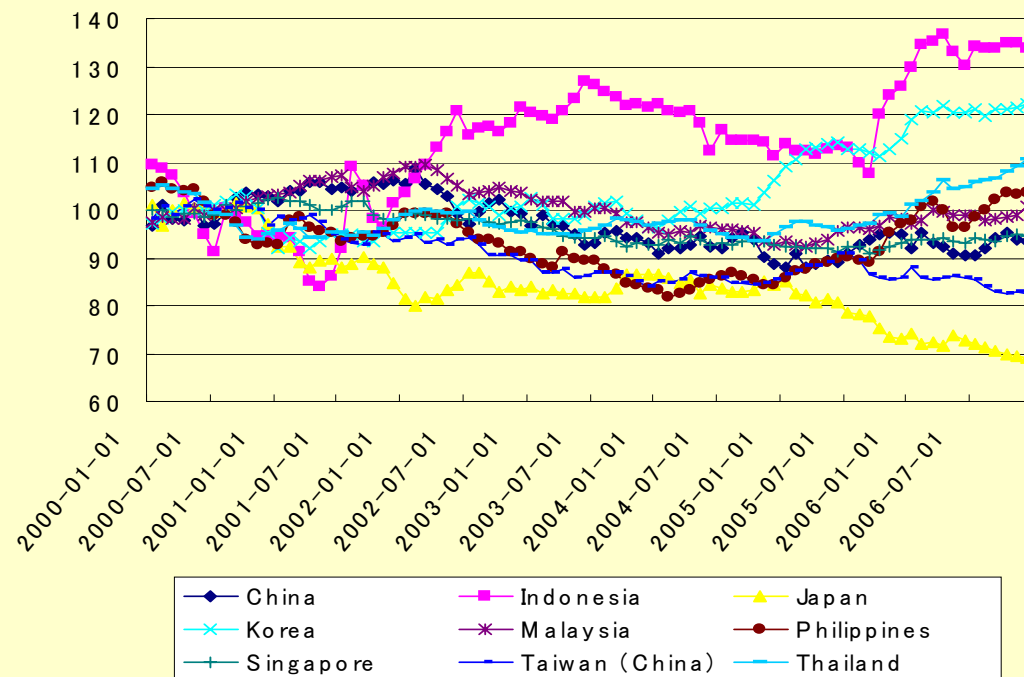
More risk averse in private sector: decreasing investment



## 3. More Flexible Exchange Rates

Exchange rate appreciates more than most Asian economies

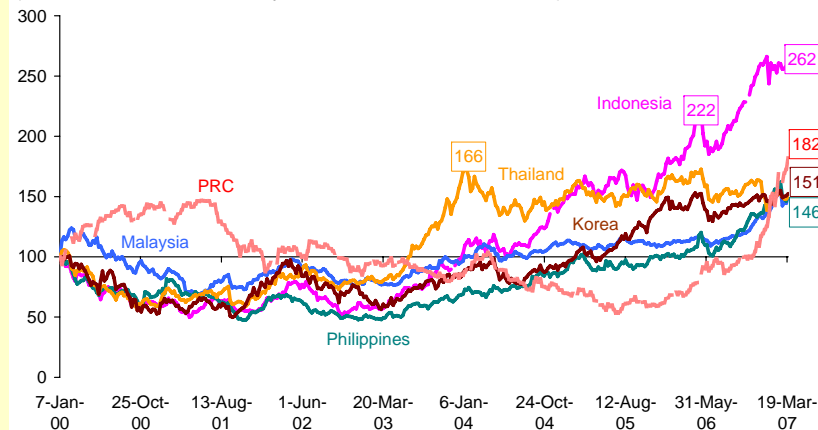
Inflation targeting is appropriate for SOE (Chung, Jung and Yang, 2006)



## 4. More Liquidity

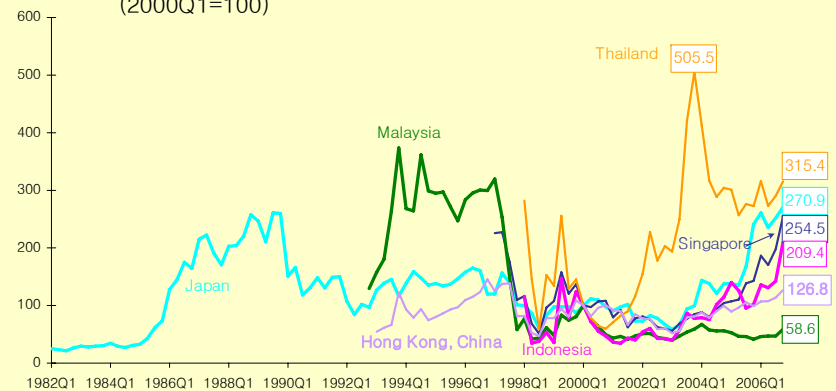
More liquidity in the market create asset price hike (Kim and Yang, 2007)

Figure 1: Composite Stock Price Indexes<sup>1</sup>—ASEAN-4, PRC and Korea  
(end of week, 7 January 2000 = 100<sup>2</sup>, local index)



<sup>1</sup> Weekly averages of PRC (Shenzen), JCI (Indonesia), KLCI (Malaysia), PCOMP (Philippines), SET (Thailand).  
Source: OREI staff calculations based on Bloomberg data.

Figure 3: Property Indexes for Selected East Asian Economies<sup>1</sup>  
(2000Q1=100)



<sup>1</sup>TPREAL Index (Japan), SESPROPO Index (Singapore), KLPRP Index (Malaysia), JAKPROP Index (Indonesia), SETPROP Index (Thailand), HSP ndex (Hong Kong, China).  
Source: Bloomberg.

# CONTENTS

- ◆ 1. Recent Economic Performance.....●
- ◆ 2. Economic Changes since the Crisis.....●
- ◆ 3. Challenges and Opportunities from the crisis.....●

**Implications for Regional Monetary and  
Financial Cooperation**

- 1. Regional Monetary and Financial Cooperation should be strengthened**
  - current challenges in Asia's EME can't be solved by individual economies
- 2. CMI phase II should more focused on structural issues such as policy cooperation in order to solve the major challenges in the region**
- 3. Financial Market integration is crucial for regional economic growth, and provide a possible solution for global imbalances**

The image features a bright orange background that resembles a folder. In the top right corner, there is a grey, three-dimensional tab. Centered on the orange surface is the text "THANK YOU" in a bold, black, sans-serif font, which is slightly tilted upwards to the right.

**THANK YOU**