

Current Economic and Financial Movements

Summary

During the second quarter of 1997, the Korean economy showed a higher growth rate than in the previous quarter, due to the expanded pace of the increase in exports. Domestic demand, however, continued to be sluggish, and as a result, the current account deficit narrowed and prices displayed stabler movements than in the previous quarter.

The GDP growth rate rose to 6.3 per cent in the second quarter from 5.5 per cent in the first quarter, supported by a large increase in exports, whose positive effects were only partially offset by the continued slackening of domestic demand, particularly private consumption and investment. Thus, the national economy grew by 5.9 per cent over the first half of the year.

Exports, on a customs-clearance basis, shifted to a 7.3 per cent increase during the quarter under review from a 5.6 per cent decrease during the previous quarter. In July, the pace of their increase accelerated to 19.3 per cent. This improvement was attributable to the recovery in the prices of main export products such as iron and steel products and chemical products, although it also reflected the low growth rate of exports in the base quarter of the previous year. In contrast, imports, on a customs clearance basis, showed only a slight increase of 0.6 per cent during the second quarter and shifted to a 0.8 per cent decrease in July. This was mainly due to the sluggishness of domestic demand and stable international prices of raw materials. As the growth rate of exports exceeded that of imports, the current account deficit narrowed to 2.7 billion U.S. dollars during the second quarter from 7.4 billion U.S. dollars during the previous quarter. Thus for the first seven months of the year, the current account accumulated a deficit of 11.1 billion U.S. dollars, less than the 12.2 billion U.S. dollars for the same period of the previous year.

Producer prices maintained a stable range of movements, rising by 0.6 per

cent during the second quarter and dropping by 0.4 per cent in July. Consumer prices maintained a stable range of movements from May onwards, holding to a 0.1~0.2 per cent increase per month. Thus during the January-July period, the rate of consumer price increases moderated to 2.6 per cent over those in December of the previous year, as against their 4.2 per cent rise in the same seven month period a year earlier.

Viewing monetary and financial movements, the growth rate of MCT(M_2 +CDs+Money-in-trust), on a period average basis, eased to 15.3 per cent in the second quarter from 18.2 per cent in the first quarter, and further slowed to 15.1 per cent in July. This was mainly due to the contraction of corporations' demand for funds in view of the lackluster economic conditions. Market interest rates eased steadily during the second quarter of this year, but shifted back to an upward trend in July, reflecting the recurrence of financial market instability caused by the Kia Group's difficulties.

Economic Movements

Economic Growth

During the second quarter of this year, GDP growth rate rose to 6.3 per cent from the 5.5 per cent of the first quarter. This was mainly attributable to the large expansion in the volume of exports, which more than offset the sluggishness of domestic demand, particularly private consumption and investment.

The growth rate of final consumption expenditures remained subdued, standing at 5.0 per cent during the second quarter of this year, only slightly higher than the 4.4 per cent during the previous quarter. Among its components, private consumption rose by just 4.8 per cent, reflecting both the employment instability against the backdrop of the economic slowdown, and the reduction in the propensity to consume(the reduced zest for consumption) brought about by serial large corporate insolvencies. Viewed by type, spending on durables, such as automobiles and mobile phones, shifted to an increase, and that on services accelerated its upward pace, while expenditure on non-durables, such as gasoline, moderated and consumption of semi-durables remained sluggish. Government consumption, meanwhile, grew by 6.1 per cent, a higher rate than that of the previous quarter, mainly due to the increased spending on materials and personnel affected by the enlargement of the functions of local government.

Fixed investment decreased by 0.1 per cent, due to the slackening of both equipment and construction investment. Equipment investment decreased by 1.5 per cent, following a similar downward pace in the previous quarter and attributable both to the decline in profitability brought about by the economic sluggishness and to the increased uncertainty caused by the insolvencies of several large corporations. Machinery investment recorded a low growth rate of 0.4 per cent, reflecting the reduced pace of investment in general industrial machinery, such as metal-working machinery and textile-working machinery, which offset the briskness of investment in wireless telecommunications equipment and electricity transmission and distribution apparatus. Transportation equipment investment also contracted by 7.0 per cent, due to the sharp decrease of investment in ships and railroad carriages. Meanwhile, construction investment registered only a 1.1 per cent increase. This listlessness was attributable to the steady decline in both residential and non-residential construction investment, as well as the slowdown of public works projects, such as roads, ports, and railroads.

Exports, in real terms, increased by 24.0 per cent, a much higher rate than the 15.5 per cent of the previous quarter. This boost was mainly provided by a sharp pick-up in exports of heavy industrial and chemical products, centering on chemical products, semi-conductors and automobiles. It was also helped by the favorable performance of service exports, especially transportation and communications.

[Table 1] Growth Rates by Component of Expenditure¹⁾

	1995	1996 ²⁾				1997 ²⁾		
		I	II	1st half	Year	I	II	1st half
G D P	8.9	7.8	6.9	7.3	7.1	5.5	6.3	5.9
G N P	8.7	7.5	6.9	7.2	6.9	5.1	5.6	5.4
Final Consumption Expenditure	7.2	7.5	7.2	7.4	6.9	4.4	5.0	4.7
(Private Consumption)	8.3	7.7	7.4	7.5	6.9	4.4	4.8	4.6
Gross Fixed Capital Formation	11.7	8.2	5.2	6.6	7.1	-1.2	-0.1	-0.6
Equipment	15.8	4.9	4.6	4.8	8.2	-1.6	-1.5	-1.5
Construction	8.7	11.2	5.6	8.0	6.3	-0.9	1.1	0.2
Exports of Goods and Services	24.0	20.3	10.0	14.8	14.1	15.5	24.0	19.9
Imports of Goods and Services	22.0	16.3	12.5	14.3	14.8	8.4	7.3	7.8

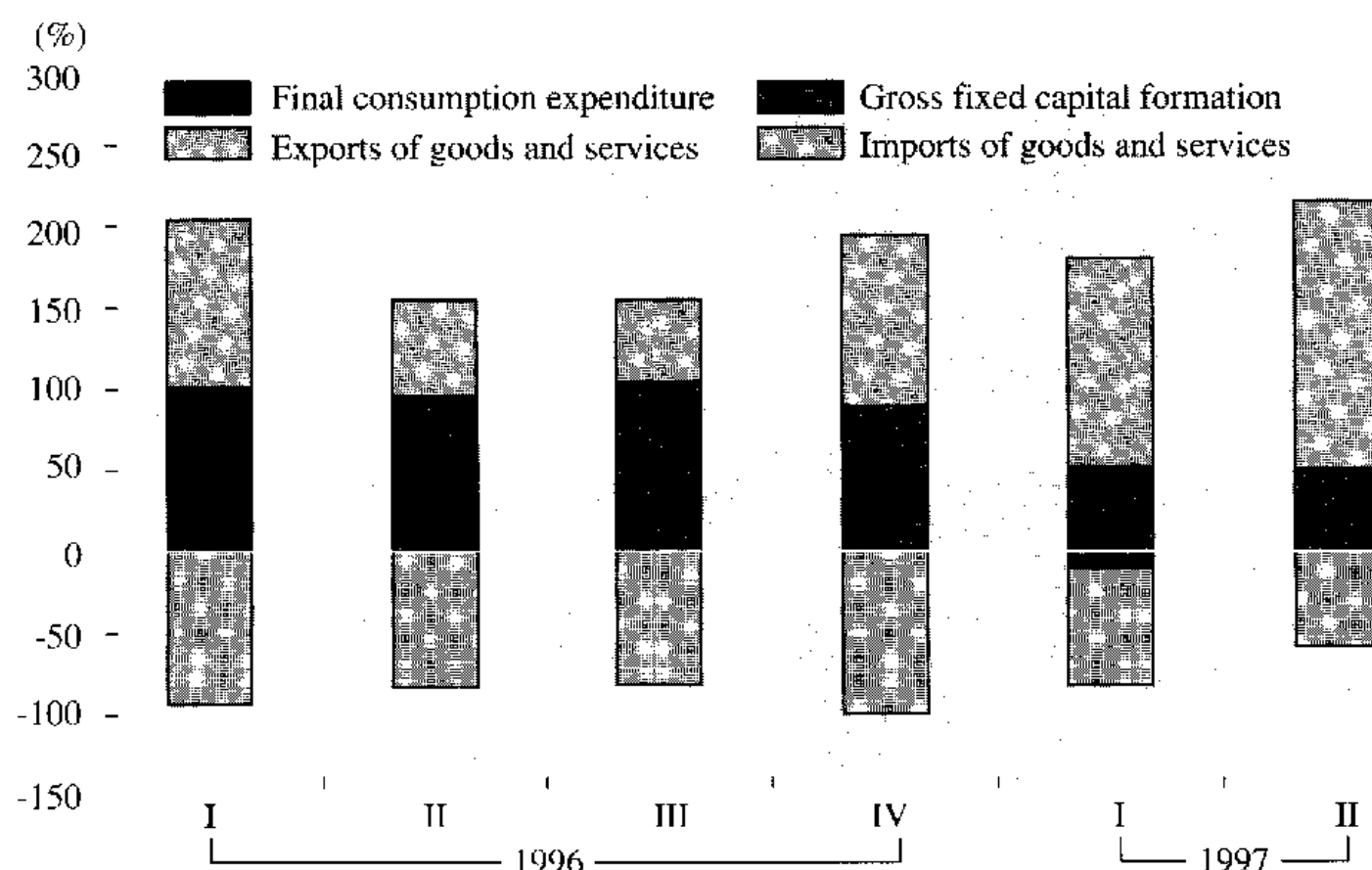
Notes : 1) Rates of change compared with the same period of the previous year.

2) p : preliminary.

Imports, in real terms, exhibited a growth rate of 7.3 per cent, slightly lower than the 8.4 per cent of the previous quarter. Both capital goods, notably machinery, ships and railway locomotives, and consumer goods, centering on automobiles and fur garments, maintained their subdued pace while imports of services, centering on transportation-related services, also slowed.

Looking at contribution ratios to GDP growth by components of expenditure, that of exports marked a sharp increase to 166.8 per cent from the 127.6 per cent of the previous quarter, underlining their leading role in economic growth during the quarter under review. Meanwhile, the contribution ratio of consumption continued its declining trend evident since the third quarter of the last year, falling to 50.0 per cent from the 53.2 per cent of the previous quarter. Fixed investment made a negative contribution of -0.3 per cent to economic growth, following its negative contribution of -8.3 per cent of the previous quarter.

[Chart 1] Contribution Ratios to Growth by Components of Expenditure



Viewing economic growth by sector of economic activity, both agriculture, forestry and fishing and the construction industry showed sluggish performance, while manufacturing, services, and electricity, gas and water exhibited high growth rates.

Manufacturing production grew by 7.6 per cent during the second quarter,

well above the 5.7 per cent of the previous quarter, owing to the briskness of exports. Within manufacturing, heavy industrial and chemical production recorded a growth rate of 11.2 per cent, higher than the 8.7 per cent of the previous quarter. This was attributable to the large increases in the production of electric and electronic products and of chemical products, boosted by the favorable pace of their exports, and to the recovery in the production of transportation equipment, supported by the heightened domestic and external demand for automobiles. In contrast, the production of light industries declined by 4.8 per cent, a drop similar to the 5.0 per cent decrease in the previous quarter. Viewed by item, rubber and plastic products exhibited positive growth, while the production of most other items including textiles, apparel, footwear, foods and beverages declined due to the contraction of both domestic and external demand.

The growth rate of the electricity, gas and water sector moved up to 8.8 per cent from the 4.8 per cent in the preceding quarter, aided by the increase in the generation of electricity for both home and industrial use, along with the continued expansion of the urban gas pipeline network.

Meanwhile, the construction industry continued its subdued pace, registering a growth rate of just 1.1 per cent, due to the slackening of both private and government construction. Viewed by sector, private construction failed to grow at more than 0.2 per cent, as activity in both residential construction for housing and non-residential construction for factories and commercial buildings continued to decline, while there was a slowdown in the pace of civil engineering construction associated with infrastructure projects. Government construction also grew by only 1.4 per cent, due to the sluggishness of road construction and urban civil engineering projects, whose effects outweighed the favorable pace of the construction of buildings, such as public offices.

The service sector recorded a growth rate of 8.0 per cent, higher than the 7.3 per cent of the previous quarter. Within this sector, the wholesale and retail trade displayed a growth rate of 5.6 per cent, a little higher than the 4.9 per cent of the previous quarter, due to the expansion of transactions involving both domestic industrial and export goods. Transportation, storage and communications, which had shown a high growth rate of 13.8 per cent in the previous quarter, continued its robust growth pace, rising by 15.3 per cent. It was driven by the continued expansion of communications, centering on mobile communications and information communication services, together with the favorable performance of the transportation and storage sector that reflected the increase in shipments of export goods. Finance, insurance, real estate and business services slowed their pace, posting a growth rate of 7.5 per

cent, slightly lower than the 7.9 per cent of the previous quarter. Their pace faltered in response to the sluggishness of business services, as corporations reduced their advertising budgets, despite the favorable performance of finance and insurance owing to the increase in insurance institutions' premiums and securities companies' commission income.

Meanwhile, agricultural, forestry and fishing production registered a growth rate of 0.2 per cent, much lower than the 4.7 per cent of the previous quarter. This poor performance was attributable to the decrease of agricultural production, induced by the reduction of the area under cultivation for major items of the quarter under review, such as barley and garlic, and to the sluggishness of livestock farming. It occurred in spite of a sharp increase in fisheries aided by the favorable marine aquaculture production and large catches from deep-sea fishing.

[Table 2] Growth Rates by Sector of Economic Activity¹⁾

	Unit : per cent							
	1995	1996 ²⁾				1997 ²⁾		
		I	II	1st half	Year	I	II	1st half
Agriculture, Forestry & Fishing	3.7	1.0	1.3	1.2	3.5	4.7	0.2	1.6
Mining & Manufacturing	10.6	7.6	6.2	6.9	7.3	5.7	7.5	6.6
(Manufacturing)	10.8	7.7	6.5	7.1	7.4	5.7	7.6	6.7
Electricity, Gas & Water	8.7	11.9	10.7	11.3	10.7	4.8	8.8	6.8
Construction	8.6	10.4	6.7	8.3	6.7	-1.0	1.1	0.2
Services	10.1	8.3	8.5	8.4	8.2	7.3	8.0	7.7
Government & Private Non-Profit Services	2.1	3.6	3.7	3.6	3.5	2.7	2.7	2.7

Notes : 1) Rates of change compared with the same period of the previous year.

2) p : preliminary.

Employment and Wages

For the second quarter, the increase in the total number of persons in employment, which had risen steeply in the first quarter of the year, showed a reduced pace that reflected the contraction of labor demand in response to the economic slowdown. However, the rate of increase in the economically active population also slowed, as the number of persons, and especially of women, leaving the workforce and no longer actively seeking employment in-

creased, as jobs became more difficult to secure. In consequence, the seasonally-adjusted unemployment rate, which had soared to 2.9 per cent in March, returned to a downward trend from April onwards, falling to 2.4 per cent in July.

Viewing the pattern of employment by sector during the period, the decline in manufacturing employment gathered further pace. Employment in manufacturing dropped by around 4 per cent, affected by corporations' continued downsizing. However, employment in the service sector maintained a high growth rate of around 5 per cent and that in construction also continued its favorable pace.

[Table 3]

Employment Trends¹⁾

	Unit : per cent								
	1995	1996				1997			
		I	II	Jan.~Jul.	Year	I	II	Jul.	Jan.~Jul.
Increase in the economically active population	471 (2.3)	345 (1.7)	357 (1.7)	348 (1.7)	391 (1.9)	687 (3.4)	523 (2.5)	394 (1.8)	575 (2.7)
Increase in total number of persons in employment	540 (2.7)	378 (1.9)	350 (1.7)	359 (1.8)	387 (2.9)	495 (2.5)	387 (1.8)	304 (1.4)	421 (2.0)
Manufacturing	78 (1.7)	-91 (-1.9)	-103 (-2.1)	-95 (-2.0)	-96 (-2.0)	-137 (-2.9)	-209 (-4.4)	-239 (-3.8)	-182 (-3.9)
Construction	119 (6.7)	56 (3.2)	66 (3.4)	64 (3.4)	72 (3.8)	42 (2.3)	73 (4.9)	65 (3.2)	59 (3.1)
Services	514 (4.8)	579 (5.3)	536 (4.8)	550 (5.0)	549 (4.9)	614 (5.4)	591 (5.1)	576 (4.9)	598 (5.2)
Unemployment rate ²⁾	2.0	1.9	2.0	2.0	2.0	2.6	2.6	2.4	2.6

Notes : 1) Figures in parentheses indicate rates of change compared with the same period of the previous year.

2) Seasonally adjusted rates in per cent.

During the second quarter, the growth rate of nominal wages across all industries fell to 9.7 per cent from the 11.6 per cent in the preceding quarter, due to the economic slowdown and the subsequent heightened uncertainty in the job market. By sector, the growth of nominal wages in transport, storage and communications rose slightly faster than in the previous quarter, while the growth of those in manufacturing, construction, and the wholesale and retail trade, restaurants and hotels sector all slowed.

[Table 4] Rates of Increase in Nominal Wages by Industry¹⁾

	Unit : per cent							
	1995	1996				1997		
		I	II	1st half	Year	I	II	1st half
All industries	11.2	13.7	10.3	12.0	11.9	11.6	9.7	10.7
(Manufacturing)	9.9	15.6	10.5	13.0	12.2	9.9	9.3	9.6
(Construction)	9.0	8.0	19.4	9.9	8.5	13.2	8.5	10.8
(Wholesale and retail trade, restaurants and hotels)	10.5	13.8	11.9	12.8	12.2	15.7	9.0	12.3
(Financial intermediation, real estate, renting and business activities)	12.1	16.1	17.5	16.8	17.8	11.3	12.3	11.8
(Transport, storage and communications)	14.6	7.8	3.3	5.6	7.4	10.0	9.3	9.7

Note : 1) Rates of change compared with the same period of the previous year.

External Transactions

Exports reversed their trend to post an increase of 7.3 per cent in the second quarter of 1997 and a strong expansion of 19.3 per cent in July, compared with the same period in the previous year. Their improved performance was largely attributable to an upturn in the international prices of major export products and to their low growth rate in the base period of the previous year. By commodity group, exports of heavy industrial and chemical products, which had been sluggish, shifted to an increase of 7.8 per cent during the second quarter, consolidating their renewed strength with a rise of 18.5 per cent in July. They were led by expanded exports of chemical products, automobiles, iron & steel products, and semiconductors. Exports of light industrial products, also, posted strong growth at the 25.5 per cent level in July, centering on those of textile yarns.

Seen by region, the trend of exports to industrial countries reversed its decline to show an increase during the second quarter and one of 20.6 per cent in July. It was headed by expanded exports to the United States and the EU. Exports to developing countries also recorded a high growth rate owing to the expansion in exports to China and Southeast Asian countries.

L/C arrivals during the second quarter increased slightly. In July, however, they registered a negative growth rate, falling 4.4 per cent compared with the same period of the previous year.

[Table 5] Rates¹⁾ of Increase of Exports²⁾ & L/C Arrivals

	Unit : per cent									
	1996					1997				
	I	II	Jul.	Jan. ~ Jul.	Year	I	II	Jul.	Jan. ~ Jul.	
Exports	20.3	3.5	-5.6	8.5	3.7	-5.6	7.3	19.3	3.4	
Light industrial products	10.3	9.7	3.8	9.0	7.5	2.3	3.7	25.5	6.4	
Textiles & clothing	-4.3	-3.3	3.8	-2.6	-2.1	3.3	3.7	7.5	4.2	
(Textiles)	-5.2	3.3	13.3	1.3	2.4	5.8	3.1	4.4	4.3	
(Textile yarns)	4.2	-2.8	-0.3	0.3	9.9	34.1	26.5	41.7	31.6	
Tires & tubes	24.3	16.6	8.4	18.4	16.5	-15.8	-7.4	6.9	-8.9	
Footwear	-27.3	-29.1	-19.7	-27.0	-27.6	-24.7	-27.4	-30.9	-26.7	
Others	43.1	37.5	6.0	34.4	28.1	5.7	6.9	63.6	13.7	
Heavy industrial & chemical products	24.5	0.1	-12.2	7.4	0.9	-11.9	7.8	18.5	0.4	
Chemical products	3.0	-14.0	2.3	-4.7	-1.6	4.8	31.3	28.3	18.8	
Iron & steel products	-17.7	-41.8	-28.5	-31.6	-26.8	15.3	14.5	25.5	16.3	
General machinery	24.4	11.8	-6.5	13.8	10.8	7.8	8.5	20.4	9.7	
Electric & electronic products	29.9	-5.9	-26.0	4.4	-6.8	-16.8	13.0	36.9	1.7	
(semiconductors)	56.9	-17.3	-42.5	5.0	-19.3	-41.0	7.7	36.6	-15.7	
Automobiles	24.1	22.8	-4.2	19.3	26.4	-10.1	31.2	30.7	14.0	
Ships	87.6	57.8	30.2	64.3	28.8	-45.7	-16.9	-0.2	-26.2	
Others	40.4	7.2	-5.5	17.5	-0.4	-27.5	-15.8	-14.4	-20.9	
To industrial countries	16.5	-9.5	-16.7	-0.8	-8.2	-14.7	8.6	20.6	-0.1	
To developing countries	23.9	16.3	6.1	17.7	15.6	2.6	6.3	18.2	6.4	
L/C arrivals	-1.2	-8.6	3.8	-3.8	-4.4	-7.0	0.8	-4.4	-3.3	

Notes : 1) Compared with the same period of the previous year.

2) On a customs-clearance basis at f.o.b. prices.

Imports themselves registered a modest increase of 0.6 per cent during the second quarter and reversed to a small decrease in July. This was largely in response to the listlessness of domestic demand and stable international prices of raw materials.

By commodity group, consumer goods imports showed a trend of decrease from the second quarter, reflecting the sluggishness of domestic consumption and the stable movements of international grain prices. Imports of capital goods, which had recorded an increase of 2.6 per cent during the second quarter caused by a surge in imports of aircraft, decreased 14.4 per cent in July, led downward by imports of general machinery. Meanwhile, imports of

raw materials increased only slightly in the second quarter, responding to stable international crude oil prices. In July, though, they climbed steeply rising by 12.5 per cent, because of increased imports of petroleum & its derivatives.

Seen by region, imports from industrial countries continued to decrease in absolute terms, led downward by those from Japan and the EU. Meanwhile, there was a slowdown in the growth of those from developing countries.

[Table 6]

Rates¹⁾ of Increase of Imports²⁾

Unit : per cent

	1996					1997			
	I	II	Jul.	Jan.~Jul.	Year	I	II	Jul.	Jan.~Jul.
Imports	16.8	6.7	12.6	11.6	11.3	3.9	0.6	-0.8	1.8
Consumer goods	25.1	19.1	16.0	20.9	21.2	5.3	-5.0	-3.3	-0.6
Raw materials	19.0	9.5	9.8	13.4	10.2	8.7	0.4	12.5	5.6
Crude petroleum	15.1	5.9	87.6	17.7	33.5	67.4	22.7	10.6	39.9
Others	19.8	10.2	0.2	12.6	5.8	-3.2	-4.0	12.9	-1.4
(Iron & Steel)	48.7	18.9	2.0	26.9	0.5	-26.1	-18.8	-8.2	-20.5
(petroleum & derivatives)	31.2	30.0	-11.4	26.4	16.9	-27.4	-23.8	39.4	-21.2
Capital goods	11.9	0.3	14.7	7.0	10.0	-3.2	2.6	-14.4	-2.6
General machinery	8.8	-2.2	17.6	5.1	7.2	-13.7	-8.5	-32.6	-14.7
Electric & electronic products	15.7	6.2	13.1	11.0	9.6	11.6	16.3	16.2	14.3
Aircraft	0.2	-50.1	-9.9	-22.3	12.0	-36.7	145.7	-28.4	13.0
Precision machinery	10.0	3.4	35.9	11.0	20.2	3.8	4.8	-23.1	-0.8
Others	22.0	12.5	7.3	15.2	15.9	-3.2	-37.9	-25.8	-22.5
From industrial countries	13.9	4.1	9.4	8.7	7.8	-5.3	-1.2	-6.6	-3.7
From developing countries	22.8	12.5	20.3	17.8	18.4	21.1	4.2	12.3	12.6

Notes : 1) Compared with the same period of the previous year.

2) On a customs-clearance basis at c.i.f. prices.

The current account accumulated a deficit of US\$ 11.1 billion during the first seven months, less than that of the same period in the previous year (US\$ 12.2 billion). This narrowing was mainly attributable to the continued decline in the size of the trade deficit caused by the increased exports combined with sustained deceleration of import growth. However, the scale of the improvement was reduced by a large deficit on invisibles that reflected increased outlays for transportation services and overseas travel.

[Table 7]

Balance of Payments: Current Account

Unit : billion U.S. dollars

	1996					1997			
	I	II	Jul.	Jan.~Jul.	Year	I	II	Jul.	Jan.~Jul.
Current account balance	-4.6	-5.3	-2.3	-12.2	-23.7	-7.4	-2.7	-1.0	-11.1
Trade balance	-2.5	-3.1	-1.8	-7.4	-15.3	-5.4	-0.6	-0.3	-6.3
Invisible trade balance	-1.9	-1.9	-0.5	-4.3	-7.6	-1.8	-2.0	-0.6	-4.4
Transfers(net)	-0.2	-0.3	-0.0	-0.5	-0.8	-0.2	-0.1	-0.0	-0.4

From early April onwards, the Korean won showed stable movements at around the 890 won per U.S. dollar level thank to the narrowing current account deficit and the increase of the capital inflows. Since July, however, it has depreciated against the U.S. dollar, affected by the Kia crisis and the rapid depreciation of several Southeast Asian currencies and softening of the Japanese yen. At the end of August, it was trading at 902 won per dollar, showing a loss of 6.4 per cent of its value at the end of the previous year.

[Table 8]

Exchange Rate Trends of the Korean Won
(End of period)

	1996		1997				
	Dec.	Mar.	Apr.	May	Jun.	Jul.	Aug.
U. S. dollar(W/\$)	844.20 (-8.2)	897.10 (-5.9)	892.10 (-5.4)	891.80 (-5.3)	888.10 (-4.9)	892.00 (-5.4)	902.00 (-6.4)
Japanese yen(W/100¥)	726.51 (3.1)	723.18 (0.5)	702.72 (3.4)	767.14 (-5.3)	775.29 (-6.3)	755.93 (-3.9)	746.69 (-2.7)
Deutsche mark(W/DM)	542.89 (-0.7)	534.53 (1.6)	517.01 (5.0)	522.90 (3.8)	510.26 (6.4)	486.17 (11.7)	498.62 (8.9)

Note : 1) Figures in parentheses indicate appreciation(depreciation,-) rates compared with the end of the previous year(%).

Against the Japanese yen the Korean won began to weaken rapidly from May, in response to the yen's strengthening in international financial markets. As the Japanese yen has softened again in international financial markets, the won has rebounded against it since July. As of the end of August, the won exhibited a 2.7 per cent depreciation over its value in yen terms at the end of the previous year.

Prices

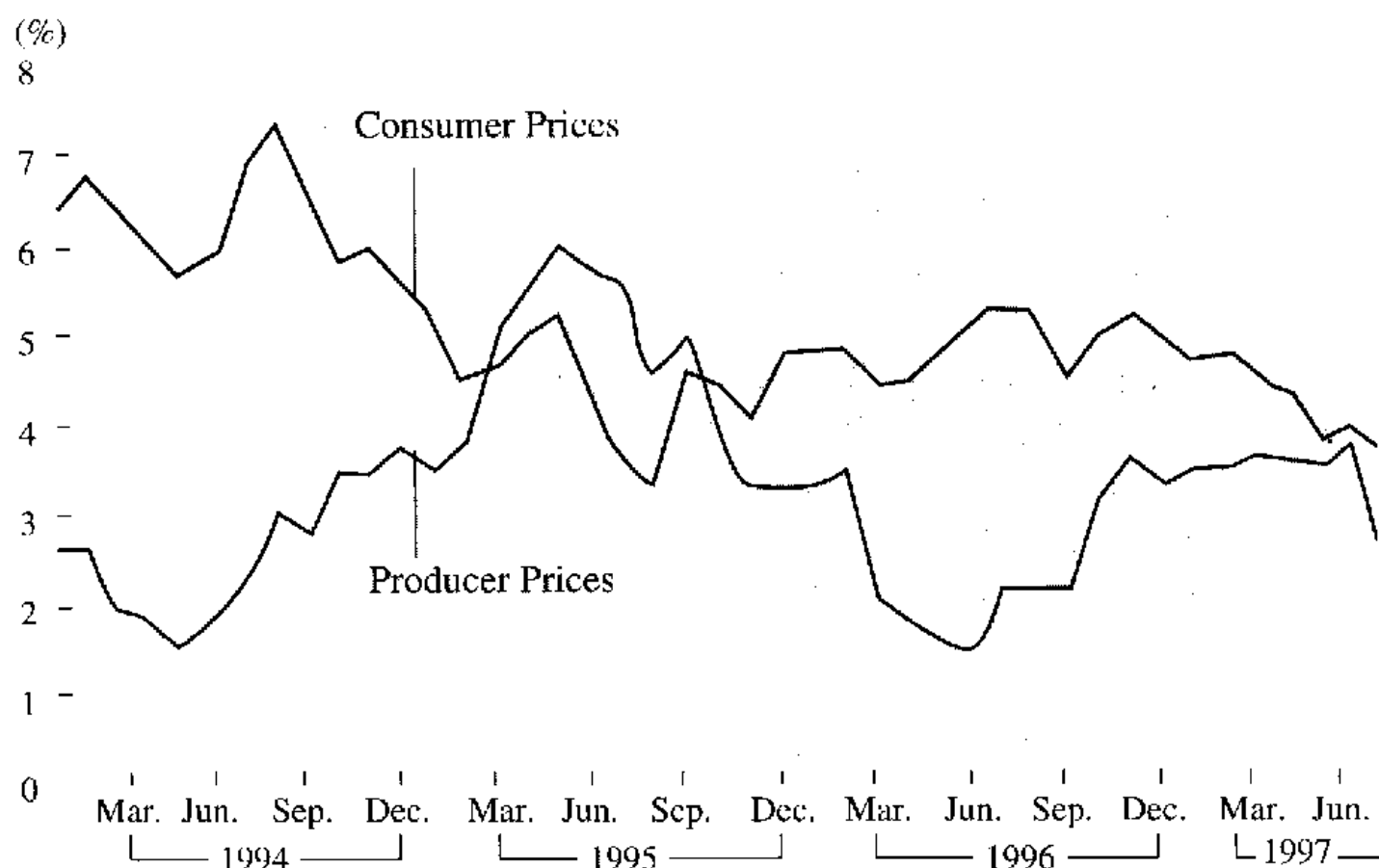
Prices, which had shown unstable movements during the first quarter, regained stability during the second quarter and July.

Producer prices rose by only 0.6 per cent during the second quarter over the last month of the preceding quarter, and dropped by 0.4 per cent in July over the preceding month. Viewing their movements by item, the prices of manufacturing goods remained stable, helped by the downturn in prices of petroleum products, paper products, and television and communication equipments, as a result of the stability of international raw material prices and increased price competition. Charges for electric power, water and gas supply also showed stable movements during the quarter under review, but in July they displayed an exceptional upturn, caused by higher electricity rates. Meanwhile the prices of agricultural, forestry and marine products gradually stabilized during the second quarter, with the clearing of the supply-demand imbalances for some items that had caused price instability earlier in the year. Notably during July, they dropped by 0.7 per cent, owing to the increased shipments of some fruit, such as water melon, and the seasonal contraction of the demand for wet fish.

Consumer prices maintained a stable range of movements from May onwards, holding to a 0.1~0.2 per cent increase per month. Thus during the January-July period, the rate of consumer price increases moderated to 2.6 per cent over those in December of the previous year, as against their 4.2 per cent rise in the same seven-month period a year earlier.

Viewing the movements of consumer prices by item, those of agricultural and marine products stayed within a stable range during the second quarter, but showed a rising trend around the beginning of July, affected by the poor crops of some vegetables. The prices of manufactured goods slowed down their rate of increase during the second quarter and dropped by 0.2 per cent in July, led by textile products and furniture, as demand-push pressures weakened amid dull domestic business conditions and international raw material prices remained stable. Charges for services also showed a slower upward pace from the second quarter onwards than in the same period of the previous year. This was thanks to the stability of house rents and charges for personal services, which largely offset the upward pressures caused by higher charges for public utilities such as electric power and gas supply, and bus, railroad and subway services.

[Chart 2]

Price Movements¹⁾

Note : 1) Rates of increase compared with the same period of the previous year.

Real estate prices, which had displayed steep upward trends at the beginning of the year, exhibited a greater degree of stability from the second quarter onwards. Housing prices continued to move within a stable range, in line with the seasonal cooling of demand and the hesitation by potential buyers amid widespread expectations of the continued stability of housing prices. Housing rents shifted to decreasing trend during the second quarter, falling by 0.5 per cent. In July they continued to decline, dropping by 0.2 per cent. Land prices marked only a 0.14 per cent rate of increase during the second quarter, reflecting the government's continued policy of stabilizing real-estate prices and enlarged supply of land from several large corporations following their insolvencies.

[Table 9]

Trends of Real Estate Prices¹⁾

	Unit : per cent								
	1995	1996				1997			
		I	II	Jan. ~ Jul.	Year	I	II	Jul.	Jan. ~ Jul.
Housing prices	-0.2	0.6	0.0	0.6	1.5	2.4	0.0	-0.1	2.3
(Apartments)	0.7	1.2	0.0	1.2	3.5	4.4	0.0	0.1	4.5
Land prices	0.55	0.22	0.24	0.45	0.95	0.15	0.14	—	0.29
Housing rents	3.6	3.2	0.7	3.9	6.5	2.5	-0.5	-0.2	1.9

Note : 1) Rates of change during the period.

Money and Banking Movements

Money

During the second quarter of 1997, the annual growth rate of MCT(M_2 + CDs + Money-in-trust) declined to 15.3 per cent from its 18.2 per cent of the previous quarter, and it slowed further to 15.1 per cent in July. This was mainly due to the contraction of firms' demand for funds caused by a protracted economic downturn. The growth rate of M_2 , which had continued to accelerate since the realignment of the trust account system, also eased to 19.3 per cent from the 19.5 per cent of the previous quarter and slowed further to 17.9 per cent in July as the effects of the realignment had somewhat subsided.

[Table 10]

Rates of Increase¹⁾ of Monetary Aggregates
(Average of daily figures)

Unit : per cent

	1996					1997					
	I	II	III	IV	Year	I	II	Apr.	May	Jun.	Jul. ²⁾
MCT	22.3	22.7	21.9	20.0	21.7	18.2	15.3	16.0	15.2	14.8	15.1
M_2	14.0	15.2	17.3	18.3	16.2	19.5	19.3	20.9	19.0	18.1	17.9
Reserve money	11.9	3.1	-0.6	-5.5	2.1	-16.3	-17.1	-21.6	-14.5	-15.0	-16.6
Currency-in-circulation	9.4	9.4	6.2	8.1	8.3	6.1	4.9	3.8	5.7	5.3	4.8
M_1	11.3	9.9	9.1	7.1	9.3	5.6	3.1	3.2	3.7	2.5	2.1
M_2 + CD	13.5	14.9	16.1	17.1	15.5	17.7	15.9	16.6	15.8	15.2	15.1
M_3	18.6	19.9	19.7	17.9	19.0	17.3	15.8	16.2	15.8	15.5	..

Notes : 1) Compared with the corresponding period of the previous year.

2) P : Preliminary.

Surveying the increase of MCT by sector during the second quarter based on changes in period-end figures, the private sector supplied only 13,444 billion won. This was because corporate demand for loans decreased due to the economic slowdown. Moreover, in response to the widespread nervousness of the markets caused by the insolvencies of several large corporations, financial institutions became more cautious in their lending to companies and showed little appetite for purchases of securities such as corporate bonds. The government sector absorbed 1,207 billion won, a substantial reduction from the

previous quarter, on account of the decrease in tax receipts associated with the economic downturn. The foreign sector, which had been a net absorption sector since the second half of the previous year, supplied 3,870 billion won. This was attributable to the narrowing of the current account deficit and to inflows of foreign funds for stock investment. The size of absorption by the other sector was 4,273 billion won, less than in the previous quarter as sales of cover bills declined.

In July, claims on the private sector expanded mainly through increases in general loans. The scale of the government sector's absorption decreased greatly compare with the same month of the previous year, led largely by the effects of the lending-out of surplus Treasury funds to the banks. The supply of liquidity through the foreign sector decreased due to the reduced scale of capital inflows amid the protracted sluggishness of the domestic stock market; meanwhile the scale of liquidity absorption through the other sector widened.

[Table 11]

Money Supply by Sector
(End-of-period figures)

Unit : billion won

	1996					1997				
	I	II	Jul.	Jan.~Jul.	Year	I	II	Jul. ^{P)}	Jan.~Jul. ^{P)}	
Claims on government sector	-5,097	-1,717	-4,806	-11,620	-2,600	-6,178	-1,207	-1,747	-9,131	
Claims on private sector	13,950	20,022	10,815	44,787	71,044	20,295	13,444	7,216	40,955	
(Loans)	(4,602)	(11,920)	(7,539)	(24,061)	(34,447)	(10,693)	(7,922)	(4,543)	(23,158)	
(Securities)	(8,037)	(5,944)	(1,800)	(15,781)	(24,648)	(9,134)	(2,736)	(2,005)	(13,876)	
Foreign sector	424	1,956	-2,631	-251	-2,279	-3,610	3,870	391	651	
Other sector	-2,963	-4,087	-2,182	-9,232	-15,988	-5,676	-4,273	-3,039	-12,988	
MCT	6,315	16,174	1,196	23,685	50,178	4,832	11,834	2,821	19,487	

Note : 1) P : Preliminary.

In its conduct of monetary policy during the second quarter of 1997, the Bank of Korea placed priority on siphoning off the liquidity that had been supplied in order to reduce financial market instability. To this end, it offered a larger volume of sales of government and public bonds under resale agreements, termed reverse RPs, than of purchases of them under repurchase agreements.

Through its partial implementation of the fourth stage of interest rate deregulation, the Bank also made efforts to improve the monetary policy instruments available to it in preparation for the shift to a fully market-based and indirect system of monetary management. As of July 4, it eased regulations on banks' loan management by lowering the guideline ratio for local banks' credit to small and medium enterprises and abolishing the restriction on the extension of credit for business related to condominiums. With effect from July 7, it liberalized interest rates on savings deposits and on both preferential savings deposits and company savings deposits with a maturity of less than three months. The Bank also eased the conditions on the issue of market-based financial products such as CDs, RPs and cover bills and abolished the restriction on maximum interest rates payable after maturity on deposits with fixed maturities. It also allowed commercial banks to issue financial debentures with a maturity of at least three years.

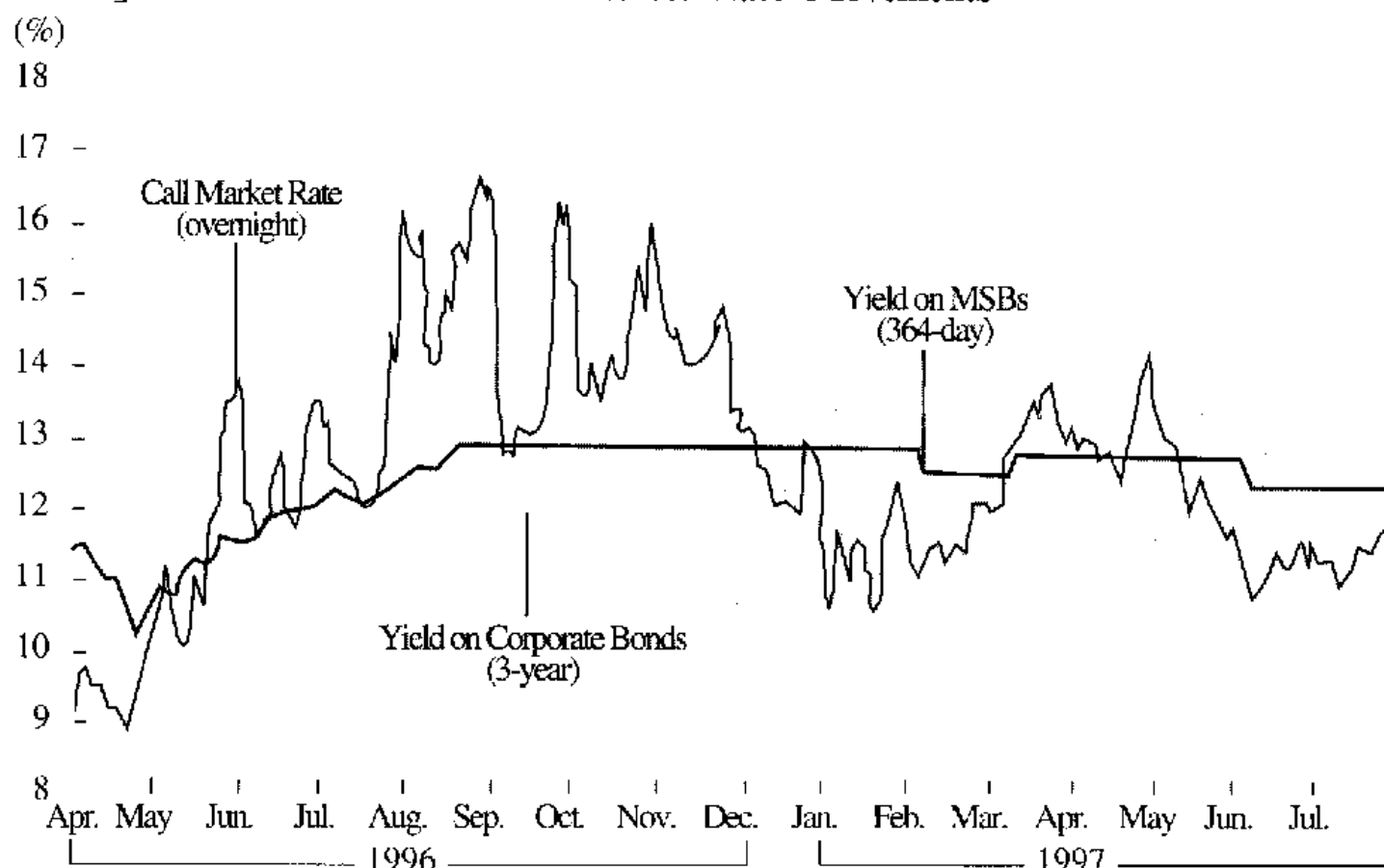
Financial Markets

During the second quarter, market interest rates showed a downward trend as financial markets gradually recovered from their uneasiness. Call rates fell to around a level of 10 per cent in early June and yields on corporate bonds continued to soften throughout the period. In July, though, call rates exhibited an upward trend toward the end of month affected both by renewed market fears provoked by the application of the bankruptcy-prevention accord to Kia group and by the increased demand for funds to meet value-added tax payments. The yield on corporate bonds, although it did show a temporary rise with the loss of the market's appetite for corporate bonds given their heightened credit risk, remained around the level of 12 per cent for the month as a whole.

Turning to deposits at financial institutions during the second quarter, deposits taken by merchant banking corporations shifted to a net decrease. Deposits at deposit money banks and investment trust companies exhibited a similar increase to that in the previous quarter and deposit-taking by banks' trust accounts expanded.

[Chart 3]

Market Interest Rate Movements



Among the products offered by deposit money banks, the growth of short-term savings deposits which may be used for settlement decreased, being influenced to some extent by tax-payments. Time deposits, however, expanded markedly led by market interest rate linked products following the abolition in February 1997 of the minimum maturity, previously one year, of deposits on which flexible interest rates may be applied. Meanwhile, the upward trend in sales of cover bills, which had expanded considerably in the previous quarter reflecting the elimination of ceilings on their issuance by individual banks, shifted to a decrease due to the shortage of the original bills which underlie this product. Sales of CDs, however, changed to a slight increase. In the case of merchant banking corporations, while their sales of own paper showed a favorable pace, those of commercial paper decreased sharply as banks' trust accounts mainly purchased only highgrade commercial paper, being influenced by the continuing wave of corporate insolvencies. As for investment trust companies, stock funds shifted to a decrease and short-term bond funds exhibited a slower increase. But their long-term bond funds experienced stronger growth, reflecting their enhanced competitiveness following the fall of market interest rates. Among banks' trust accounts, products such as non-specific money-in-trust and development trusts continued to show weak performance as a consequence of the realignment of the trust account system, whereas specific money-in-trust products expanded markedly thanks to high returns.

In July, deposits at deposit money banks showed much slower growth. This was because, although time deposits experienced a favorable increase, demand deposits shifted to a decrease and sales of CDs and cover bills were sluggish. Deposits taken by merchant banking corporations continued to shrink. On the other hand, deposit taking by investment trust companies showed a sizable increase and banks' trust accounts exhibited a similar increase to that in the second quarter.

[Table 12] **Growth of Deposits at Financial Institutions**
(End-of-period figures)

Unit : billion won

	1996					1997			
	I	II	Jul.	Jan.~Jul.	Year	I	II	Jul. ²⁾	Jan.~Jul. ²⁾
Deposit money banks	727	9,651	559	10,937	28,137	7,156	7,642	1,225	16,022
Demand deposits	-3,031	985	-970	-3,016	643	-2,596	1,296	-1,868	-3,168
Time and savings deposits	2,074	7,768	1,215	11,058	22,946	5,616	6,851	3,221	15,689
Short-term savings deposits	1,150	2,087	-971	2,266	5,370	454	-1,569	878	-237
Time deposits	86	3,113	1,198	4,397	4,629	1,038	4,225	1,721	6,984
Installment-type deposits	838	2,569	989	4,396	12,948	4,124	4,196	622	8,942
CDs	1,574	626	-277	1,924	1,901	-1,924	1,026	-40	-938
Cover bills	109	272	590	971	2,648	6,059	-1,531	-90	4,439
Merchant banking corporations	8,585	3,721	1,131	13,436	23,723	7,825	-1,404	-81	6,340
Sales of own paper	354	230	1,916	2,500	5,602	837	3,076	-51	3,862
CMAAs	1,223	-534	-840	-151	139	684	960	-426	1,218
Sales of commercial paper	7,008	4,025	54	11,087	17,982	6,305	-5,440	396	1,260
Investment trust companies	4,905	2,808	617	8,330	8,337	3,793	3,720	5,311	12,824
Short-term bond funds (MMFs)	1,396	-303	250	1,342	4,538	2,158	1,687	2,219	6,064
	(-)	(-)	(-)	(-)	(5,666)	(3,120)	(1,049)	(1,637)	(5,807)
Long-term bond funds	3,978	3,984	239	8,200	3,568	1,107	2,637	2,493	6,236
Stock funds	-604	-773	152	-1,226	256	447	-225	658	879
Trust-type securities savings	53	-76	-30	-53	-1	209	-354	-15	-160
BMFs	83	-23	7	66	-24	-127	-24	-45	-196
Money-in-trust	8,508	8,044	1,275	17,827	26,203	3,940	5,860	1,726	11,523
Company money-in-trust	990	-8	-404	578	-728	-539	-106	-341	-986
Household money-in-trust	6,202	4,022	689	10,912	12,002	-580	-905	-51	-1,536
Specific money-in-trust	655	126	175	956	5,631	3,059	5,299	1,104	9,462
Individual pension-trust	-498	-119	-125	-741	-1,346	-679	-566	-280	-1,525
Other trusts ¹⁾	1,158	4,023	941	6,123	10,643	2,679	2,137	1,294	6,108

Notes : 1) Including installment money-in-trust, non-specific money-in-trust and development trusts.

2) P : Preliminary

The stock market staged a recovery during the quarter under review, helped by greater stability of interest and exchange rates, the raising of the overall ceiling on foreign portfolio investment and expectations of economic recovery following the strengthening of the Japanese yen. As a result, there was a brisk fund-raising by way of rights issues. In the bond market, the issuance of MSBs was increased considerably in order to soak up the additional liquidity which had been supplied in order to help stem the wave of corporate insolvencies. Issuance of corporate bonds, however, continued to decline, mainly because of the contraction of firms' demand for funds and the cancellation of some issues as banks and securities companies were reluctant to guarantee them following the increased number of company failures.

In July, the stock market made a brisk start to the month amid expectations of economic recovery and enlarged foreign portfolio investment. But around the middle of the month, sentiment again turned bearish in response to Kia group's being placed under the bankruptcy-prevention accord. Issuance of corporate bonds, meanwhile remained at about the same level as in the second quarter.

[Table 13]

Securities Markets

Unit : billion won

	1996					1997			
	I	II	Jul.	Jan.~Jul.	Year	I	II	Jul. ^{p)}	Jan.~Jul. ^{q)}
<Stock Market>									
Value of stocks traded (Daily average)	381	680	406	512	487	515	684	586	598
Korea Composite Stocks Price Index ¹⁾									
(End of period)	874.2	817.4	821.8	821.8	651.2	677.3	745.4	726.1	726.1
(Daily average)	865.9	910.6	832.2	879.8	833.4	673.8	723.8	752.3	707.1
Stock issued	970	983	515	2,468	5,043	383	742	654	1,779
Public issues	264	159	0	423	1,392	98	77	83	257
Rights issues	706	824	515	2,045	3,652	285	665	571	1,521
<Bond Market>									
Value of bonds traded (Daily average)	873	814	459	785	701	726	881	846	810
Government & public bonds	322	289	198	289	258	334	417	407	380
Corporate bonds	551	524	261	496	443	392	465	439	430
Net bond issuance	7,911	9,123	951	17,985	25,359	1,448	11,135	2,182	14,764
Government & public bonds	3,082	5,612	318	9,012	9,071	-1,328	8,256	1,256	8,184
(Monetary control bonds)	(-240)	(3,219)	(260)	(3,239)	(-795)	(-3,410)	(4,591)	(168)	(1,349)
Corporate bonds	4,829	3,511	633	8,973	16,288	2,775	2,879	926	6,580

Notes : 1) 1980. 1. 4=100.

2) P : Preliminary.