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The Chairman's Summing Up at the Conclusion
of the 1982 Article IV Consultation with Korea
Executive Board Meeting 82/66 - May 5, 1982

Executive Directors expressed broad support for the thrust of views expressed in the appraisal for the 1982 Article IV consultation with Korea. They noted with satisfaction that all performance criteria under the recent stand-by arrangement had been observed and that the major macroeconomic objectives of the program had been achieved.

Directors observed that the resumption of economic growth in 1981 had been due in part to a moderate fiscal stimulus and rapid export growth in the first three quarters of 1981. But it was noted that with depressed profits, excess capacity, and high inventory levels continuing, the business climate had shown little improvement and real investment had declined for the second consecutive year. Directors were encouraged by the remarkable progress achieved in reducing inflation but felt that the present level of inflation was still high compared to that of the main trade partners of Korea. With regard to the balance of payments, Directors commended the authorities on the improvement in the external position and the further liberalization of imports. Based on the strength of export growth in the first three quarters of 1981, the current account deficit had declined, in spite of relatively high imports and the adverse impact of higher international interest rates on the services account. With higher interest rates and the rapid accumulation of external debt since 1979, the debt service ratio and the ratio of debt to GNP had reached historically high levels in 1981.

Directors emphasized that the balance of payments deficit on current account was still high by Korea's past standards and that further external adjustment was needed in order to alleviate the growing debt service burden and to reduce Korea's vulnerability to external shocks. Therefore, Directors were encouraged that the Korean authorities were aiming at a further reduction of the current account deficit. Directors also supported the authorities' objectives of achieving a further reduction in inflation and resuming sustained economic growth. To meet the twofold need of securing a resumption of sustained growth and further external adjustment in 1982 and beyond, continued strong export growth was required.

Directors centered many of their comments on exchange rate policy, considering that it presented difficult issues of analysis, policy, and timing. Directors were aware of the price effects of a depreciation of the currency and of the international context in which trade movements are taking place and noted the reliance of the authorities on wage moderation and productivity improvements to restore export competitiveness; they agreed that these factors were indeed essential ingredients to further progress in external adjustment. But doubts were also expressed whether these factors alone would be sufficient to provide the required boost to exports given the recent developments in export orders. While most Directors felt that a flexible exchange rate policy would be helpful in providing adequate export incentives and ensuring that Korea would benefit from the expected upswing in external demand, they also noted that the timing question was an important one. The preponderant view was that a restoration of competitiveness could in any case require a more restrictive monetary policy than the one presently in place. This would also help to dampen the price effects of a possible further move in the exchange rate.

With regard to the authorities' target for monetary growth for 1982, Directors commented that it was probably on the high side for the time being and that, hence, a tightening would be needed to achieve the inflation target, especially if growth were to be lower than projected because of a shortfall in exports. In this context, Directors expressed support of the more restrictive fiscal stance envisaged for 1982 and advised against a relaxation in the course of the year, while stressing the need for close monitoring of the situation. Several Directors noted that real interest rates were positive but stressed the importance of maintaining positive real interst rates to ensure the availability of sufficient domestic financial resources given, inter alia, the envisaged reduction in the use of foreign savings in the next few years. Executive Directors commended the authorities on the recent tax reform and their pursuit of a number of structural adjustment measures. They also stressed the importance of proceeding with the structural reforms and in particular the financial reform. Directors welcomed the authorities' intention to review policies in the course of the year in light of developments in the economy, in particular the performance of exports. The authorities were also commended for their efforts to improve the performance of public enterprises, including, in some cases, by divestiture.