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The Chairman's Summing Up at the Conclusion
of the 1992 Article IV Consultation with Korea
Executive Board Meeting 93/18, February 8, 1993

Executive Directors expressed their admiration for Korea's outstanding economic record over the past three decades. They observed, however, that macroeconomic policies in recent years had contributed to a pattern of overheating and abrupt slowdown and suggested that policies be firmly geared to achieving sustainable growth with low inflation. Directors also pointed out that, in order to complete the transition to a fully industrialized economy, structural reforms were needed to dismantle the prevailing system of detailed government control and intervention at the microeconomic level, notably in the financial sector.

Directors observed that economic activity in Korea slowed markedly in 1992. While welcoming the decline in inflation, they noted that the downturn in the second half of the year had been steeper than anticipated. Given the short-term outlook for gradual recovery of investment and growth in 1993, Directors were of the view that a broadly neutral stance of macroeconomic policy would be appropriate. Most speakers agreed that the budget for 1993 appeared consistent with such a broadly neutral stance.

Directors observed that monetary conditions had eased significantly during 1992. They noted the difficulties encountered in targeting monetary aggregates in a rapidly changing financial environment and suggested a flexible approach to monetary targeting, in light of the ongoing structural changes in the financial sector.

Directors agreed that financial sector reform was currently the main challenge in the area of structural policies and supported drawing up a comprehensive plan for financial liberalization and capital account opening. Directors emphasized that this plan should contain a detailed timetable covering measures in all relevant areas, including interest rate deregulation, the phasing out of policy loans, the development of money and bond markets, and the liberalization of capital transactions. The capital base of financial institutions should be strengthened, and more competition--domestic and foreign--should be injected into the system. Directors also stressed that successful financial sector liberalization required a strong system of bank supervision and the development of indirect instruments of monetary control. Directors understood that the weaknesses in Korea's financial system required a carefully considered pace of reform, although many speakers felt that preliminary reform plans envisaged an unduly slow process and suggested a more compressed timetable.

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Directors noted that considerable progress had been made over the past decade in the area of trade liberalization, but they stressed the need for further action, particularly with respect to agricultural trade. Korea's commitment to abide by the results of the Uruguay Round, even if this implied a faster pace of liberalization than was currently envisaged, was welcomed. The new foreign exchange management act was also welcomed, but the authorities were encouraged to move forward more rapidly with the further liberalization of exchange regulations.

Directors observed that Korea's medium-term prospects remained favorable; they noted, however, that the outlook was subject to the uncertainties related to future developments in relations with the Democratic People's Republic of Korea. Directors agreed that, although the gradual opening of the capital account may imply modest current account deficits over the medium term, these should not be a cause for concern, as external debt was small in relation to exports and GNP.

It is expected that the next Article IV consultation with Korea will be held on the standard 12-month cycle.