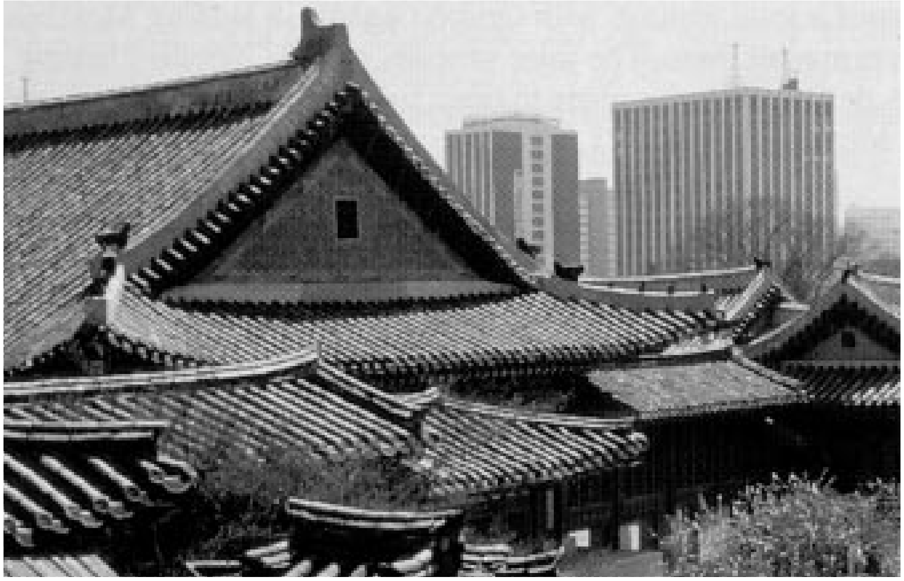

Korea National Tourism Organization

Korea's Agricultural Imports Reflect Emergence from Financial Crisis

In 1997, South Korea was the fourth-largest destination for U.S. agricultural products, buying 5 percent of U.S. agricultural exports. Beginning in late 1997 and extending into 1998, Korea experienced a major economic shock—including devaluation of its currency, a decline in the production of goods and services, and temporary difficulty in obtaining credit. What was the significance of the economic shock to Korea's agricultural trade, and what does the future hold?

Korea's financial crisis hit hard in November 1997, when the value of the won, and confidence in Korea's financial situation, went into free fall. By January 1998, the won lost more than 50 percent of its year-earlier value in U.S. dollar terms. Korean banks seemed close to insolvency, and credit from both Korean and foreign sources became extremely difficult to obtain. Interest rates more than doubled in January, to more than 25 percent. Without affordable access to credit, the economy began to stagger.

Strong intervention by the government and the International Monetary Fund, including measures to restore credit, gradually rebuilt confidence in the economy. Value of the won increased after January 1998, and currently lies 30 percent below its pre-crisis level. While gross domestic product (inflation-adjusted) declined 5.8 percent in 1998, it is expected to grow by more than 4 percent in 1999.

Despite containment of the crisis, total imports fell 35 percent in calendar-year 1998. The dollar value of Korea's agricultural imports fell by 28 percent, or $2.6 billion. The volume of most major agricultural imports also fell, but not by as much. U.S. agricultural exports to Korea dropped 22 percent (by about $640 million).

Several factors explain much of the decline in agricultural trade. The Korean economy, and most of its consumers, became poorer in 1998 because of rising unemployment, reduced asset value, and lower salaries. What money they had was worth less at the border, effectively raising the price of imported goods relative to domestic products. With most importers short on cash, inability to get credit severely limited transactions early in 1998.

The economic setback in Korea explains only part of the decline in the value of trade in 1998. Also contributing were weak global commodity prices, due mostly to bumper crops around the world, a supply-side result that had little to do with the financial crises. But in most cases, the loss in buying power of the won outweighed the dollar decreases in world commodity prices, and import unit values in won were higher in 1998 than in 1997.

The year-to-year drop in agricultural imports understates the full impact of the financial crisis because it fails to capture potential trade gains lost when Korea's economy plunged into recession. Korea was a rapidly expanding economy, and demand for imported agricultural products grew in most years. Before the crisis, for example, USDA projected that Korea's beef imports would rise 30,000 tons in 1998; instead, they dropped 92,000 tons. Pork imports were expected to double in 1998, the first year of liberalized trade in frozen pork. But imports fell 11,000 tons. Likewise, trade in processed and high-value agricultural products in general had been expected to increase rather than fall.

Examination of several of Korea's major commodity markets illustrates the ways in which economic weakness, global price changes, and other forces have affected Korea's agricultural imports in 1998 and 1999.

Imported Beef Demand Dropped Sharply

The financial crisis intensified what was already a cyclical downturn in Korean ***cattle*** prices that began in June 1997, with cattle farmers facing higher imported feed prices and high interest rates after November. Following devaluation, beef imports became more expensive and were arriving in a market where the domestic cattle price was in a downward spiral. With the price advantage of imported beef diminished and turmoil in the credit market making it difficult for private-sector importers to arrange for imports, beef trade dried up in early 1998.

Imports by the government trading entity continued, but Korea's WTO-mandated quota of beef imports was not filled in 1998, and import volume dropped by about 45 percent from 1997 levels. U.S. beef exports to Korea dropped 41 percent. Imports have been rebounding strongly in 1999, but are not equal to the pace of pre-crisis imports in the January-May period.

South Korea's Economy: Reviewing the Rebound

Korea's battered economy has bottomed out. After a drop of almost 6 percent in output in 1998, the Korean economy is expected to grow more than 4 percent in 1999 and in 2000. Several factors are responsible for recovery, including improved credit availability, easing of monetary policies, and renewed investor confidence. The value of the Korean won also has risen more than 40 percent since the early stages of the financial crisis in January 1998, as foreign capital has started to flow back into the country. The government budget deficit is expected to increase to 5.5 percent of Gross Domestic Product, with government spending further stimulating the economy. With a stronger economy and increased investor confidence, Korean foreign reserves now stand at $61 billion, compared with $18 billion at the end of 1997 when the crisis hit.

Financial and corporate restructuring is proceeding, although restructuring of the five largest chaebols (large conglomerates) is slow. Another concern is high unemployment, about 6.4 percent this year. Whether this recovery will be sustained depends on progress in these as well as other areas of the economy.

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Growth should increase through the rest of 1999, since credit issues are resolved, demand is rising, and Korean production is now falling after the intense slaughter of 1997/98.

The economic crisis may have strengthened Korea's ***pork*** sector. Before the crisis, Korea's industry was preparing for a possible doubling of imports after frozen pork trade was liberalized in July 1997. However, devaluation dramatically changed the industry's prospects as pork imports became more expensive and pork exports more competitive.

Korea had enjoyed some success in filling the gap left in Japan's supply when Taiwan ceased pork exports after a foot-and-mouth disease outbreak in early 1997. The won's devaluation in late 1997 and 1998 meant that Korea's pork was cheaper in Japan relative to domestic Japanese product and U.S. product. While Korean feed costs were higher because of devaluation, the cost of labor and processing (in terms of foreign currencies) declined, and the volume of Korean exports grew by 65 percent.

Unlike the cattle industry, there was no sharp cyclical downturn for swine, nor did pork imports confront sharply declining domestic prices. Imports of frozen pork were virtually unchanged in quantity, although they dropped in dollar value. In the first 5 months of 1999, pork imports soared to record levels, finally reflecting the liberalization of trade in frozen pork that took place in mid-1997. Korea will import and export different cuts of pork, based on the disparity of preferences between Korea and its trading partners.

Total consumption of the three main meats declined by 2 percent in 1998. Poultry meat, consumed heavily in restaurants, declined by 12 percent. Beef, the most expensive meat, dropped 10 percent (despite sharply lower prices), while pork consumption grew by over 8 percent. Although pork prices fell less than beef prices, pork was still the cheaper meat. In 1999, a recovery in consumer confidence is expected to send people back to restaurants, benefiting meat consumption, especially poultry and beef.

Grain used for feed in the October 1997-September 1998 marketing year is estimated down only 5 percent. Korea's imports of grains for feed in January-December 1998 actually rose slightly over 1997 levels. This level of use and trade, given the financial difficulties that traders faced, might not have been possible without the allocation of guarantees by the U.S. government early in the crisis. U.S. credit guarantees for 3.2 million tons of corn enabled Korean importers to overcome a lack of affordable credit, especially in the first half of 1998. Chinese corn exports to Korea declined in 1998 because credit could not be arranged.

Because Korea's animal producers are almost totally dependent on imported feedgrains, they would have to reduce herd sizes if grain import flows are interrupted. Feed use for Korea's swine industry was stable, partially offsetting declining feed use for beef cattle. Prospects for 1999 and later years are mixed. Recovering poultry meat consumption will be partly satisfied by domestic production and therefore imported feeds, but much of Korea's consumption growth will be satisfied by imported meats and dairy products rather than domestic production. Feed wheat from Eastern Europe continues to displace some corn in early 1999.

Crisis Altered Structure Of Oilseed Industry

The crisis has made it more likely that Korea will import ***vegetable oils and meals*** in the future, rather than oilseeds. Two out of the three Korean soybean crushing companies went into bankruptcy protection in early 1998. The crushing companies terminated credit sales, and Korea's feedmills, unable to import meal freely because of a general lack of credit, were left with reduced prospects for domestic and imported supplies. When U.S. government credits enabled them to buy U.S. meal, imports from the U.S. soared to over 300,000 tons, compared with almost no trade in 1996 and 1997.

Now it will be more difficult for Korean soybean crushers to convince feedmillers to buy domestic meal at prices higher than import prices, since domestic supplies failed at a critical moment. Increasingly, Korea is turning to meal imports, which exceeded domestic production in 1996 and 1998. Korea's imports of soymeal increased by over 25 percent in 1998. Similarly, soy oil imports are replacing domestic production. Korea's soy oil imports rose 8 percent in 1998 despite the difficult economic climate and higher world prices (in dollar and won terms). Imports of soybeans for crushing declined by 12 percent. So far in 1999, imports of soy oil and soymeal are up dramatically from the high levels of 1998, and soybean imports have dropped by another 17 percent. The profitability of crushing is likely to decrease in the coming years, given agreed-on annual reductions of soy oil tariffs between now and 2004.

Wheat for milling, raw ***sugar*** for refining, ***corn*** for sweetener production, and ***soybeans*** for food use together represented 13 percent of Korea's total agricultural import value in 1997. When the economic crisis hit, GSM guarantees restored Korea's access to U.S. wheat, corn, and soybeans. Australia and Canada also provided credit assistance. The import volume of these commodities changed very little in 1998, although world price declines reduced the dollar value of imports. In early 1999, volumes lagged behind those in the same period in 1998, but should end the year at levels similar to recent years.

Inputs for nonfood manufacturing accounted for about a quarter of the value of all agricultural imports in 1997: hides for tanning; cotton, wool, and silk to be spun into yarn; natural rubber; and raw furs. In 1998, the import volume of all these input commodities declined due to credit problems both for Korean importers and for domestic and export buyers of Korean products made from these raw materials. Manufacturers reportedly drew down stocks as much as possible to avoid new purchases.

Korea is one of the world's largest importers of hides, and the largest market for U.S. hide exporters. Despite GSM credit assistance, U.S. export volume of whole cattle hides to Korea dropped 35 percent in 1998, a contributing factor in the very low prices for hides at U.S.

Settling a Beef Between the U.S. & Korea

In April 1999, the U.S. government requested a dispute settlement panel from the World Trade Organization, stating that Korea had failed to implement parts of earlier agreements. The request cited several areas of concern, including restrictions on retail sales of imported beef, markups applied to imported beef prices by the government, restrictions on which private-sector groups could import, delays in soliciting bids to buy under the quota, establishment of minimum import prices, manipulation of imported beef volume allowed to go to market, and denial of import approvals. The request also stated that Korea's government support to domestic cattle producers exceeded limits established in the Uruguay Round Agreement on Agriculture.

Korea accounted for almost 15 percent of U.S. beef exports in 1995, and its 1998 share (under 8 percent) was well below what would have been expected if trade barriers fell. High potential domestic consumption and a poor resource base for cattle raising in Korea make it likely that free trade would result in large amounts of beef imports from major producers like the U.S.

Value of South Korea's Agricultural Imports Fell by More Than a Fourth in 1998

	Value			Volume			Unit value		
	1996	1997	1998	1996	1997	1998	1996	1997	1998
	US$ million			1,000 tons*			$/ton*		
Total agricultural imports	10,504	9,357	6,701	—	—	—	—	—	—
Selected commodities									
Feedgrains									
Corn	1,217	965	667	6,802	6,524	5,335	179	148	125
Wheat	192	154	271	958	1,096	2,349	201	141	115
Meats									
Beef	496	464	249	162	166	92	3,053	2,793	2,705
Pork	143	220	138	40	61	53	3,621	3,585	2,599
Oilseed complex									
Soybeans, for crush	372	407	293	1,166	1,244	1,089	319	327	269
Soymeal	294	224	207	1,113	731	930	264	306	223
Palm oil	103	110	98	185	197	151	558	556	644
Inputs to food industry									
Wheat, milling	531	440	392	2,219	2,229	2,345	239	197	167
Sugar, raw	443	420	375	1,399	1,437	1,378	317	293	272
Corn, industrial use	350	283	240	1,870	1,787	1,774	187	159	135
Soybeans, food use	102	108	86	299	324	324	340	332	266
Inputs to nonfood manufacturing									
Cattle hides	806	813	482	13,350	12,478	8,698	60,393	65,166	55,426
Cotton	714	583	522	346	315	303	2,060	1,853	1,725
Consumer-ready products									
Juices	112	110	66	63	75	45	1,778	1,459	1,454
Chocolate	78	81	46	25	28	18	3,168	2,943	2,607

*For hides, volume is in 1,000 pieces and unit value is per 1,000 pieces. — = not available.
Source: World Trade Atlas, Korean Republic Edition, GTI, Inc.

Economic Research Service, USDA

GSM Credits Spur U.S. Agricultural Exports

Late in December 1997, USDA offered a $1-billion allocation of credit guarantees under the GSM-102 program (GSM is General Sales Manager at USDA). These guarantees are used by importers to secure credit so that they can buy U.S. agricultural products. While GSM's relatively long repayment period (up to 2 years) held some attraction for Korea in the pre-crisis years, use had been declining as commercial credit became more plentiful.

In the past, GSM credits had been assigned to bulk input commodities, such as cotton and corn. In 1998, the program was designed with portions of the total allocated to meats and other consumer items, in addition to bulk commodities. By the end of fiscal-year 1998, applications for GSM guarantees totaled $1.38 billion out of $1.5 billion available for Korea—a high rate of use. The 1997/98 financial crisis demonstrated how useful the program could be when other credit sources are not available.

slaughter plants. Imports have grown slightly in 1999, but remain far below 1997 levels. U.S. exports of cotton to Korea increased both in volume and value, aided by the GSM program. Total cotton imports fell in 1998, but not as dramatically as imports of other industrial inputs. Imports in 1999 have increased somewhat, but the long-term trend is toward continued decline.

The value of Korea's imports of ***processed foods and beverages*** fell by over 40 percent in 1998. Although relatively new to Korea, these products accounted for 11 percent of total agricultural imports in 1997. Imports of processed foods and beverages had been insignificant until Korea began reducing trade barriers in 1989. Since then, imports have grown quickly, including items such as fruit juices, chocolate products, wine, beer, sausages, noodles, dairy foods, frozen french fries, cola bases, seasoning mixtures, tomato paste, ketchup, and canned vegetables and fruits.

Declining volume accounted for most of the decrease in total value of processed food and beverage imports in 1998. During the crisis, supermarket sales held up well while consumption in restaurants fell as consumers stayed home to save money. In addition, imports regarded as luxuries, or as discretionary purchases, declined sharply in volume: wine (73 percent), beer (84 percent), mineral and aerated water (58 percent), jams and jellies (78 percent), ice cream (69 percent), and biscuits (70 percent).

Imports of almost all processed foods and beverages have grown in the early part of 1999, but had not reached 1997 levels through May. Processed food imports, the most income-sensitive, are closely tied to modernization of the food retailing sector, which stalled during the crisis. As investment in hyper- and supermarkets resumes, consumer demand for diversity and convenience will lead to strong growth in imports of processed foods and beverages.

Agricultural Imports to Rebound

With economic growth resuming and credit becoming widely accessible, Korea's agricultural imports are rebounding sharply in 1999 and are expected to grow in coming years. Trade barriers, such as quotas, tariffs, and technical barriers, have recently fallen and are scheduled to fall even more. The crisis delayed many initiatives to increase imports in response to the new opportunities, but Korea's recovery of stability and prospects for growth will allow new imports to emerge rapidly.

The lower level of Korea's won helps domestic production and hurts imports. As long as Korea's currency buys less than it did two years ago, Korea's imports will be less than previously expected. However, the cost of agricultural production in Korea is still so much higher than in exporting countries that imports are viable. Many foods will be more efficiently produced outside Korea, stimulating imports.

Parts of Korea's manufacturing sector will again slip in international competitiveness as it regains economic vitality and lowers trade barriers. Higher income implies higher labor costs, and any industry heavily dependent on relatively unskilled labor will consider leaving Korea. The impact on agricultural imports will be mixed. Spinning and tanning will continue a gradual shift out of Korea, following footwear and textile production to other parts of Asia, Latin America, and Africa, reducing demand for cotton and hide imports. Soybean imports for crushing are likely to continue falling, replaced by meal and oil imports.

Other commodities have strong prospects for rapid growth. Meat consumption is still growing, and several factors indicate that the market for meats has not yet matured. Domestic prices are still relatively high, especially for beef, and meat marketing still faces infrastructural and legal constraints, such as government restrictions on the location of retail sales and on the choice of firms that can import beef. As prices decline and marketing practices modernize, meat consumption—and imports—will increase. Greater reliance on meat imports will reduce growth in Korea's feed imports, but this simply shifts the location of animal feeding to major producers like the U.S.—with little effect on the amount of feed necessary to provide Korea with increasing amounts of meat.

In addition to favorable prospects for meat imports, Korea's imports of fish are rising as catches of the domestic fleet decline. They rebounded by 90 percent over 1998 levels in the January-May period and will continue to grow, as strong demand confronts weakening domestic supply. The outlook for imports of processed products and beverages is bright, and shipments will tend to come from competitive producers such as the U.S., as trade barriers fall and the consumer economy once again prospers. AO

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Based in part on information and analysis from USDA's Foreign Agricultural Service in Seoul, Korea.

For more information on Korea's agricultural trade, policies, and outlook, visit the Economic Research Service briefing room at
www.econ.ag.gov/briefing/region/korea