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REPORT AND RECOMMENDATION

OF THE

PRESIDENT

TO THE

EXECUTIVE DIRECTORS

ON A

PROPOSED LOAN

TO THE

KOREA DEVELOPMENT BANK

WITH THE GUARANTEE

OF THE

REPUBLIC OF KOREA

March 7, 1975

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Currency Unit	=	Won
Won 485	=	US\$1.00
Won 1,000	=	US\$2.06
Won 1,000,000	=	US\$2,061.86
Fiscal Year	=	January 1 - December 31

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

REPORT AND RECOMMENDATION OF THE PRESIDENT  
TO THE EXECUTIVE DIRECTORS ON A PROPOSED LOAN TO  
THE KOREA DEVELOPMENT BANK WITH THE GUARANTEE OF  
THE REPUBLIC OF KOREA

1. I submit the following report and recommendation on a proposed loan in an amount in various currencies equivalent to \$60 million to the Korea Development Bank (KDB) to be guaranteed by the Republic of Korea. Interest on the loan would be at 8-1/2 percent per annum. The loan would be repaid substantially in conformity with a schedule based on the aggregate of the amortization schedules of sub-loans made pursuant to this loan. The maximum repayment period would be 18 years, including three years of grace.

PART I - THE ECONOMY

Background

2. The last Economic Report ("Current Economic Position and Prospects of the Republic of Korea") was distributed under cover of R74-42 dated March 4, 1974. An assessment of Korea's economic situation is given below. The Country Data Sheets are included in Annex I. An Industrial Sector Mission visited Korea in the fall of 1974 and an Economic Updating Mission returned in February 1975 after completing its field work in Korea; their reports are under preparation.

3. Korea's economic performance over the last decade has been outstanding. In the period 1964-73, the GNP growth rate averaged 10 percent a year in real terms and real per capita income more than doubled. The rapid rise of output and an appreciable decline in the population growth rate (from nearly 2.7 percent in the early sixties to 1.7 percent in 1973) were major reasons for the rapid increase in income. A key factor in the growth of the economy has been the increase of manufactured exports from about \$60 million in 1964 to \$2,800 million in 1973. Such exports in 1973 accounted for over 90 percent of commodity exports and about 29 percent of industrial output. The ratio of exports to GNP rose rapidly from 4 percent in 1964 to 27 percent in 1973 and the manufacturing sector as a proportion of GNP increased from 16 percent to 28 percent in the same period. Agriculture, which has had a growth rate of about 3.5 percent a year over the past several years, declined as a proportion of GNP from 46 percent in 1964 to 23 percent in 1973.

4. Rapid growth transformed the Korean economy from one characterized by dependence on agriculture and sluggish growth in the 1950s to one of dynamic growth based on increasing industrialization in the 1960s. Nevertheless, there have been problems. The two which have caused the Korean

Government most concern are (a) the resource management problem, resulting from a heavy reliance on external capital and (b) the question of distribution of growth benefits, arising out of a faster productivity growth in manufacturing than in agriculture.

5. Total real investment grew six-fold between 1964 and 1973, and the ratio of investment to GNP rose from 13 percent to 25 percent. External resource requirements also grew rapidly during 1970-71 averaging over 9 percent of GNP, roughly the same level as in the early sixties. The marginal saving rate during the last decade was 30 percent which would indicate that the large capital inflows did not weaken efforts to mobilize resources domestically. Korea, however, entered upon a period of rapid growth with a very low level of domestic savings and, therefore, in the interest of rapid acceleration of investment and growth tolerated relatively heavy dependence on external capital. In the early seventies when financial difficulties resulted from bunching of payments due on short and medium term debt and a sharp rise in the debt service ratio, the Government took corrective action to moderate the rate of private investment, to increase the inflow of capital on concessional terms from official sources, to impose restrictions on suppliers' credits, and to improve the balance of payments position through substantial exchange rate adjustments.

6. These measures, combined with a reduction in Government real investment and uncertainty in the Korean business community about export prospects, produced a marked slowdown in the economy during the 1970-72 period. Even with a continued high rate of export expansion (about 50 percent per annum on average in current terms), real GNP growth averaged only 8 percent per annum during 1970-72, compared with about 13 percent in the preceding three years. Real investment stagnated during 1970-72, and the ratio of fixed investment to GNP dropped from 27 percent in 1969 to 22 percent in 1972.

7. Although income distribution in Korea is generally more equitable than in comparable developing countries, the benefits of economic growth have not been shared evenly. The absolute gap in incomes between urban and rural areas widened during the 1960s despite a massive migration to the cities. Growth of labor productivity in agriculture has been considerably slower than in the manufacturing sector. Since 1967, the Government has attempted to raise farm incomes and to provide incentives for increasing foodgrain production through a price support system for rice and barley. These measures reduced markedly the gap between average rural and urban incomes during 1968-72. Nevertheless, growth of the industrial sector is likely to continue to be more rapid than that of the agricultural sector, and the Government believes that, unless the proportion of rural incomes provided by non-farm sources is increased, the disparity of incomes will tend to widen. Therefore, the Government broadened its efforts to achieve more balanced growth by pursuing policies of decentralizing industry and emphasizing investment in the less developed regions, and in late 1971 initiated the Sae Maeul (New Community) Movement as a nationwide comprehensive self-help program to increase productivity and incomes in the rural areas, where nearly half the population still lives, and to improve the quality of rural life.

### Recent Changes

8. During the last two years or so the Korean economic situation has been subject to sudden and sharp changes. Beginning with the latter part of 1972, the Korean economy witnessed an unprecedented boom. 1973 was an exceptional year, even by Korean standards, and set new records of growth in GNP, exports and savings. GNP grew by 16.5 percent in real terms, primarily because of increases in exports and fixed investment. Commodity exports, in nominal terms, rose by over 90 percent, denoting an increase in real terms of about 60 percent. National savings, which had dropped to about 15 percent of GNP in 1972, rose to 22 percent in 1973, surpassing the previous peak (1970) of about 18 percent. Foreign savings were only about 3 percent of GNP and financed only about 12 percent of total investment, compared with about 40 percent from 1968 to 1971. The rapid rise in foreign exchange earnings, which included a marked increase in tourism income, also reduced the ratio of debt service payments to export receipts to about 10 percent in 1973.

9. The remarkable performance of the economy in 1973 encouraged both business and Government to view the future with increased confidence. In the latter part of 1973, Korean economic aspirations were expressed in terms of targets of \$1,000 per capita income and \$10 billion of exports by the early 1980's. The long-term strategy implied the continuation over the next decade of the overall rate of GNP growth of about 10 percent per annum but with reduced dependence, in relative terms, on net inflows from abroad. At the same time, major structural shifts were being planned for manufacturing. The objective of deepening the industrial structure was to be achieved by emphasizing shipbuilding, steel, petrochemical and metal-working industries, while continuing to develop existing industries such as textiles and electronics. The long-term plan also provided for the achievement of parity between rural and urban household incomes by the early 1980's through accelerated growth in labor productivity in agriculture and an increase in off-farm employment by greater regional dispersion of industry.

10. The favorable economic developments of 1973 were interrupted by external developments in 1974. The sharp rise in the price of petroleum in late 1973, the recession in the Japanese and the U.S. economies during 1974, and the high level of foodgrain import prices have combined to bring about a major change in the short-term economic position of Korea. Owing to its poor natural resource endowment and because of its economic structure and growth strategy, Korea was severely affected by these recent international developments. Merchandise exports now account for about 30 percent of GNP in Korea and dependence on the Japanese and U.S. markets has remained heavy. A major element in the Korean export picture during 1973 was an expansion of over 200 percent in exports to Japan, which was made possible by a very sizeable expansion in total Japanese imports. Nearly 75 percent of total Korean exports went to the U.S. and Japan during 1973. Korea was thus particularly vulnerable to the recession in the Japanese and U.S. economies during 1974. The revival of the Japanese economy and the future trend in Japanese manufactured goods imports will probably continue to be major

determinants of the Korean growth rate in the future, although the Government is making efforts to diversify its export markets by encouraging sales in the Middle East and Europe.

11. In the short-run, however, the higher costs of energy and food imports have added a burden to the economy which is even more serious than the setback to export growth. Korean dependence on imported fuels is not only extremely heavy but is very closely linked to essential industrial and transport uses. The passenger vehicle fleet is small, with only one private car per 152 families; truck transport and diesel-powered rail traffic are the basic transport modes for commercial goods. The higher costs of petroleum added almost \$800 million to the Korean import bill between 1972 and 1974. Over the same period, the three-fold rise in the prices of foodgrains increased foreign exchange requirements by more than \$350 million, despite a decline in the volume of imports. Korea is at present importing about 2 million tons of wheat and about half a million tons of rice annually, constituting respectively 85 percent and 11 percent of total domestic consumption. Together petroleum and foodgrains accounted for 36 percent of Korea's increased import bill in 1974 and 25 percent of total import payments that year.

12. These international developments have greatly weakened the Korean balance of payments position in 1974 and prospectively in 1975, slowed the rate of growth of output and employment and increased inflationary pressures.

13. The current account balance of payments deficit widened from the low level of \$308 million in 1973 to an estimated \$1,440 million during 1974, or by more than \$1,100 million. The major factors in the deterioration were an adverse swing in the terms of trade of 16 percent (equivalent to a loss of about 5 percent of GNP) and a large negative balance on the services account, due in part to a decline in tourism receipts. The deterioration was notwithstanding a substantial further improvement in real exports of about 10 percent, to a total of \$4.8 billion, and only a modest growth in real imports. The entire improvement in export volume was concentrated in the first half of 1974. Real export earnings in the final quarter of 1974 are estimated to have been six percent below the corresponding quarter of 1973.

14. At current prices, total import payments (c.i.f.) are estimated to have been about \$6.9 billion in 1974, an increase of \$2.3 billion, or about 63 percent, over 1973. But in real terms, imports are estimated to have increased by little more than 2 percent in 1974, mainly as a result of decreases in imports of grains and capital goods, and only a small increase in raw materials.

15. It is estimated that the net inflows of capital (medium and long-term loans and foreign private investment) into Korea during 1974 remained at the 1973 level of about \$1 billion. Consequently, the increased current account deficit had to be financed entirely through an increase in private short-term debt, a reduction of external reserves, Bank of Korea borrowings

abroad and drawings on the IMF gold tranche and first credit tranche and the use of the IMF oil facility. Korea's net international reserves, which stood at about \$945 million at the end of 1973, had declined to about \$90 million by the end of 1974. The rundown of net reserves enabled the maintenance of levels of imports and economic activity in 1974 which otherwise would not have been possible.

16. Notwithstanding the Government's policy, the impact of external developments on Korea's domestic output, employment and prices has been marked. In the first half of 1974, GNP continued to grow in real terms by 14 percent over the corresponding period of 1973, as industrial output and real exports continued to increase and fixed investment remained at a relatively high level. In the second half of the year, however, there was a sharp slowdown in industrial output, private fixed investment and export sales (particularly for textiles and plywood). The GNP for the second half of 1974 is estimated to have been only about 3 percent above the level in the latter half of 1973. Despite the levelling off of industrial production there was a substantial build up in inventories of export products. Unemployment began to rise as a result of the combined effects of the industrial slowdown, business failures and temporary closures. Between August and November, 20,000 workers were idled. Failures of over 100 businesses in textiles, ceramics and electronics were reported and more than 250 others experienced temporary closures for varying periods. More than 650 businesses partially curtailed operations. Open unemployment at the end of 1974 is estimated to have reached about 600,000, or about 5 percent of the labor force, compared with an average of about 4 percent in 1973. However, because of less overtime, fewer shifts and partial workweeks, the real increase in unemployment and the decline in real wages was much greater.

17. Imported inflation has led to a very sharp upward pressure on the domestic price level. In addition to the sharply higher prices of imported petroleum and foodgrains, the average unit value of other imports increased by 45 percent during 1974. <sup>1/</sup> Consequently, the rate of domestic inflation accelerated with consumer prices rising at an annual rate of 31 percent between December 1973 and June 1974 and wholesale prices increasing at double that rate. Since the middle of the year the rate of domestic inflation has slowed somewhat, reflecting seasonal factors, the slower increase in the prices of imported goods and the dampening effects of rising inventories of manufactured goods. It is estimated that during calendar year 1974, wholesale prices rose by about 45 percent.

18. In general, the Government is committed to accepting necessary adjustments arising from higher energy and other import costs. It was

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<sup>1/</sup> The unit value of exports also increased during the year, but by only 34 percent.

not, however, prepared to place on consumers the full burden of higher import costs of basic foodstuffs. Thus, despite dramatic increases in prices paid by consumers for foodgrains, substantial subsidies are still involved in the sale of wheat and rice. Complete avoidance of these subsidies at a time of growing unemployment and declining real wages in manufacturing was considered inequitable. Nevertheless, the Government intends to move during 1975 to reduce the deficit on the grain account which has largely offset public savings during the last two years.

Government's Response to Higher Import Prices  
and Reduced International Trade

19. The Government began early in 1974 to take action to limit the growth of imports. In January, the general exemption from customs duties available for machinery imports for the export sector was eliminated. Taxes on luxury imports and a number of domestically produced commodities were raised. However, finished non-food consumer goods comprise a relatively small share of Korea's total imports (about 5 percent in 1973), so there has been limited scope for cutting down on non-essential imports. To reduce demand for petroleum products, tax rates including tariffs on private cars were raised substantially.

20. Because of slack demand, the burden of financing inventories and continued increases in costs, a growing number of industries faced serious cashflow problems in the second half of the year. This prompted a number of mid-year changes in Governmental policies. The generally tight financial policies in effect in the first half of the year were eased, credits for imported and domestic industrial inputs were increased and programs to purchase excess stocks and make available special credits to smaller businesses were begun or expanded.

21. The Government in December 1974 introduced a set of special measures to offset the sluggish demand for exports that had been experienced since mid-year. It expanded the program of export financing and provided loans for the stockpiling of essential raw materials. Credits to exporters for the purchase of imported raw materials and domestic goods were increased. On December 7, 1974, the currency was devalued by 17.5 percent to Won 485 per US dollar. The devaluation was not expected to increase exports appreciably because of the depressed state of Korea's overseas markets, but like some of the other measures, it was intended to improve the liquidity position of manufacturing enterprises. It should also improve the competitive position of import substitution industries which had been weakened during the year. But the devaluation will also result in continued inflationary pressures in 1975. Among measures taken by the Government to help the low income groups are substantial income tax relief, a 30 percent increase in salaries of Government employees and public works projects mainly in the urban areas to alleviate unemployment. The rural areas appear to have been hit less hard by domestic inflation. The terms of trade moved further in favor of the farmers during 1974 as the support price for rice was adjusted sharply upward.



22. The past year has been a period of very difficult adjustments for Korea which, by and large, have been made quickly and with realism. The Government rightly views some of its current economic problems as being essentially short-term in nature. It assumes that a recovery in the growth rate of OECD countries will take place in the second half of 1975, in which event Korean merchandise exports could be expected to increase by 10 to 12 percent in real terms for the year as a whole. Private fixed investment may remain depressed for some months but the Government intends to stimulate business and employment through increased public sector outlays, especially for irrigation, farmland reclamation, highway construction, housing and urban waterworks. For example, about 87,000 units of housing, in addition to the 112,000 units originally planned will be undertaken in 1975, and about 334,000 new jobs are to be created in the public sector with hiring priority to be given to unemployed persons in the low income groups. In addition to increased capital expenditures, the Government proposes to continue purchasing and stockpiling surplus inventories of such major industries as textiles and plywood, for later release when the export and domestic markets are more favorable. The overall budgetary deficit is expected to be substantially larger than in 1974 and it is to be financed mainly by borrowing from the Bank of Korea and from abroad. The Government is expected to restrict the expansion of credit in low priority areas, raise interest rates and increase the reserve requirements for banks to moderate inflationary pressures. Essentially, the Government's strategy is to minimize damage to the private sector during the current period of slack demand, so that when international economic activity picks up the Korean export sector will be able to respond. Excessive business failures and loss of capacity in the private sector during the present slump would make recovery of the Korean economy slower and more costly.

23. The considerable uncertainty surrounding the international economic situation makes it difficult to assess confidently Korea's economic prospects for 1975. The Government hopes that, with its antirecessionary measures, aided by a recovery in OECD countries in the second half of 1975, GNP in real terms may increase by 6-7 percent and industrial output by as much as 14 percent. However, if the recovery in the export markets is delayed, industrial growth would be less vigorous, perhaps in the range of 10 percent, and levels of unemployment and underemployment would be even higher.

24. Even with a recovery in the OECD countries later this year, Korea will face a large current account deficit estimated at about \$1,700 million. This estimate assumes that merchandise exports will increase by 10 percent in real terms during 1975, that real import growth will be limited to less than 9 percent, and that some marginal improvement (about 2 percent) in the terms of trade will take place. An overall import growth of around 9 percent will permit 11-12 percent growth in petroleum, food and raw materials imports and a modest increase in capital goods imports. With a slower growth of imports it would be difficult to maintain an adequate level of food supplies and to achieve the expected recovery of industrial output and exports in the second half of 1975. Finding the means to finance the large external deficit is Korea's most urgent economic challenge. The

servicing of the sizeable foreign borrowing required should not pose serious difficulties for Korea given the present low debt service ratio and continued good long-term prospects for export growth, provided that the proportion of added debt incurred on short and medium terms and at high interest rates is not too great. Korean export growth, which in real terms averaged approximately 30 percent a year during the last decade cannot be expected to be sustained at that rate in the future. Considering, however, that 90 percent of Korea's exports now, and prospectively, consists of manufactured goods, that its links with the Japanese economy remain strong, that vigorous efforts are being made to penetrate new markets, especially in the Middle East, and that progress has already been made in diversifying the industrial structure, a long-term real growth rate of exports of 10 to 12 percent seems entirely possible even if world trade in manufactures should expand comparatively slowly. With the prospect of slower growth in exports than in the past, Korea's plans already envisage greater emphasis on import substitution in agriculture, especially foodgrains, and in industry with special emphasis on increasing the domestic value added in exports. Forecasts of developments in the world economy and their impact on Korea which is so dependent upon them are especially difficult to make at this time. However, given Korea's record of successful economic management in the past 10 years and the skills, adaptability, vigor and inventiveness of its workers and entrepreneurs, one can be confident that ways will be found to surmount the problems facing the economy.

## PART II - BANK GROUP OPERATIONS

25. As of January 31, 1975, Korea had received 16 Bank loans and 8 IDA credits, amounting in total to \$517.2 million in loans and \$107.0 million in credits (taking into account cancellations and the refinancing of one IDA credit in a subsequent Bank loan).

26. About one-half of the total has been for the transport sector - \$119.7 million for railways, \$101.5 million for highways and \$80 million for ports. \$130.5 million has gone to agricultural projects - \$93 million for irrigation projects, \$7 million for livestock development, \$10.5 million for the provision of medium- and long-term credit through the National Agricultural Cooperative Federation (NACF), \$7 million for seeds production and \$13.0 million for an integrated agricultural products processing project. The Korean Development Finance Corporation (KDFC) has received \$95 million in Bank loans for relending to private industry. The balance of \$97.8 million was for two education projects, a tourism project, and a secondary cities regional project.

27. IFC has made six investments in Korea and its gross commitments amounted to \$21.1 million in loans and shares. <sup>1/</sup> It made its first equity

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<sup>1/</sup> A seventh investment in the Atlas Paper Co. amounting to \$5 million was cancelled at the request of the Company.

investment in KDFC, of \$0.7 million or 14 percent of KDFC's paid-in capital, at the time the Bank made its first loan to KDFC. A loan of \$1.4 million to, and an equity investment of \$0.3 million in, the Honam Silk Co. was made in 1969. In 1971, IFC purchased \$0.7 million of the shares of the Korea Investment and Finance Corporation - an institution whose function is to assist in the development of the capital and money markets, a further investment of about \$0.3 million was made in 1974. In July 1973, the IFC exercised preemptive rights and purchased at par about \$400,000 equivalent of KDFC's common stock. In June 1974, IFC approved an investment of \$17.3 million in the Gold Star Company Ltd. consisting of a loan of \$16.0 million and \$1.3 million in equity. Gold Star is a leading electronics manufacturer. Investments of \$9 million in Tong Yang Nylon Co., Ltd., and about \$3.5 million in Hae Un Dae Development Co., Ltd. for hotel development have been approved; an investment in the Korea Securities Finance Corporation is under consideration.

28. Of total Bank and IDA lending, about \$278.1 million remained undisbursed on effective loans and credits as at January 31, 1975. The rate of disbursements has increased in recent months. Annex II contains a summary statement of Bank loans, IDA credits, and IFC investments as of that date and notes on the execution of ongoing projects. As indicated in the notes, progress on project implementation is generally satisfactory, although difficulties have been encountered with some projects and most seriously with the Pyongtaek-Kumgang and Yong San Gang Irrigation Projects (Loan 600-KO and Loan 795/Credit 283, respectively).

29. The Bank's program for FY75 includes four operations in addition to the proposed loan: the secondary cities regional project, a program loan, a third education project and a fifth railway project. The first of these has been approved, documents relating to the proposed program loan have been distributed and negotiations on the two other projects have been substantially completed.

30. The emphasis which the Government places on agricultural and rural development will be reflected in the programs for the succeeding years FY76 and FY77. The report of the agriculture sector mission (R73-287, dated December 19, 1973) provided the basis for developing additional high priority agricultural projects. A second livestock project, the second stage of the Yong San Gang Irrigation Project, the Okseo irrigation and regional development project and the Miho Cheon and Naeseong-Cheon watershed development projects have already been identified and are under preparation, and follow-on projects in agricultural credit and agricultural products processing are also being considered.

31. Another major emphasis in Korea's plans is the development of industries such as steel, shipbuilding, machine tools and petrochemicals. Hitherto, the Bank's lending for industry to Korea has been solely through the KDFC. As indicated, a loan for industrial development through a second financial intermediary, the Korea Development Bank (KDB) - a Government-owned institution responsible for the largest share of term lending for industry in Korea - has already been appraised. Also under consideration

is a loan to the Medium Industry Bank which provides financing to smaller businesses.

32. The development of the industrial and agricultural sectors and of exports will require concurrent infrastructural development. Although the transport sector will be given relatively less emphasis than in the past, the investments required are large, and thus there is considerable financing for this sector in the proposed program.

### PART III - THE INDUSTRIAL SECTOR AND INDUSTRIAL FINANCING

33. Korea's highly successful growth performance in recent years was particularly impressive because it has a poor resource-endowment - apart from relatively poor grade coal and some iron ore it has hardly any mineral deposits and few sources of hydro-electric power. In the immediate post-Korean War years the economy, which was then predominantly agricultural, was sluggish; however growth began to accelerate sharply about 1963 and has resulted in the transformation of the traditional economy into one in which the dynamic industrial sector plays a pivotal role. The pace of industrialization led by the expansion of manufactured goods exports has been about the most rapid attained by any developing country over the last decade. The output of the manufacturing sector has risen at the rate of about 18 percent annually since 1963, and its exports which stood at less than \$50 million in that year rose to about \$2.8 billion by 1973, accounting for nearly 90 percent of total merchandise exports. The average annual manufacturing growth rate during the last decade has been over 19 percent per year and resulted in a rise in the share of manufacturing in GNP from 11 percent in 1960 to over 28 percent in 1973.

34. The industrialization strategy followed by Korea over the last decade was based on a clear recognition of the limitations placed on it by the country's relative lack of natural resources. It was primarily on this account that development planning centered around the aim of expanding the export of manufactures rather than concentrating almost entirely on import-substitution as was the case in many developing countries in the early sixties. One important ingredient in the success of this policy was the fact that formal education during the fifties was at a level comparable with that of countries enjoying income-levels three times as high as Korea. This gave Korea the advantages of a skilled and adaptable labor force as well as the ability to quickly develop efficient managerial talent. Therefore, Korea has adopted a policy of concentrating on labor-intensive industries such as textiles, clothing, electronics and plywood the capital requirements of which are low compared to output. In this respect, it is noteworthy that the great expansion of Korea's industrial structure in recent years has absorbed only 20 percent of total fixed investment, that the incremental capital:output ratio in manufacturing declined from 1.7 in 1968 to 1.4 in 1972, and that value added per worker, which is about \$1,700, compares favorably with that in other East Asian countries (Philippines: \$600; Taiwan: \$1,150; Malaysia: \$1,500).

35. The extent to which the Korean economy depends upon its light industry can be gauged from the fact that, in 1972, it accounted for nearly 90 percent of the exports of the manufacturing sector and about 80 percent of the value of total merchandise exports. Exports of textiles, plywood and electronics amounted to US\$950 million equivalent (roughly 56 percent of total merchandise exports). The Government has, however, been making efforts to deepen and diversify the industrial structure by encouraging the growth of intermediate and heavy manufactures. Since 1970, over half the total industrial investment has been allocated to the basic metal, chemical and petroleum industries. The opening of Korea's first steel mill at Pohang (which has an initial capacity of just over a million tons per annum) and a large shipyard at Ulsan (of a million ton gross capacity) are indicative of a shift into more sophisticated lines of production.

36. Korea's long-term development plans are formulated on the premise that the direction of its growth over the past decade, which lay along rapidly expanding manufactured goods export, can be extrapolated through the early 1980's. In 1972 the Government prepared a macro-economic planning framework for the 1972-81 period. This envisaged a rate of GNP growth of about 10 percent per annum and the expansion of exports at a rate somewhat in excess of this figure. Targets of expanding manufacturing output at the rate of about 17 percent per annum and its increase, as a proportion of total output (in value added terms), to 40 percent at the end of the period, as compared with around 25 percent at present, were also postulated. These quantitative goals were to be achieved, in large part, by increasing the capacity of heavy industry which was expected to absorb over 70 percent of planned industrial investment during 1973-76 and about 60 percent between 1977 and 1981.

37. The recent economic setbacks have led to a re-examination of these objectives and the strategy formulated to achieve them. The revision of the long range plan has not yet been completed, but it appears that the target for the average annual increase in GNP will be lowered to 7 to 8 percent and greater emphasis than formerly envisaged will be placed on increasing domestic value added. Consequently, the rate of growth of exports will also be lower than envisioned. However, one element of the new strategy which aims at a change in the structure of manufacturing output and exports towards heavier industries (shipbuilding, steel and petro-chemicals) will remain essentially unchanged although the shift will take place more gradually than had been anticipated prior to the increase in energy prices. Most of the figures relating to the projections of exports, value of production and investment needs of various segments of the industrial sector given in this section reflect the premises made in the 1972-81 plans which are currently under review. However, it is not expected that any drastic scaling-down or deferment of the investments proposed will be necessary. The allocation of a greater proportion of industrial investment towards increasing the production of capital and intermediate goods is a prudent move in view of the trend towards protectionism in some of Korea's potential markets and increasing competition from other developing countries with cheaper labor costs which will tend to limit the opportunities to continue expanding the export

of light manufactures at a pace sufficient to sustain the projected growth rate of the industrial sector. For this reason the Government expects to rely more heavily on heavy industry in the achievement of its economic growth targets. Thus, it is expected that the export of the products of heavy industry will account for a considerably greater proportion of the total export of manufactures by 1981 as compared to about 10 percent at present. Further, the proposed shift towards heavier industry should increase net foreign exchange earnings from the export of light industry products as a result of the reduction of the import component of the capital and intermediate goods it uses.

38. Korea's plans to develop its shipbuilding, steel and machine tool industries are illustrative of the proposed re-alignment of its development strategy towards increasing the production of intermediate and capital goods. The first steps in this direction have already been taken as pointed out in paragraph 28 above. The commissioning of the Hyundai Shipyard at Ulsan in 1973 raised Korea's annual shipbuilding capacity to over a million gross tons from the almost negligible figure of 63,000 gross tons per year previously. Orders for the building of ten large tankers have already been received; the first five tankers have been launched and one has been delivered. Korea's favorable sites and climate and its well-trained labor-force will give the country a strong comparative advantage in shipbuilding. Encouraged by the demand for ships from the Hyundai works, the Government is considering the construction of additional shipyards each with an annual capacity falling within the 750,000 - 1 million gross ton range over the next decade.

39. Korea's success in implementing the first phase of the Pohang Steel Mill (POSCO) project which came into operation in 1972 has led to the formulation of plans to increase the production of crude steel by about 15 million tons by the early eighties. Financing for the expansion of the Pohang steel mill to a capacity of 2.6 million tons of crude steel has been arranged and the installation of a second steel plant is under consideration. It is forecast that most of the increased output will go to satisfy domestic demand which is expected to rise to nearly 9.0 million tons by 1981 as compared to 2.6 million tons in 1972. Even so, exports of nearly a third of total production may be necessary by the early 1980's.

40. Korea's imports of industrial machinery amount to about \$700 million per annum. The domestic machine tool industry's output is about \$475 million equivalent; it operates at a low level of efficiency largely on account of the sub-optimal scale of its production units and the poor technology they employ. Korea's industrial plans for the remainder of the seventies will create a heavy demand for industrial machinery. The Government sees in this expected development an opportunity to modernize and expand the industrial machinery industry with the objective not only of becoming self-sufficient but also of realising export earnings of about \$1.5 billion per year by the beginning of the next decade. This implies a more than tenfold increase, by value, of the present output of the industry. Accordingly, investments totalling over \$4 billion equivalent to streamline

existing plants and install new capacity are planned for the 1973-81 period. Approximately 50 percent of the amount has been earmarked for a new machine-tool complex to be located at Chang-Won (near Masan on Korea's south-eastern coast).

41. The part which light industry is expected to play in the fulfillment of the export expansion objectives, though less important than in the last decade, is nevertheless still vital. In this connection, the textile industry in which some 30 percent of the industrial labor force is employed is expected to export goods of about \$2.4 billion by 1981 as compared with about \$1.3 billion in 1974. It is estimated that the industry will need an investment of about \$2.7 billion over the next decade in order to expand its capacity sufficiently to meet this goal. The 1981 export target for the buoyant electronics industry is of the order of about \$5 billion; it is expected to absorb nearly \$1.5 billion in additional investment over the next six to seven years.

42. The major re-structuring and expansion of Korea's industrial sector will require a heavy outlay of capital. Tentative figures indicate that the investment needs of major industries for the 1973-81 period could amount to as much as \$15 billion equivalent. The Government has embarked on a major effort to mobilize the funds required by increasing domestic savings. A National Investment Fund (NIF) Law was enacted in December 1973. The Minister of Finance is in charge of the Fund but in effect delegates its management and operation to the Governor of the Bank of Korea. By 1981, the NIF is expected to finance about 75 percent of total investment needs of major industries. The resources of the Fund will be mobilized mainly (about three-fourths) by issuance of NIF-Bonds and the remainder by direct subscription by the Government. NIF-Bonds will be bought by various savings institutions including banks and insurance companies and by private investors. The funds will be on-lent through the banking system for investments in fixed assets (about two-thirds) and for working capital needs (one-third) of major industries.

43. The timely provision of long-term finance for the key industries will depend to a large extent on the efficient operation of the NIF and the tapping of other sources of funds such as Korea's three major development finance companies - the Korea Development Finance Corporation (KDFC), KDB and the Medium Industry Bank (MIB). These three institutions were responsible for 64 percent of total medium and long term loans in Korea in 1973. The Bank has already made four loans to KDFC and is contemplating a fifth; the proposed loan will be the Bank's first to KDB which is the largest financial intermediary in Korea; a loan for the MIB is also being considered in order to support the Government's efforts to encourage the location of relatively small industrial units in the rural areas and so increase off-farm employment opportunities. The magnitude of the demand for term finance in Korea is such that these three institutions, even if their operations increase significantly, will continue to act in a complementary rather than a competitive manner.

#### PART IV - THE PROJECT

44. A report entitled "Appraisal of Korea Development Bank" (No. 592a-KO, dated February 26, 1975) is being distributed separately. A Loan and Project Summary is attached as Annex III. Negotiations were held in Washington from January 27 - February 4, 1975 with a Korean delegation led by Mr. W.T. Shim, KDB's Deputy Governor.

##### The Company

45. The KDB was established in 1954 as a fully owned Government bank and assumed the functions, assets and obligations of the Industrial Bank of Korea which had been operating since 1918. KDB's role in its first few years consisted essentially of helping in the reconstruction and rehabilitation of industry which had been severely disrupted during the Korean war. However, by the late sixties KDB had become considerably more "development-oriented" in its approach. In the first, post-war phase of its existence, KDB restricted its activities largely to making local currency loans to finance enterprises engaged in power generation, coal mining and textile manufacture. In recent years it has broadened its activities to include the provision of finance for virtually all the industrial sub-sectors.

46. In order to achieve its primary objective of promoting the industrial development of the nation, KDB's functions consist of: making long-term loans (in both local and foreign currency) to public and private industrial firms; extending working capital loans (in local currency) to existing clients; underwriting and guaranteeing debentures issued by public and private enterprises; making equity investments and underwriting share issues; extending guarantees (both in local and foreign currency), and providing foreign exchange banking services for its clients and Government enterprises. In addition, KDB performs an important function by temporarily retaining the majority interest in a number of Government-sponsored projects and eventually selling shares to private investors after improving their performance. KDB also carries out statistical surveys, conducts economic and industrial research, undertakes engineering surveys and business analyses and provides managerial assistance for the projects it sponsors. On occasion, it has been asked by the Government to advise on major economic policy issues and assist in the formulation and execution of government projects.

##### Policies and Functions

47. Although the Government is KDB's sole shareholder and appoints the Board of Executive Directors its policies are developed independently within the framework of overall economic priorities enunciated by the Government. Operational planning is done through an annual operational program which is essentially a statement of projected sources and uses of funds for a one year period. Significant amendments to KDB's operating procedures, its by-laws and annual budget are subject to the Government's approval. The



Government also takes the basic decisions with regard to very large projects of national priority for which it provides the funds although KDB does influence project-formulation in such cases and has the right to refuse to finance projects which do not meet its standards and criteria. Decisions in connection with KDB's guarantee operations are taken by a ministerial level committee. KDB has full autonomy in respect of the projects which it finances from the funds raised independently of the Government. Until 1969, KDB was completely dependent on the Government for its foreign currency resources. This position changed when the Asian Development Bank (ADB) made its first loan of \$10 million to KDB in 1970. Since then, over 95 percent of KDB's foreign currency resources have been obtained directly by the institution. KDB will have complete independence and autonomy in making decisions with regard to projects to be financed from the proceeds of the proposed loan.

48. KDB's operations are governed by the KDB Act, KDB's By-Laws, Operating manuals and a Policy Statement. The first Policy Statement was adopted by the KDB Board in 1970. It summarized principles defined in the other documents and added a few new ones. It contained the usual "financial prudence" limits on its operations (e.g. limits on its total equity investments and equity investment in a single enterprise, limit on total assistance to any single enterprise, etc.). However, the 1970 Policy Statement allowed KDB to exempt from the various limits all transactions relating to public sector projects and projects benefiting concerns in which KDB held equity. It also defined some of the limits in terms of KDB's net worth and "quasi-equity" <sup>1/</sup> whereas, in fact, KDB had no "quasi-equity". As of June 30, 1974, 64% of KDB's total portfolio was accounted for by the "exceptional" projects. The 1970 Policy Statement has now been revised to provide for a uniform financial discipline for all projects for which KDB assumes the risk; exceptions, which are expected to be very rare, to the various limits would still be permitted on the basis of the merits of individual cases. The revised Policy Statement also contains a new clause emphasizing that KDB shall follow sound financial policies, levy financial charges to cover not only all expenses but also to build adequate reserves, etc. The adoption of the revised Statement by KDB's Board is expected shortly and has been agreed as a condition of effectiveness of the proposed Bank loan.

#### Management and Organization

49. KDB is administered by a full-time Board of Executive Directors composed of the Governor, the Deputy Governor (both of whom are appointed by the President of the Republic upon the recommendation of the Minister of Finance) and seven Directors (who are appointed by the Minister of Finance upon the recommendation of the Governor). There is also an Auditor appointed by the Minister of Finance. Historically, all appointments to the Board, except that of the Governor, have always been made by means of promotion from within KDB thus insuring that the Board is composed of experienced professionals.

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<sup>1/</sup> KDB defines "quasi-equity" as those portions of Government loans to it which are repayable after 15 years though not subordinated.

50. KDB has more than 1,700 staff members of whom about a third can be considered as being in the professional cadre. About a fifth of the total staff is located in its 9 branches throughout Korea and its 2 Representative Offices in New York and Tokyo. About 200 of the professional staff have been trained in Japan or the USA. Most of the Department Directors have served KDB for many years. Professional staff are recruited just after finishing college through open competitive examination and they usually spend their entire career with KDB. It has a systematic training and career development program for staff at all levels.

#### Operations and Resources

51. During its 20 years of operation, KDB's total loan commitments have amounted to Won 659 billion (US\$1.4 billion equivalent). Over 85 percent of this amount has been committed during the six years ending December 31, 1974, reflecting an acceleration in its operations in recent years. Total outstanding loans amounted, at the end of December last year, to over Won 426 billion (\$878 million equivalent) relating to 2,070 projects; of this amount Won 394 billion (\$812 million equivalent) for 1,773 projects were for local currency loans; foreign currency loans amounted to Won 32 billion (\$66 million equivalent) for 297 projects. KDB's foreign currency lending operations began in 1960 when it assumed responsibility for the use of a line of credit given to the Government by USAID. Since then, as indicated in paragraph 40 above, KDB has obtained resources for foreign currency lending from the Asian Development Bank (3 loans totalling \$60 million), two syndicated Bank loans of \$25 million and \$80 million and a recent loan of \$19 million from Abu Dhabi. Nearly all foreign currency funds obtained from ADB and the U.S. Agency for International Development have been used to finance equipment purchases; the two loans obtained from foreign commercial banks have been used largely to make domestic currency loans.

52. One deficiency of KDB's usually competent appraisal procedures relates to the fact that it does not routinely undertake a thorough appraisal of the economic aspects of the projects it considers. Its staff does, however, have the professional capability to make such analyses. KDB will include an economic rate of return analysis for all sub-projects to be financed from the proceeds of the proposed loan and involving financing of more than \$750,000. The timing for the application of this kind of analysis for the vast majority of all of KDB's operations would be discussed during the course of the first Bank supervision mission for this loan.

53. KDB has a majority share holding in a few companies. It holds equity amounting to about Won 24 billion (\$49 million equivalent) in seven concerns 1/. In order to reduce its exposure in these companies (except

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1/ Two of the companies - the Readjustment Corporation (RC) and the Korea Industrial Leasing Company (KIL) - are regarded as "permanent" subsidiaries of KDB and represent an extension of its corporate functions.

for BC and KIL) KDB and the Government have agreed that the former will not increase its holdings in companies in which it has a majority share holding at present and that it will divest itself of its present holdings as soon as it prudently can. KDB has also agreed as a general rule, not to acquire more than 50 percent of the paid-up capital of any single company in the future. These measures are reflected in the amended Policy Statement.

54. KDB's guarantee operations amount to over twice the size of its loan and investment operations. In the 6 years ending December 31, 1974, total guarantees issued by KDB amounted to Won 1,616 billion (\$3.3 billion equivalent); total guarantees outstanding at the end of December 1974 amounted to Won 1,311 million (\$2.4 billion). If guarantees are included in its debts, KDB's debt/equity ratio would be 11.7:1. Moreover, some of the guarantees issued by KDB are very large, e.g., as of June 30, 1974, the fourteen largest guarantees represented almost 70 percent of total outstanding guarantees as of that date and the range was W 11.2 billion to W 201 billion (\$25 million to \$414 million). Although the delinquency rate so far has been negligible, the existing potential risk to KDB is considerable and could seriously affect KDB's long-term creditworthiness and financial soundness. Yet a complete elimination of KDB's guarantee function, or even a severe curtailment of it, would not be in the broader interests of the country. Korea needs and will long continue to need large inflows of foreign capital, and KDB is in a good position to facilitate such inflows by continuing to offer guarantees. On the other hand, KDB's risk needs to be reduced, particularly as in most guarantee operations the decisions are made by a ministerial level Committee and not solely by KDB. In order to safeguard KDB against the excessive risks associated with its guarantee operations, a "Guarantee Release Arrangement" has been worked out between the Government and KDB, covering more than 80 percent of the total outstanding guarantee portfolio. This Arrangement provides that the Government shall take the steps necessary to enable KDB to meet all of the obligations falling due under any default covered by the Arrangement. Further, as and when the Government and KDB reach the conclusion that the defaulting party will not be able to meet its obligations, the Government shall assume all future obligations of KDB under the guarantee contract. In view of this Guarantee Release Arrangement, it is appropriate to exclude the guarantees covered under the Arrangement from KDB's debt. Taking this into account, KDB's debt/equity ratio, at the end of December last year, was 3.3:1.

55. KDB's total investment in the Korea Electric Company (KECO) - the almost wholly Government-owned electricity generating and distribution company - amounted, as of June 30, 1974 to Won 134.5 billion (\$277.1 million). KDB's loans to KECO (amounting to Won 132.7 billion - \$273.3 million) accounted for nearly 37 percent of the former's total outstanding loan portfolio. In order to protect KDB against potential risks, KDB and the Government have entered into an arrangement whereby the Government has undertaken to reimburse KDB in the event of a default on KECO's part.

### Financial Results

56. KDB's overall profitability is low because the Government, which is the sole shareholder, regards it mainly as a purely developmental agency and not a profit-making institution. KDB's profits are tax-exempt and it is not required to pay any dividends.

57. KDB's interest rate structure has been influenced by the role it is expected to play. The interest rates on equipment loans in domestic currency range from 7.5 percent to 15.5 percent and those on foreign currency loans from 9 to 10.5 percent with the sub-borrower assuming the exchange risk. The economic cost of capital in Korea and the increasing cost of KDB's own foreign resources suggest that the interest rate structure needs revision. However, this is a question which needs to be addressed in the context of interest-rates applied for all term lending in the country. The Government is reviewing the level of interest rates and in particular the foreign exchange lending rates for all credit intermediaries. The matter will be discussed with the authorities during the course of discussions (scheduled for April this year) on the draft report of the economic mission which recently returned from Korea. The minimum interest rate on sub-loans made under the proposed loan would be the Bank's rate plus 2 percent with the exchange risk being borne by the sub-borrower.

### Economic Impact of KDB's Operations

58. KDB plays a predominant role in term financing in Korea. In 1973, it accounted for a little under half of all medium- and long-term loans made by the banking sector; it directly financed 8 percent of total fixed capital formation and 16 percent of total fixed investment in the manufacturing sector. Its clients account for about 40 percent of Korea's total exports of manufactures.

59. In 1972, enterprises assisted by KDB accounted for about a fourth of total industrial employment and output in the country; by the end of 1972, projects assisted by KDB had created 250,000 jobs.

60. An analysis of a sample of KDB projects indicates that they had highly satisfactory economic rates of return, which in most cases exceeded the financial rates of return; moreover in all cases the economic rate of return exceed 12 percent, which the Bank staff considers a reasonable estimate of the opportunity cost of capital in Korea. These results are not surprising since Korea's industrial development policies have been highly successful and KDB's close adherence to them has enabled it to finance economically sound projects.

### Audit

61. KDB's accounts are audited by its Government appointed internal auditor who is a permanent member of its Board. At the request of the

Bank, KDB engaged the services of outside auditors, who have given an unqualified report for 1973. KDB's accounts will be audited in future by independent qualified auditors satisfactory to the Bank.

#### Future Operations and Resource Requirements

62. Although the impact of the energy crisis has caused some slowing down of Korea's rate of growth and has affected export performance, it is likely that in the longer-term Korea will be able to adhere to the growth path of the last decade. Industry will have to continue to play an important role in Korea's growth efforts, and it is expected that the manufacturing sector will have to contribute a significant proportion of incremental output and will, in turn, require a high level of investment in the next decade if Korea is to achieve her growth targets. Because of its size, its competent management and staff, and its development oriented policies, KDB will have a crucial role to play in aiding Korea's continuing economic development.

63. KDB's operational forecasts for the 1975-79 period show that it will commit a total of Won 108.5 billion (\$2.2 billion equivalent) in loans and investments. The results of a recent KDB survey of the credit needs of its clients indicates that the projected volume of operations is likely to be restricted, if at all, by resource considerations rather than by any lack of demand for KDB's assistance.

64. The share of foreign currency loans in the total mix of loans is projected to increase gradually from 10 percent in 1973 to 15.8 percent in 1974 and to 19.4 percent in 1975. This reflects the anticipation of a change in the pattern of the financing of imports rather than a change in the nature and composition of projects to be financed. In the past, on average, 27 percent of KDB's domestic currency resources was used for the procurement of imported equipment and machinery. (Foreign exchange is made available for authorized imports by the Korean Government against equivalent payment in domestic currency). In view of the large demand for its domestic currency funds, KDB proposes to use foreign currency loans to an increasing extent to finance the import needs of its sub-projects.

65. Given Korea's rapid industrial growth and its increasing capacity to supply capital and intermediate goods to satisfy domestic demand for them, the need for domestic currency funds on the part of KDB's clients is likely to remain at a high level. Therefore, KDB intends to use only its borrowings from such international institutions as Kreditanstalt fur Wiederaufbau, ADB and the Bank to finance foreign currency loans, while funds to be raised through borrowings from foreign commercial banks and issuance of Industrial Finance Debentures (IFD's) in foreign currency would be converted to augment the domestic currency resources of KDB. During negotiations for the proposed loan, the Government confirmed that it would take steps to ensure that the year to year rollover of these IFD's would be achieved since a significant part of KDB's reserves are obtained by the

issuance of these nominally short-term securities. Moreover, KDB has taken a policy decision, with the knowledge of the Government, to raise a greater proportion of its resources through issuing more of its long-term debentures in foreign capital markets rather than short-term debentures in the domestic market. The Government has also agreed to guarantee KDB's debentures issued in the foreign capital markets. During the two years ending December 31, 1976, KDB's total additional commitments (loans and investments) are projected at about Won 385.7 billion (approximately \$795 million equivalent). Including an addition of about Won 35 billion (\$72 million equivalent) to maintain its satisfactory liquidity (actual investment in liquid assets as of December 31, 1974 was Won 31 billion; \$64 million), KDB's total resource needs to the end of 1976 total about Won 421 billion (\$868 million equivalent). KDB's business forecasts are conservative and should be attainable unless there is an unexpected setback to the Government's or KDB's efforts to raise resources. Between January 1975 and December 31, 1976 KDB plans to raise total resources of Won 374.4 billion (\$772 million equivalent) as follows:

<u>Source of Funds</u>	<u>Amount</u>	
	(Won billion)	(\$ million)
Increase in paid-in capital	11.5	23.7
Borrowings from:		
Government	59.8	123.2
NIF	122.2	251.7
IRF	11.5	23.7
Foreign commercial banks	38.8 /a	80.0
Issuance of IFD	66.0 /b	136.0
KfW (DM 15 million)	3.0 /a	6.2
ADB	32.5 /a	67.0
IBRD	<u>29.1 /a</u>	<u>60.0</u>
<b>Total</b>	<b>374.4</b>	<b>771.5</b>

/a In foreign currencies.

/b To be issued partly in foreign currency.

66. To the new resources referred to above should be added the uncommitted balance (W 45.2 billion - \$93.1 million) of resources available as of December 31, 1974, which would give a total of W 419.6 billion - close to the estimated net requirement of the period.

67. KDB intends to use the proceeds of the proposed Bank loan principally for projects in the private manufacturing sector although public sector projects will also be eligible to receive Bank funds. Individual sub-loans financed from the proceeds of the proposed loan will not normally exceed \$4 million in order to ensure that a reasonable number of sub-projects benefit. A free-limit of \$750,000 with an aggregate free limit of \$18 mil-

lion has been agreed upon during negotiations; this will ensure that the Bank will review sub-projects accounting for about 70 percent of the proceeds of the proposed loan.

#### Justification

68. Korea's ability to make the adjustments necessitated by the deterioration in its terms of trade, caused largely by the high prices it has had to pay for energy imports since late 1973, will be a crucial determinant of the success of its efforts to sustain a high growth rate. Industrial growth will remain one of the most important elements in the economy. The Government's overall economic and industrial policies (which are outlined in Annex I and Part III above) and, in particular the increased emphasis on the development of the capital and intermediate goods industries, are appropriate for the situation in which Korea is placed at present. KDB's organization, competent staff and its relations with the Government and the business community make it particularly suitable for providing finance for these types of projects. KDB has processed a large number of projects each year and has played an important role in the industrial development process of the country. Its investments are economically sound and have contributed significantly to employment. The average investment per worker of KDB's projects has been US\$17,000 including some very capital intensive projects. The average capital cost per new job compares favorably with the experience of other DFC-financed sub-projects in the region.

69. For the future, KDB's continued growth is not expected to be constrained by a lack of demand for the financing and other services it offers. The main objective of the Bank loan in addition to the provision of finance for industrial investment is to help KDB to expand its operations on an economically and financially sound basis by improving its appraisal standards, overall planning and financial management. The Bank's technical assistance is considered essential towards this end. The Government shares this view and has specifically expressed the wish that the Bank extend its support of DFCs in Korea, which has been confined to lending to KDFC, to include KDB and MIB - the two other major sources of long-term industrial finance.

#### PART V - LEGAL INSTRUMENTS AND AUTHORITY

70. The draft Loan Agreement between the Bank and the Korea Development Bank, the draft Guarantee Agreement between the Republic of Korea and the Bank, the report of the Committee provided for in Article III, Section 4(iii) of the Articles of Agreement of the Bank and the text of a Resolution approving the proposed loan, are being distributed to the Executive Directors separately.

71. I am satisfied that the proposed loan would comply with the Articles of Agreement of the Bank.

PART VI - RECOMMENDATION

72. I recommend that the Executive Directors approve the proposed loan.

Robert S. McNamara  
President  
by J. Burke Knapp

Attachments  
March 7, 1975



## COUNTRY DATA - KOREA

AREA	POPULATION	DENSITY
98,477 km <sup>2</sup>	32.4 million (mid-1972)	725 Per km <sup>2</sup> of arable land

## SOCIAL INDICATORS

	Korea		Reference Countries		
	1960	1970	Thailand	Turkey	Japan*
	1970	1970	1970	1970	1970
GNP PER CAPITA US\$ (ATLAS BASIS) /1	140 /a	310 /b	220 /b	370 /b	2,320 /b
<b>DEMOGRAPHIC</b>					
Crude birth rate (per thousand)	40 /c	28	43 /d	38 /d,e	19.2 /f
Crude death rate (per thousand)	11 /c	8	10 /d	13 /d,e	6.6 /f
Infant mortality rate (per thousand live births)	..	..	80-90	145 /g	12.4 /f
Life expectancy at birth (years)	56	65	59	55 /h	72
Gross reproduction rate /2	3.1 /n	2.5	3.2	2.6 /e,h	1.0
Population growth rate /3	3.0 /a1	2.2 /i	3.1 /i	2.5 /i	1.1 /i
Population growth rate - urban	7 /i	6 /i	5 /k	4.5 /i	3 /m
Age structure (percent)					
0-14	44	40 /b	45 /e	42	24.0 /f
15-64	53	57 /b	52 /e	54	68.8 /f
65 and over	3	3 /b	3 /e	4	7.2 /f
Age dependency ratio /4	0.9	0.8	0.9	0.8	0.4
Economic dependency ratio /4	1.6	1.4	1.1	1.1	0.6
Urban population as percent of total	28 /i	41 /i	25 /k	38 /b,l	72 /m
Family planning: No. of acceptors cumulative (thous.)	..	..	490	484 /o,p	..
No. of users (% of married women)	..	..	10	8.2 /g	..
<b>EMPLOYMENT</b>					
Total labor force (thousands)	7,500	10,500 /b	16,500	14,500 /r	53,000
Percentage employed in agriculture	66	48 /b	81	67	19.1
Percentage unemployed	9	4.5 /b	1	4	1.4
<b>INCOME DISTRIBUTION</b>					
Percent of national income received by highest 5%	17 /s,ai	15 /e,t	17 /t,u	32 /g,t,v	..
Percent of national income received by highest 20%	42 /s,ai	37 /e,t	46 /t,u	60 /g,t,v	..
Percent of national income received by lowest 20%	7 /s,ai	10 /e,t	7 /t,u	3 /g,t,v	..
Percent of national income received by lowest 40%	20 /s,ai	24 /e,t	17 /t,u	10 /g,t,v	..
<b>DISTRIBUTION OF LAND OWNERSHIP</b>					
% owned by top 10% of owners	27	28	..	53	..
% owned by smallest 10% of owners	3	2	..	0.9	..
<b>HEALTH AND NUTRITION</b>					
Population per physician	3,000 /c,v	2,210 /w	7,970	2,220	880
Population per nursing person	..	1,760 /w	6,650	1,880 /x	240
Population per hospital bed	2,600 /c	1,920	850	490	80
Per capita calorie supply as % of requirements /5	85	103	105	110	106
Per capita protein supply, total (grams per day) /6	53	65	52	78	76
Of which, animal and pulse	13 /c	19 /y,e	17 /ae	22 /aa	45
Death rate 1-4 years /7	..	..	..	15 /h	1.0 /f
<b>EDUCATION</b>					
Adjusted /8 primary school enrollment ratio	96	104	80 /g	111	100
Adjusted /8 secondary school enrollment ratio	27	41	13 /g	28	90
Years of schooling provided, first and second level	12	12	11	11	12
Vocational enrollment as % of sec. school enrollment	14	15 /f	12 /y,ab	14	20
Adult literacy rate %	..	91 /ac,ak	70 /e,r	55 /ad	99 /r,y
<b>HOUSING</b>					
Average No. of persons per room (urban)	2.8 /ae	2.7	..	1.9	1.0 /z
Percent of occupied units without piped water	88 /af	80 /af	..	64 /ag	5 /g,ag
Access to electricity (as % of total population)	28	50	17	41 /ah	..
Percent of rural population connected to electricity	12	30	13	18 /ah	..
<b>CONSUMPTION</b>					
Radio receivers per 1000 population	32	128 /f	83 /b	107 /b	658 /b
Passenger cars per 1000 population	0.4	2 /b	7 /f	4	117 /b
Electric power consumption (kwh p.c.)	71	392 /b	164 /b	304 /b	3,909 /b
Newsprint consumption p.c. kg per year	1.8	3.7 /b	1.5 /b	2.2 /b	19.6 /b

Notes: Figures refer either to the latest periods or to the latest years. Latest periods refer in principle to the years 1956-60 or 1966-70; the latest years in principle to 1960 and 1970.

/1 The Per Capita GNP estimate is at market prices for years other than 1960, calculated by the same conversion technique as the 1972 World Bank Atlas.

/2 Average number of daughters per woman of reproductive age.

/3 Population growth rates are for the decades ending in 1960 and 1970.

/4 Ratio of population under 15 and 65 and over to population of ages 15-64 for age dependency ratio and to labor force of ages 15-64 for economic dependency ratio.

/5 FAO reference standards represent physiological requirements for normal activity and health, taking

account of environmental temperature, body weights, and distribution by age and sex of national populations.

/6 Protein standards (requirements) for all countries as established by USDA Economic Research Service provide for a minimum allowance of 60 grams of total protein per day, and 20 grams of animal and pulse protein, of which 10 grams should be animal protein. These standards are somewhat lower than those of 75 grams of total protein and 23 grams of animal protein as an average for the world, proposed by FAO in the Third World Food Survey.

/7 Some studies have suggested that crude death rates of children ages 1 through 4 may be used as a first approximation index of malnutrition.

/8 Percentage enrolled of corresponding population of school age as defined for each country.

/a Computed by applying to the 1970 figure the growth rate of GNP per capita in real terms from 1960 to 1970; /b 1972;

/c 1962; /d 1965-70 UN estimate; /e Derived from Sample Survey estimates (240,000 persons), excluding 17 eastern provinces

/f 1971; /g 1968; /h 1965-67; /i 1960-72; /j Seoul city and municipalities of 3,000 or more inhabitants; /k Over 10,000 population; /l Administrative centers of provinces and districts ("Village" and "Kaza" centers); /m Cities ("Shi") having 30,000 or more inhabitants; /n 1950-55; /o 1964-June 1974; /p 86 percent being IUDs; /q Employed labor force; /r 15 years and over; /s Wage and salary income of households;

/t Households; /u Urban only; /v Disposable income; /w Number of the register not all working in the country;

/x Including assistant nurses and midwives; /y 1969; /z Estimate; /aa 1964-66; /ab Data on vocational education refer to public schools and includes technical education at the post-secondary level; /ac Definition unknown;

/ad Persons six years old and over who tell the census takers that they can read and write; /ae Data refer to households

/af Water piped inside; /ag Inside or outside; /ah Percentage of dwellings with electric lighting; /ai 1964;

/aj 1955-60; /ak Ten years and over.

\* Japan has been selected as an objective country due to the similarity of the present Korean economic structure to that of Japan in the mid-fifties (with the same principal resource base, i.e., efficient, industrious, cheap labor and heavy reliance on imported raw materials). Moreover, agriculture, transport, and other sectors of the economy have similar characteristics. Korea also has, in its Long-Term Plan (1972-81), a pattern of industrial development which is not very different from the one Japan pursued with great success in the sixties.

## KOREA

ECONOMIC DEVELOPMENT DATA SHEET  
(amounts in millions of U.S. dollars)

	Actual			Projected			1960-	1965-	1970-	1973-	1960	1970	1979
	1960	1962	1970	1973	1975	1979	1965	1970	1975	1979			
<b>NATIONAL ACCOUNTS</b>													
	3-Year Averages at 1967-69 Prices & Exchange Rates						Average Annual Growth Rate				As Percent of GDY		
Gross Domestic Product	3,167.6	4,343.0	7,252.0	9,760.8	11,766.2	16,306.2	6.5	10.8	10.2	8.9	100.2	100.1	101.6
Gain from Terms of Trade (+)	-8.6	-24.0	-8.6	-142.2	-318.7	-251.4	..	..	-	..	-0.2	-0.1	-1.6
Gross Domestic Income	3,161.0	4,319.0	7,243.4	9,618.6	11,447.5	16,054.8	6.5	10.9	9.6	8.9	100.0	100.0	100.0
Imports (incl. NFS)	337.3	548.4	2,142.5	2,766.7	3,511.7	4,499.0	10.2	31.2	10.4	8.5	10.7	29.6	28.0
Exports (import capacity)	113.1	302.5	1,301.7	2,536.0	3,395.0	4,566.0	21.7	34.0	21.0	10.3	3.6	18.0	28.0
Resource Gap	-224.2	-245.9	-840.8	-230.7	-116.7	67.0	1.1	29.0	-35.0	-	-7.1	-11.6	0.4
Consumption Expenditures	3,075.5	3,862.3	5,926.2	7,726.9	9,242.5	12,355.0	4.6	9.0	9.3	8.2	97.3	81.8	77.0
Investment (incl. stocks)	309.7	702.6	2,158.0	2,190.5	2,321.1	3,633.3	17.8	25.5	1.5	8.8	9.8	29.8	22.6
Domestic Savings	85.5	456.7	1,317.2	1,959.8	2,204.8	3,700.3	40.0	23.5	10.8	11.2	2.7	18.2	23.0
National Savings <sup>a/</sup>	329.9	663.2	1,503.1	2,024.8	2,184.8	3,467.5	15.0	17.7	7.8	9.4	10.4	20.8	21.6
<b>MERCHANDISE TRADE</b>													
	Annual Data at Current Prices										As Percent of Total		
Imports													
Capital Goods	70.0	73.0	590.0	1,148.0	1,527.0	2,470.0	0.8	51.4	21.0	13.6	16.3	29.8	24.2
Intermediate Goods (excl. fuels)	90.0	110.0	404.0	1,477.9	2,026.0	3,060.0	4.1	29.5	38.0	12.9	21.0	20.4	29.9
Fuels and Related Materials	31.0	31.0	136.0	387.0	1,307.0	2,138.0	0.0	34.5	57.0	33.0	7.2	6.8	20.9
of which: Petroleum	28.0	29.0	133.0	380.0	1,282.0	2,096.0	0.6	35.5	57.0	33.0	(6.5)	(6.7)	(20.5)
Consumption Goods	238.0	243.0	852.0	1,228.0	1,650.0	2,560.0	0.4	28.7	14.2	13.1	55.5	43.0	25.0
Total Merchandise Imports (cif)	429.0 <sup>a/</sup>	457.0	1,982.0	4,240.9	6,510.0	10,228.0	1.3	34.4	26.7	15.8	100.0	100.0	100.0
Exports													
Primary Products (excl. fuels)	37.0	64.0	131.0	314.0	337.0	362.4	11.6	15.4	20.6	2.4	67.3	14.9	4.4
Fuels and Related Materials	3.0	2.0	9.0	55.0	43.0	70.0	-7.8	35.1	36.7	4.1	5.4	1.0	0.8
of which: Petroleum	-	-	-	-	-	-	-	-	-	-	-	-	-
Manufactures	15.0	109.0	738.0	2,843.0	4,336.0	7,878.6	48.7	46.8	42.5	18.5	27.3	84.1	94.8
of which: Exports (fob)	55.0	175.0	878.0	3,212.0	4,716.0	8,311.0	26.2	38.6	40.0	17.2	100.0	100.0	100.0
Tourism and Border Trade	..	5.0	34.0	290.0	330.0	330.0	..	46.5	50.4	5.1	..	..	..
Merchandise Trade Indices			Average 1967-69 = 100										
Export Price Index	89.2	87.5	100.0	150.0	169.0	215.0	-0.5	2.7	8.5	6.2			
Import Price Index	104.0	103.0	100.0	153.0	195.0	237.0	-0.5	-0.5	8.9	7.6			
Terms of Trade Index	85.8	84.9	100.0	98.0	86.7	90.7	-0.5	3.4	-3.0	-1.3			
Export Volume Index	13.6	36.9	153.6	324.3	406.4	542.9	22.0	33.0	16.1	9.0			
<b>VALUE ADDED BY SECTOR</b>													
	Annual Data at 1967-69 Prices & Exchange Rates												
Agriculture	1,303.4	1,684.0	2,025.2	2,226.5	2,431.4	2,832.3	5.3	3.8	3.7	4.1	45.0	31.0	20.0
Industry and Mining	311.2	540.0	1,318.5	2,241.6	3,000.7	4,556.9	11.7	19.7	17.8	12.5	10.0	20.0	33.0
Services	1,306.1	1,715.0	3,162.0	4,249.1	4,873.9	6,632.0	5.6	13.0	9.1	9.3	45.0	49.0	47.0
Total	2,920.7	3,939.0	6,505.7	8,717.2	10,306.0	14,021.2	6.1	10.5	9.6	10.0	100.0	100.0	100.0
Current Receipts	388.4	394.6	1,212.1	1,202.4	1,695.4	2,990.3	0.3	25.2	7.0	16.4	13.0	19.0	18.0
Current Expenditures	421.2	374.2	883.2	1,010.0	1,295.5	2,491.9	-2.4	18.8	7.9	16.3	14.0	14.0	15.0
Budgetary Savings	-32.8	20.4	328.9	192.4	399.9	498.4	..	73.0	3.9	17.2	-1.0	5.0	3.0
Other Public Sector Savings	16.8	49.7	168.5	..	..	..	24.0	27.0	..	..	1.0	3.0	2.0
Public Sector Investment	108.2	165.8	472.6	364.0	571.0	747.6	8.9	23.2	3.9	12.7	4.0	7.0	4.0

CURRENT EXPENDITURE DETAILS (As % Total Current Expend.)	Actual		1971	1972	Est. 1973	DETAIL ON PUBLIC SECTOR <sup>b/</sup> INVESTMENT PROGRAM	At 1967-69 Prices		As Percent of Total	
	1965	1970					Plan (1967-71)	Plan (1973-81)	Plan (1967-71)	Plan (1973-81)
Education	15.0	15.0	17.0	16.0	16.0	Social Sectors*	317	5,116	29.0	42.0
Other Social Services	10.0	14.0	11.0	14.0	15.0	Agriculture	64	2,835	6.0	23.0
Agriculture	10.0	9.0	8.0	5.0	7.0	Mining and Manufacturing	92	1,064	8.0	9.0
Other Economic Services	19.0	16.0	18.0	20.0	16.0	Power	26	*	2.0	*
Administration and Defense	36.0	37.0	28.0	27.0	29.0	Transport and Communications	479	3,167	43.0	26.0
Other	10.0	9.0	18.0	18.0	17.0	Other	129	51	12.0	..
Total Current Expenditures	100.0	100.0	100.0	100.0	100.0	Total	1,107	12,233	100.0	100.0
<b>SELECTED INDICATORS</b>										
Average ICOR	2.2	2.4	2.8	2.8	..	FINANCING <sup>c/</sup>				
Export Elasticity <sup>e/</sup>	1.6	2.8	1.1	1.0	..	Public Savings	1,481	..	69.0	..
Marginal Domestic Savings Rate	0.30	0.30	0.22	0.29 <sup>f/</sup>	..	Program Aid	485	..	22.0	..
Marginal National Savings Rate	0.29	0.30	0.18	0.25 <sup>f/</sup>	..	Foreign Borrowing (Net)	61	..	3.0	..
						Domestic Borrowing (Net)	122	..	6.0	..
						Total	2,149	..	100.0	..

LABOR FORCE AND OUTPUT PER WORKER	Total Labor Force					Value Added Per Worker (1967-69 Prices & Exch. Rates)				
	In Millions		% of Total		1960-70 Growth Rate	In U.S. Dollars		% of Average		1960-70 Growth Rate
	1960	1970	1960	1970		1960	1970	1960	1970	
Agriculture	4.6	4.8	66	51	0.4	282	419	68	62	4.0
Industry	0.5	1.3	7	13	10.1	563	986	135	145	5.8
Services	1.9	3.5	27	36	6.1	701	930	169	137	2.8
Total	7.0	9.6	100	100	3.1	416	682	100	100	5.8

.. not available  
 .. not applicable  
 e staff estimate  
 \* Included in Social Sectors

a/ 1962  
 b/ Central Government  
 c/ Official (EPB)  
 d/ Fiscal Plan  
 e/ Based on three-year average  
 f/ 1973 is included  
 g/ Includes current transfers (net)

BALANCE OF PAYMENTS, EXTERNAL ASSISTANCE AND DEBT  
(amounts in millions of U.S. dollars at current prices)

	Actual				Estimated 1973	Projected					Avg. Annual Growth Rate 1973-1981	
	1969	1970	1971	1972		1974	1975	1976	1977	1978		1981
<b>SUMMARY BALANCE OF PAYMENTS</b>												
Exports (incl. NFS)	1,113	1,341	1,587	2,205	4,048	5,045	5,714	6,499	7,760	9,711	12,971	15.7
Imports (incl. NFS)	1,903	2,107	2,515	2,606	4,469	6,056	6,827	7,686	8,987	10,592	13,200	14.5
Resource Balance (X-M)	-790	-766	-928	-401	-412	-1,011	-1,113	-1,187	-1,227	-881	-229	
Interest (net)	-	-	-	-	-	-	-	-	-	-	-	
Direct Investment Income	-5	-37	-91	-140	-150	-167	-193	-286	-434	-684	-977	26.5
Workers' Remittance	(44)	(33)	(25)	(19)	-40	-50	-60	-80	-85	-138	-186	21.2
Other	246	180	171	170	260	241	230	220	210	200	200	-2.8
	-549	-623	-848	-371	-342	-987	-1,136	-1,333	-1,536	-1,503	-1,192	16.9
Private Direct Investment	16	38	56	47	149	200	250	275	300	350	425	14.0
Official Capital Grants	56	122	135	-16	-	-	-	-	-	-	-	-
Public M&T Loans												
Disbursements	666	422	593	721	693	1,027	1,135	1,425	1,615	1,766	1,539	10.5
Repayments	-112	-205	-237	-216	-256	-243	-231	-247	-352	-554	-900	17.0
Net Disbursements	554	217	356	505	437	784	904	1,178	1,263	1,212	639	4.9
Other M&T Loans												
Disbursements	17	78	33	49	52	84	85	107	122	133	116	10.6
Repayments	-3	-8	-10	-9	-16	-18	-18	-19	-26	-42	-68	19.8
Net Disbursements	14	70	23	40	36	66	67	88	96	91	48	3.7
Short-term Capital	77	249	224	-91	45	-	-	-	-	-	-	-
Change in Gross Reserves	-162	-57	49	-155	-325	-	-	-	-	-	-	-
F Errors and Omissions	-6	-16	6	41	-	-	-	-	-	-	-	-
Other	-	-	-	-	-	-	-	-	-	-	-	-
Public M&T Loans												
IMRD 1/	65	40	85	73	183	-	-	-	-	-	-	-
IDA 1/	15	15	7	26	20	-	-	-	-	-	-	-
ADB	25	20	81	68	100	-	-	-	-	-	-	-
Other Multilateral	-	-	-	-	-	-	-	-	-	-	-	-
Governments	154	221	309	409	350	-	-	-	-	-	-	-
Suppliers	297	158	204	108	-	-	-	-	-	-	-	-
Financial Institutions	116	118	11	106	-	-	-	-	-	-	-	-
Bonds	-	-	-	-	-	-	-	-	-	-	-	-
Public Loans n.e.i.	30	-	-	-	-	-	-	-	-	-	-	-
Total Public M&T Loans	702	572	697	790	653	-	-	-	-	-	-	-
<b>DEBT AND DEBT SERVICE</b>												
Public Debt Out. & Disbursed						1,480	1,698	2,097	2,588		3,025	
Interest on Public Debt						32	61	90	92		102	
Repayments on Public Debt						112	205	237	216		256	
Total Public Debt Service						144	266	327	308		358	
Other Debt Service (net)						5	14	22	23		27	
Total Debt Service (net)						149	279	349	331		385	
<b>Burden on Export Earnings (%)</b>												
Public Debt Service						12.9	19.8	20.6	14.0		8.8	
Total Debt Service						13.4	20.8	22.0	15.0		9.5	
TDS+Direct Invest. Inc. 2/						14.3	23.6	27.7	21.4		10.5	
<b>Average Terms of Public Debt</b>												
Int. as % Prior Year DO&D						3.5	4.1	5.3	4.4		4.1	
Amort. as % Prior Year DO&D						12.1	13.8	14.0	10.3		9.8	
IMRD Debt Out. & Disbursed						2.3	9.6	40.2	94.7		139.6	
" as % Public Debt O&D						0.2	0.6	1.9	3.6		4.6	
" as % Public Debt Service						-	0.4	0.7	2.2		2.9	
IDA Debt Out. & Disbursed						25.6	25.7	39.9	47.1		54.9	
" as % Public Debt O&D						1.7	1.6	1.9	1.8		1.8	
" as % Public Debt Service						0.1	0.1	0.1	0.1		0.1	

	Actual Debt Outstanding on Dec. 31, 1972	
	Disbursed Only	Percent
World Bank	94.7	3.7
IDA	47.1	1.8
ADB	31.7	1.2
Governments	1,177.5	45.5
Suppliers	937.8	36.2
Financial Institutions	294.4	11.4
Bonds	-	-
Public Debts n.e.i.	5.0	0.2
Total Public M&T Debt	2,588.2	100.0
Other M&T Debts	206.8	-
Short-term Debt (dist. only)	-	-

. not applicable  
.. not available  
... not available separately but included in total

e staff estimate  
- nil or negligible  
-- less than half the smallest unit shown

1/ Fiscal years  
2/ 1969-72 figures include interest



KOREA

THE STATUS OF BANK GROUP OPERATIONS IN THE REPUBLIC OF KOREA

A. Statement of Bank Loans and IDA Credits (as at January 31, 1975)

<u>Loan or Credit Number</u>	<u>Year</u>	<u>Borrower</u>	<u>Purpose</u>	US\$ Million		
				<u>Bank</u>	<u>IDA</u>	<u>Undisbursed</u>
Five loans and credits fully disbursed				24.7	39.7	
600	1969	ADC	Irrigation	45.0		8.0
151	1969	Republic of Korea	Education		14.8	3.3
669	1970	Republic of Korea	Railways	40.0		2.9
234	1971	Republic of Korea	Livestock		7.0	.4
735	1971	KDFC	Dev. Fin. Co.	30.0		1.3
769	1971	Republic of Korea	Highways	54.5		1.4
283	1972	Republic of Korea	Irrigation		15.0	7.8
795	1972	ADC	Irrigation	33.0		32.4
335	1972	Republic of Korea	Agricultural Cr.		10.5	3.9
863	1972	Republic of Korea	Railways	40.0		18.3
905	1973	KDFC	Dev. Fin. Co.	40.0		11.6
906 & 394	1973	Republic of Korea	Education II	23.0	20.0	42.8
917	1973	Republic of Korea	Ports	80.0		77.9
942	1973	Republic of Korea	Seeds Production	7.0		6.9
953	1974	Republic of Korea	Tourism	25.0		25.0
956	1974	Republic of Korea	Highways II	47.0		34.2
994 /a	1974	AFDC	Agriculture	13.0		13.0
1070 /a	1975	Republic of Korea	Secondary Cities	<u>15.0</u>		<u>15.0</u>
Total				517.2	107.0	306.1
of which has been repaid				<u>11.8</u>	<u>0.3</u>	
Total now outstanding				<u>505.4</u>	<u>106.7</u>	
Amount sold				2.0		
of which has been repaid				<u>0.8</u>		
Total now held by Bank and IDA (prior to exchange adjustment)				<u>504.2</u>	<u>106.7</u>	
Total undisbursed				<u>270.8</u>	<u>35.3</u>	<u>306.1</u>

/a Not yet effective

B. STATEMENT OF IFC INVESTMENTS (as at January 31, 1975)

<u>Year</u>	<u>Obligor</u>	<u>Type of Business</u>	<u>Amount in US\$ million</u>		
			<u>Loan</u>	<u>Equity</u>	<u>Total</u>
1968	KDFC	Development financing	-	0.7	0.7
1969	Honam Silk Co.	Textiles	1.4	0.3	1.7
1970	Atlas Paper Co.	Pulp and paper	4.5	0.5	5.0*
1971	Korea Investment and Finance Corp.	Capital market development	-	0.7	0.7
1973	KDFC	Development Financing	-	0.4	0.4
1974	Gold Star & Co. Ltd.	Electronic Products	16.0	1.3	17.3
1974	Korea Investment and Finance Corp.	Capital market development	-	0.3	0.3
	Total gross commitment		21.9	4.2	26.1
	less cancellations, terminations, repayments and sales		<u>9.6</u>	<u>0.5</u>	<u>10.1</u>
	Total commitments now held by IFC		<u>12.3</u>	<u>3.7</u>	<u>16.0</u>
	Total undisbursed		<u>8.9</u>	<u>-</u>	<u>8.9</u>

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\* Cancelled at the request of the Company

PROJECTS IN EXECUTION <sup>1/</sup>

Loan No. 600

Pyongtaek-Kumgang Irrigation Project; US\$45.0 million  
Loan of May 23, 1969; Closing Date: December 31, 1976

The Project includes irrigation for about 35,000 ha, improvement of drainage and roads, consolidation of paddy fields, benching of upland and tidal land reclamation. Construction was delayed by a reorganization of the executing agency and a delay in hiring consultants. The major project components (two sea dikes, the main distribution system and pumping plants) were largely completed by the end of 1974. Contracts for nearly all of the remaining work have been awarded. Cost considerations have led to the exclusion of about 5,000 ha of land from the project. Costs have risen from US\$90 million at appraisal to about US\$130 million largely because of the increased costs of right-of-way, engineering, administration and land consolidation. Preliminary estimates indicate increases in the price of rice will partially offset the effects of higher costs and reduced irrigable area. The economic rate of return is now estimated to be about 10 percent, compared with the appraisal estimate of 14 percent. The implementing agency (ADC) has reviewed ways of economizing on the remaining work which should lead to some marginal cost savings. About 82 percent of the Loan has been disbursed. Construction is progressing satisfactorily and is scheduled for completion by mid-1976.

Credit No. 151

First Education Project; US\$14.8 million Credit  
of June 4, 1969; Closing Date: December 31, 1975

This Project comprises: (a) the expansion and equipping of 27 technical, commercial and agricultural high schools, 5 post-secondary higher schools and 4 university teacher training departments; and (b) 26 man-years of technical assistance and 20 man-years of overseas fellowships to support the development of agricultural and technical education. Project implementation, which was slow at commencement, has improved and the project is now 12 months behind schedule compared with the 15 months delay estimated a year ago. All civil works, furniture procurement, technical assistance and fellowships have been completed; 70 percent of the equipment has been procured and the remainder is expected to be delivered during 1975. The Credit is expected to be fully disbursed by the present Closing Date.

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1/ These notes are designed to inform the Executive Directors regarding the progress of projects in execution, and in particular to report any problems which are being encountered, and the action being taken to remedy them. They should be read in this sense, and with the understanding that they do not purport to present a balanced evaluation of strengths and weaknesses in project execution.

Loan No. 669                      Third Railway Project; US\$40.0 million Loan and  
Credit No. 183                      US\$15.0 million Credit of May 14, 1970; Closing Date:  
December 31, 1975

The bulk of the Loan and Credit was earmarked for the purchase of freight cars, diesel locomotives, and telecommunications and track maintenance equipment. Progress is generally satisfactory except for delays in the procurement of some microwave equipment which has been re-tendered.

Credit No. 234                      Integrated Dairy Beef Development Project;  
US\$7.0 million Credit of February 11, 1971;  
Closing Date: March 31, 1977

The development of about 700 small and medium-sized dairy farms by providing long-term loans and the construction and operation of two dairy products processing plants are the principal components of the Project which also includes the provision of management and technical services. Project execution has been satisfactory. To date, about 591 farmers have participated and farm loans of about US\$4.5 million equivalent have been approved. About 4,900 head of cattle have been purchased and two dairy plants have been constructed and are in operation. The proceeds of the Credit, except those earmarked for technical services, are expected to be fully committed by the end of this month.

Loan No. 735                      Third Korea Development Finance Corporation Project,  
US\$30 million Loan of May 14, 1971; Closing Date:  
August 31, 1975

The Project is progressing satisfactorily. The Loan is fully committed.

Loan No. 769                      First Highway Project; US\$54.5 million Loan of  
June 29, 1971; Closing Date: November 30, 1975

The construction of approximately 370 km of national highways between Jeonju and Busan was satisfactorily completed in December, 1973, at a final cost about five percent above the appraisal estimate. Feasibility studies and detailed engineering have been completed for 1,400 km and 900 km of national highways, respectively. A study of road maintenance and the establishment of a pilot maintenance organization formed the basis of the creation of a country-wide Highway Maintenance Organization which is being carried out under the Second Highway Project.



Loan No. 795  
Credit No. 283

Yong San Gang Irrigation Project; US\$33.0 million Loan  
and US\$15.0 million Credit of February 2, 1972; Closing  
Date: September 30, 1977

This Project aims at transforming an area with the highest drought frequency in Korea into one with year-round irrigation and crop diversification. Also, there will be increased production of high value crops such as fruits and winter vegetables. Design work is proceeding satisfactorily and the work on four dams, the main canals and land consolidation has started. Award of the three remaining major contracts anticipated for canals and land consolidation will be delayed until next summer, with construction to start after the rice harvest, i.e. roughly a year later than scheduled at appraisal. The delay was caused mainly by financial difficulties attributed to price escalation and design modification. The cost increases will be partially compensated for by benefits attributable to the enlargement of the area to be irrigated by about 1,400 ha.

Credit No. 335

Agricultural Credit Project: US\$10.5 million  
Credit of September 29, 1972; Closing Date:  
September 1, 1976

The Credit supports a three year lending program to small farmers to develop orchards, sericulture and mushroom production and to encourage the breeding of poultry and swine. It also finances an organizational and accounting study of the National Agricultural Cooperative Federation (NACF) and the strengthening of its training facilities. The Project is progressing satisfactorily and its disbursement is proceeding on schedule.

Loan No. 863

Fourth Railway Project; US\$40.0 million Loan of  
November 22, 1972; Closing Date: December 31, 1976

The main elements of the Project are: electrification of lines in the Seoul suburban area; purchase of electric railcars and locomotives; the completion of electrification of 350 km of line running from Seoul to the northeastern part of Korea; track and bridge renewal; provision of yard facilities; acquisition of passenger and freight cars; and improvement of facilities for the maintenance and repair of motive power and rolling stock. No major problems have been encountered; about 90 percent of the Loan proceeds have been committed.

Loan No. 905

Fourth KDFC Project; US\$40.0 million Loan of June 13,  
1973; Closing Date: December 31, 1977

The Project is progressing satisfactorily.



Loan No. 953

Kyongju Tourism Project; US\$25.0 million Loan of  
January 4, 1974; Closing Date: December 31, 1978

The Project forms part of the first phase of the planned development of the Bomun Lake resort near Kyongju. It provides for a multi-purpose dam; an irrigation system for about 1,200 ha; improvement and expansion of the water supply and sewerage and solid waste disposal systems for the city of Kyongju and the resort area; installation of electrical supply and telecommunication facilities for the resort area; the construction and/or re-alignment of about 57 kms of roads; infrastructure including storm water drainage, environmental sanitation, community facilities, a golf course, a school for training hotel personnel; and a feasibility study for the development of tourism on Cheju Island. The Loan was declared effective on May 6, 1974. Final design for almost all Project components is complete and the first four contracts have been awarded.

Loan No. 956

Second Highway Project; US\$47.0 million Loan of  
January 25, 1975; Closing Date: December 31, 1977

The Project, which forms part of the Government's 1972-76 road construction and paving program, consists of the construction, chiefly on new alignments, of about 130 kms of highways; feasibility studies by consultants of about 1,000 kms of national and provincial roads, followed by detailed engineering where justified; and the procurement of highway maintenance and workshop equipment for the extension of a new highway maintenance program from a pilot province to the remainder of the country. All construction and paving contracts have been awarded.

Loan No. 994

Integrated Agricultural Products Processing Project;  
US\$13.0 million Loan of June 7, 1974; Closing Date:  
June 30, 1979

The Project aims at integrating the on-farm production of commercial crops for export with efficient hygienic processing facilities using land that is presently idle or underutilized. It comprises (i) on-farm development of asparagus, oak mushrooms and mushrooms; (ii) construction of and improvements to facilities to process asparagus, oak mushrooms, mushrooms and fruits; and (iii) technical assistance including training of staff, services of consultants, etc. The terminal date for effectiveness of the Loan has been extended to April 15, 1975, to provide additional time for recruiting a Project Manager. The selection of a proposed Project Manager has been approved and, consequently, the Loan will be declared effective shortly.

Loan No. 1970

Secondary Cities Regional Project; US\$15.0 million  
Loan of January 15, 1975; Closing Date: March 31, 1979

The principal aims of the Project are the establishment of an organizational framework for regional investment, planning and development and to improve working and living conditions in the secondary cities of the less developed Gwangju region. The main elements of the Project are: (i) housing sites and services in the cities of Yeosu, Mogpo and Gwangju (370,384 m<sup>2</sup>); (ii) a fishery harbor complex with industrial processing zone (215,385 m<sup>2</sup>) in Yeosu; (iii) a city market in Suncheon City (33,160 m<sup>2</sup>); and (iv) access roads i Yeosu and Mogpo (6.61 km). It also provides technical assistance to strengthen regional planning and development, to improve the utilization of existing water supply systems in the four cities, to assist the management and operation of the fishery complex and to carry out feasibility studies of project proposals identified under the UNDP-financed Phase II Regional Study.

LOAN AND PROJECT SUMMARY

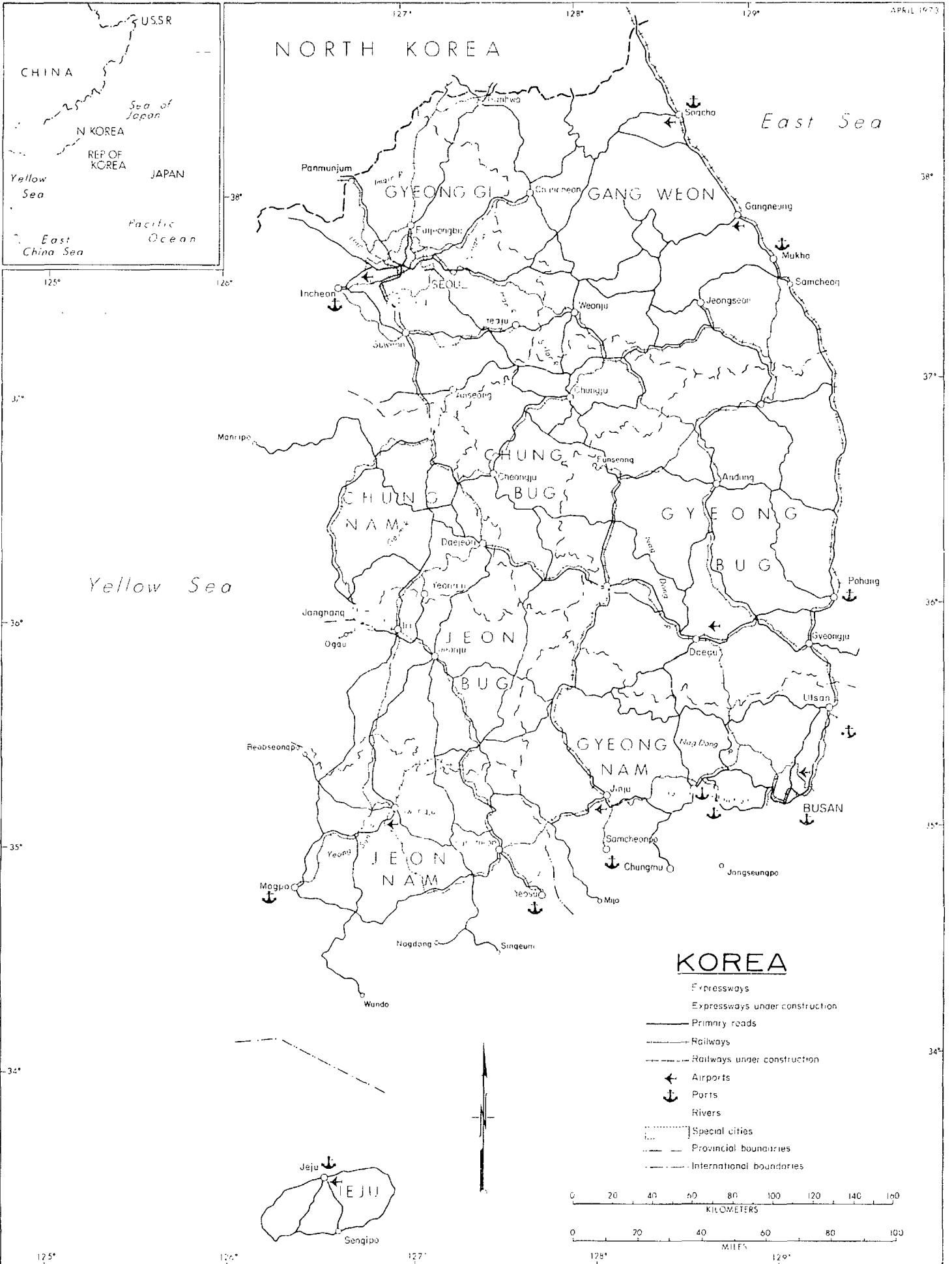
Korea Development Bank Project

Borrower: Korea Development Bank (KDB)  
Guarantor: Republic of Korea  
Amount: \$60.0 million  
Interest Rate: Standard  
Commitment Charge: Standard  
Terms: Amortization to conform substantially to the aggregate of the amortization schedules applicable to the specific investment projects financed out of the proceeds of the proposed loan. The maximum repayment period would be 18 years, including three years of grace.  
Purpose: The proposed loan would be used by KDB to make sub-loans to finance direct imports for industrial sub-projects during the period mid-1975 to mid-1977.

<u>Estimated</u> <u>Disbursements:</u>	<u>Calendar Year</u>	<u>US\$ Million</u>
	1975	1.50
	1976	27.00
	1977	29.50
	1978	2.00

Appraisal Report: 592a-KO dated February 26, 1975.





NORTH KOREA

East Sea

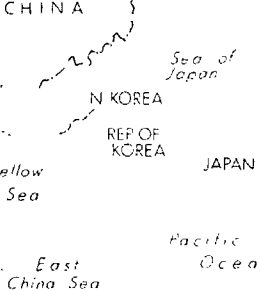
Yellow Sea

KOREA

- Expressways
- Expressways under construction
- Primary roads
- Railways
- Railways under construction
- Airports
- Ports
- Rivers
- Special cities
- Provincial boundaries
- International boundaries

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KILOMETERS

0 20 40 60 80 100  
MILES



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JEON BUG

GYEONG NAM

JEON NAM

BUSAN

Incheon

SEOUL

Seoul

Ulsan

Daegu

Busan

Mogpo

Yeosu

Chungmu

Samcheong

Jongseungpo

Jangnang

Yeosu

Samcheong

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Jongseungpo

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