

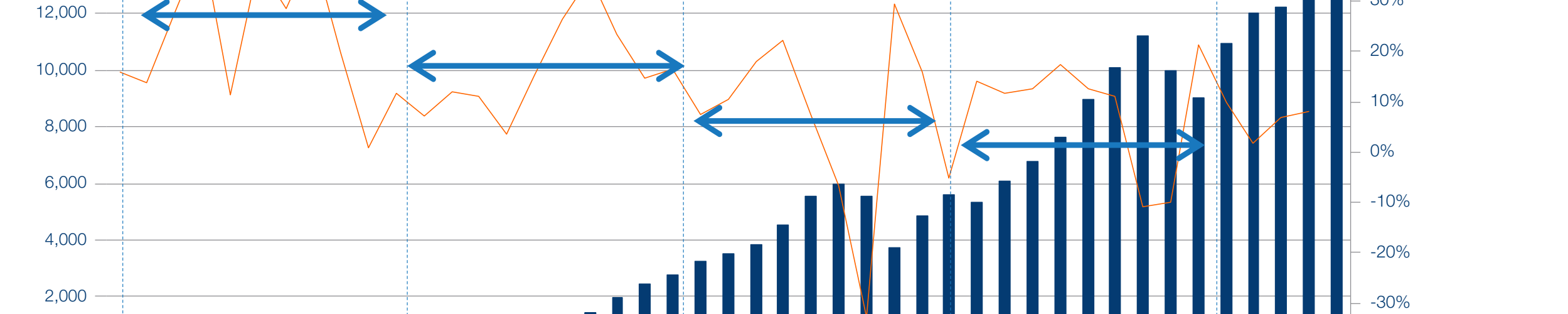


## Korea's Transformation: Factory Production to Innovation Generation

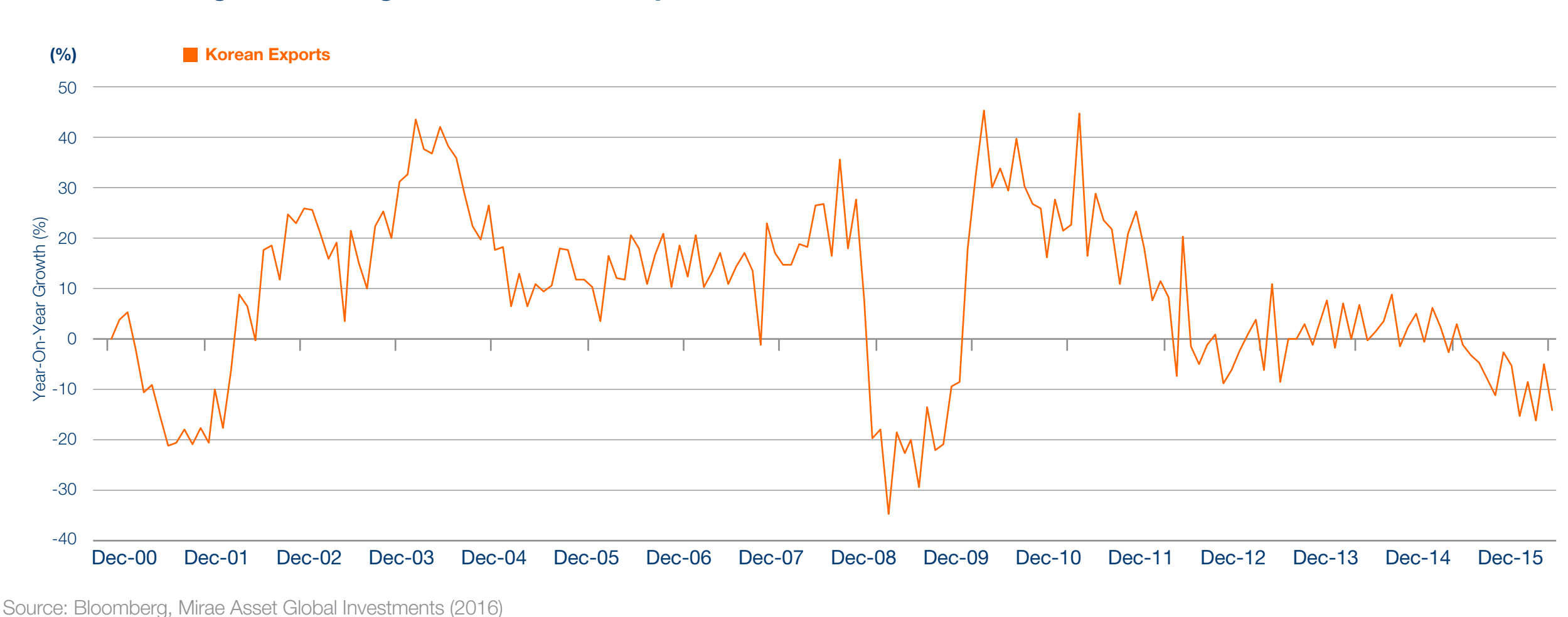
### The Hermit Kingdom: Then and Now

- Korea has been a traditional powerhouse in manufacturing, experiencing robust gains in social, political, and economic indicators in past decades, although the country now faces a “new normal” of lower growth and muted inflation as it is impacted by dynamics beyond its borders.
- A rebalancing China has pulled down Korean exports, widely regarded as a bellwether of global trade.

### Korea: Decelerating Economic Growth



### While A Slowing China Drags Down Korean Exports

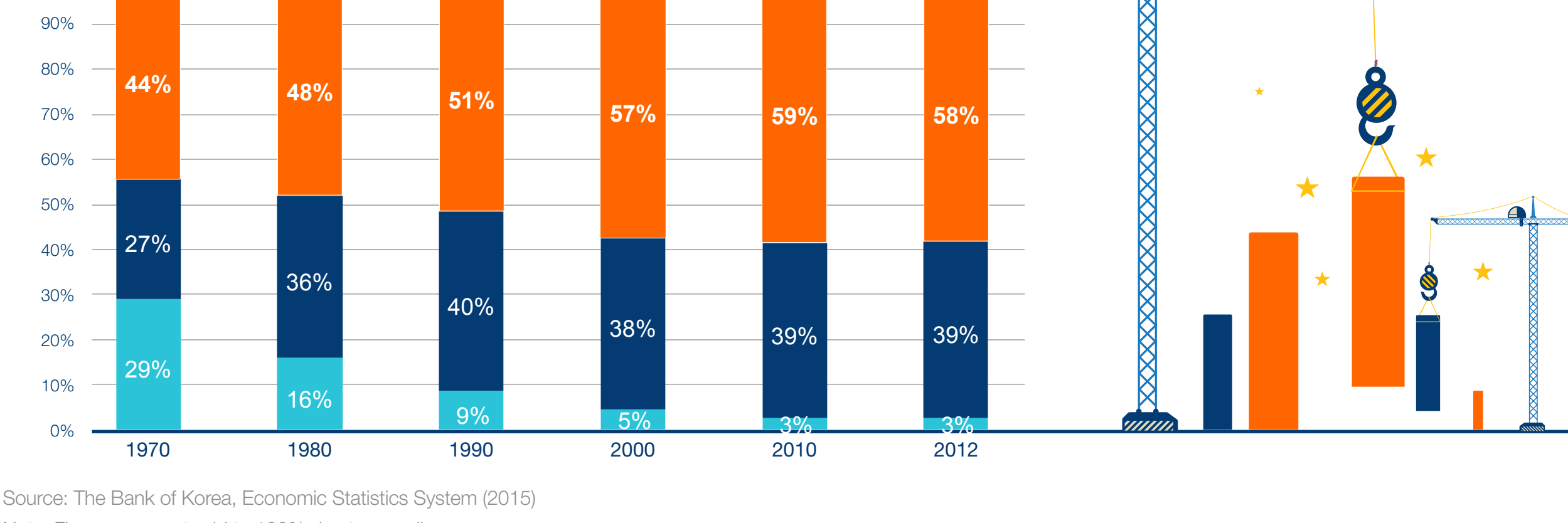


Source: Bloomberg, Mirae Asset Global Investments (2016)

### Structural Shift from Manufacturing to Innovation

- Korea has moved away from manufacturing, towards services, with industrial policies that paved the way for resilient leaders in the sectors of LCD/display, automobiles, semiconductors, and shipbuilding by the likes of Samsung, Hyundai, SK, LG, and Hanwha.
- Intense focus on indigenous capabilities in the way of education, research, and high tech development have yielded world-class results in the way of innovation (ranked no. 1 in the Bloomberg Innovation Index from 2014 to 2016).

### A Transformed Gross Domestic Product Composition



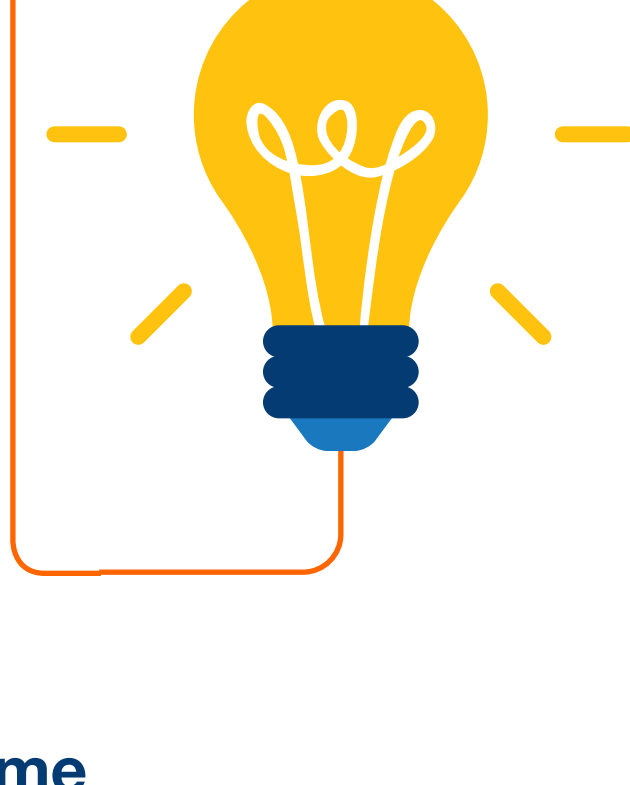
Source: The Bank of Korea, Economic Statistics System (2015)

Note: Figures may not add to 100% due to rounding

### Fostering an Indigenous Innovation Spirit

Rank	Economy	Total Score	R&D Intensity	Manufacturing Value-Added	Productivity	Hi-Tech Density	Tertiary Efficiency	Researcher Concentration	Patent Activity
1	South Korea	91.31	2	1	39	2	1	6	2
2	Germany	85.54	8	3	32	5	17	14	3
3	Sweden	85.21	5	16	16	9	16	5	8
4	Japan	85.07	3	13	29	5	34	9	1
5	Switzerland	84.96	7	8	3	10	25	13	5
6	Singapore	84.54	17	5	5	13	2	7	24
7	Finland	83.80	4	16	26	23	4	3	7
8	United States	82.84	10	26	8	1	37	21	4
9	Denmark	81.40	6	22	13	21	18	2	10
10	France	80.39	15	39	15	4	12	18	11
11	Israel	79.81	1	35	35	7	29	1	20
12	Russia	78.85	31	27	18	8	3	27	15
13	Austria	78.45	9	11	14	30	7	11	13
14	Norway	77.07	21	43	1	12	24	8	19
15	Ireland	76.67	24	7	12	25	6	24	22
16	Belgium	76.19	13	23	10	21	31	22	17
17	United Kingdom	74.92	22	44	30	11	9	20	14
18	Netherlands	74.90	18	28	24	15	41	16	9
19	Canada	73.44	23	40	19	17	22	12	26
20	Australia	73.42	14	47	2	16	21	15	32

Source: Bloomberg Innovation Index (2016)

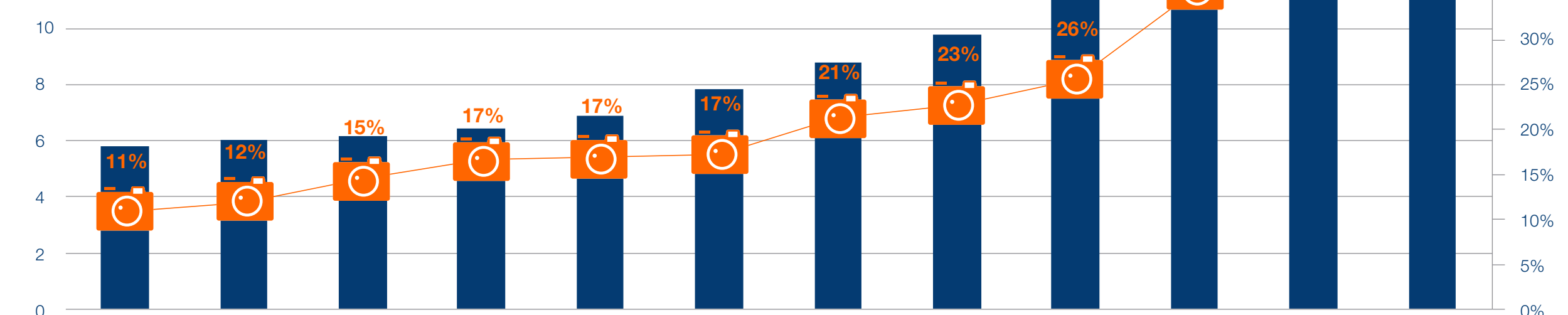


### Riding the Korean Wave High Yet Facing Challenges at Home

- Soft contents and the Korean wave are riding high on back of greater tourism levels to Korea, notably from China and Southeast Asia (Chinese spend 3x more on average than other tourists).
- On the other hand, Korea faces a shortfall in its labor force coupled to a heavier dependency ratio weighing on the country as the median age rises and fertility rates plummet to levels of nearly one-fifth what they were fifty years ago.

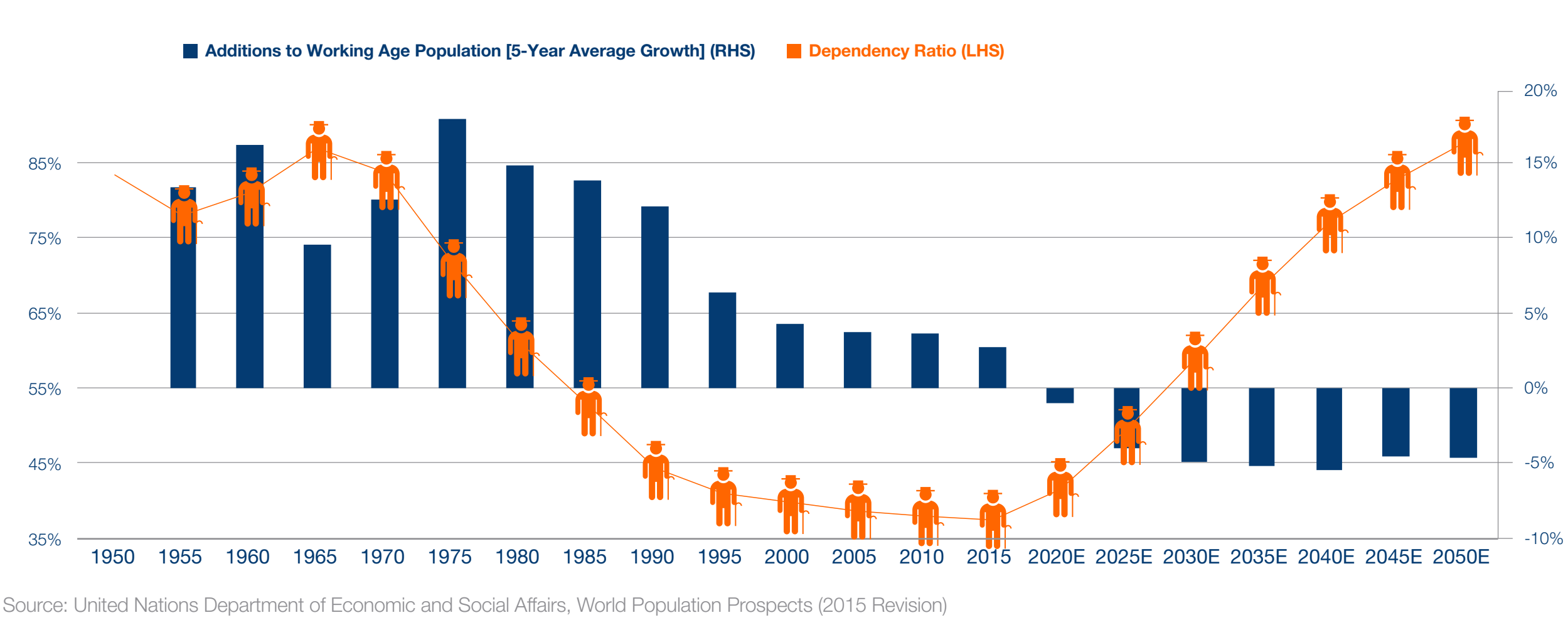
<sup>1</sup> CLSA, Korea Tourism Organization

### Korean Wave Leads to Leap in Chinese Tourists



Source: Korea Tourism Organization, Mirae Asset Global Investments (2016)

### Amid a Shrinking Labor Force and Greying Population

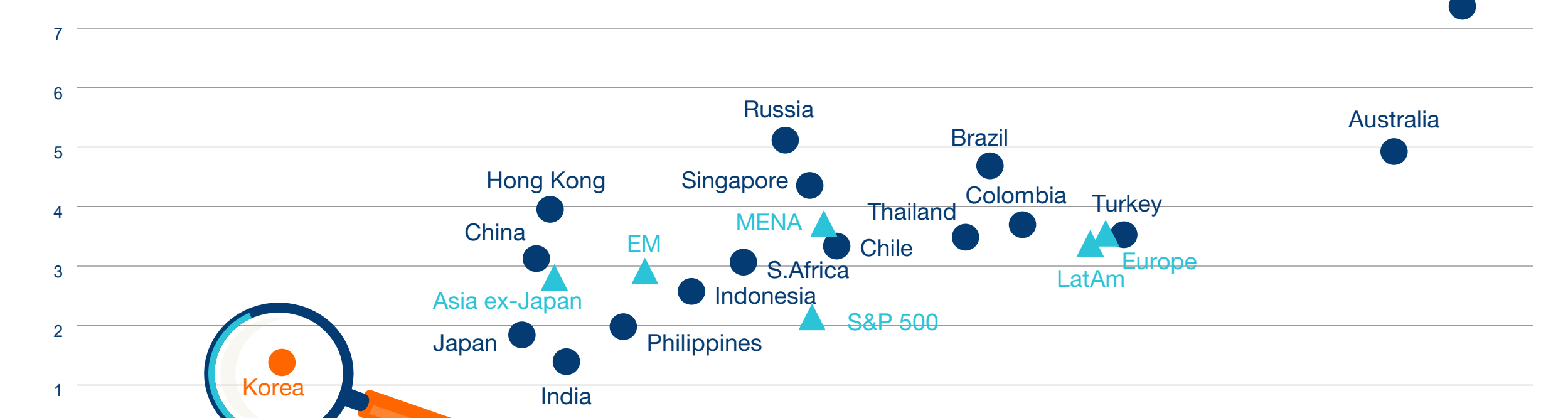


Source: United Nations Department of Economic and Social Affairs, World Population Prospects (2015 Revision)

### Country at a Crossroads

- Meanwhile, the country faces a high stakes leadership handover from the second to third generation of Chaebol families and thorny social and economic issues such as stagnating wages, higher unemployment, gender inequality, deflationary forces, elevated senior citizen poverty, and mounting household debt levels.
- Corporate governance issues are high on the agenda for all stakeholders, like those of higher dividends and eliminating conflicts of interest against shareholders, as Korea trails regional peers in Corporate Governance scores.

### “Korea Discount” of Paying Out Low Dividends

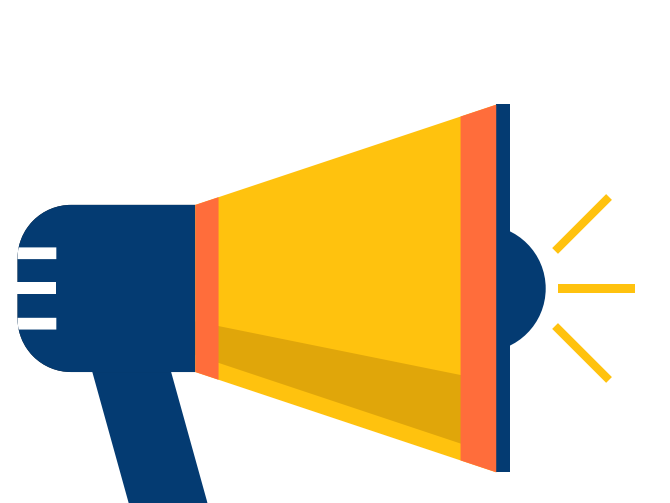


Source: Bloomberg, Mirae Asset Global Investments (December 2015)

### Korea Trails Regional Peers in Corporate Governance Scores

Rank	Country	Total	CG Rules & Practices	Enforcement	Political & Regulatory	IGAAP	CG Culture
1	Hong Kong	65	61	71	69	72	51
2	Singapore	64	63	56	64	85	54
3	Japan	60	48	62	61	72	55
4	Thailand	58	62	51	48	80	50
4	Malaysia	58	55	47	59	85	43
6	Taiwan	56	48	47	63	75	47
7	India	54	57	46	58	57	51
8	Korea	49	46	46	45	72	34
9	China	45	42	40	44	67	34
10	Philippines	40	40	18	42	65	33
10	Indonesia	39	34	24	44	62	32

Source: Asian Corporate Governance Association (2014)



### Security Umbrella and Geopolitical Entanglement

- Korea must strike a balance between a close economic interdependence with China and the traditional US alliance as typified by the American security umbrella, as geopolitics flare on the peninsula with North Korea.
- While the consensus is that reunification remains far off, the scenario analysis of pros and cons for such an event remain mixed, although they would surely exact an onerous short-term cost on South Korea's economy.

### Million Man Army and Manhattan Project in Pyongyang



Source: International Institute of Strategic Studies (Military January 2015), The Economist (2015), United States Geological Survey (January 2016), Mirae Asset Global Investments (2016)

### North vs. South Korea: Economy & Industry



Source: Bank of Korea, Statistics Korea, The Economist (2015), Mirae Asset Global Investments (2016)

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