

# **Korea Diligently Running With International Economic Policies Over the Past Six Decades**

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Over the last 60 years  
of the international economic  
Policy-making,  
**a remarkable performance,**  
**what we've done together ?**

# **Four Different Periods of Korea's International Economic Policies**

# The evolution of Korea's international economic policies over the four different periods

## Economic Upheaval and Reconstruction(1945~early 1960s)

- During 1945~1953, the Korean economy went through **severe dislocation and poverty**
- The Korean War destroyed about **42~44 percent of production facilities** in South Korea(Kim and Roemer, 1979)
- The **foreign aid played a crucial role** in the reconstruction
- The International economic policy
  - **As inward-oriented and import substitution industrialization**

## Government-led and export-oriented industrialization(1960s~1970s)

- In the first Five-Year Economic Development Plan(1962-66), Korea adopted the export-oriented growth strategy
- The incentive system for export promotion was initiated in the mid-1960s and maintained until early 1980s
- In the early 1970s, embarked on heavy chemical industry development strategy, Korea's trade policy temporarily reverted to import substitution policy
  - National security was an initial motivation to pursue HCI development strategy

# The evolution of Korea's international economic policies over the four different periods

## Expanding economic liberalization(1980s~1997)

- A New Policy Shift in the early 1980s
  - **“Comprehensive Market Liberalization”**
- Korea was determined to remove export support incentives and began to pursue Trade Liberalization
- Since the 1990s, Korea started opening service markets as well as foreign direct investment(FDI)
- In the Uruguay Round, Korea had reduced its tariff rates by 54 percent

## The globalization of the Korean economy (1998~present)

- Since the financial crisis of 1997, Korea enforced critical trade liberalization as well as reform of overall economic system
- In the late 1990s, Korea began pursuing its FTA policy, **turning away from the WTO** multilateralism-based trade liberalization
- Advancement of investment policy
- Korea is required to devise a scheme to maximize the effect of its ODA while also increasing the volume of it

# **Korea's Trade Policies Centered on Manufacturing Industries**

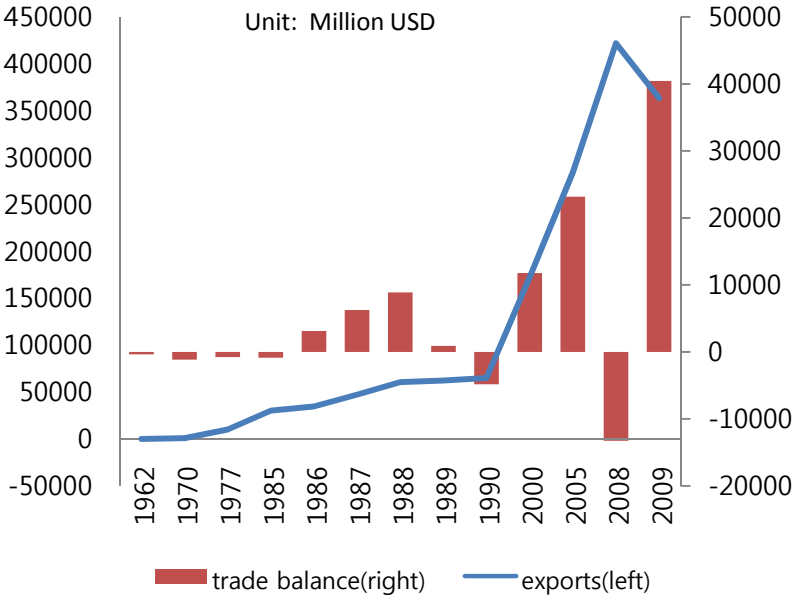
# Questions ?

- **What are Korea's trade policies and impacts of those on the Korea's economic miracle?**
  - Korea's trade policies were not consistently pursuing only a liberalizing direction
  - From the protectionist policies to extremely rapid liberalization policies, Korea's trade policies pointed to 'like a Department Store' covering all kinds of trade policies
  - Those policies taken by the Korean government proved a significant contribution to the Korea's remarkable economic performance over the years

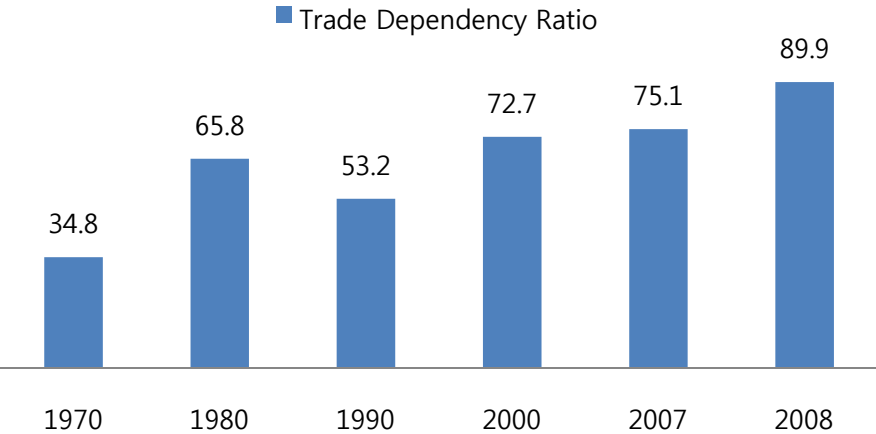
# Four Points to discuss

- Quantitative and Structural Changes in Trade
- Progress in Trade Policy
- Other Systems and Institutions, and the Exchange Rate
- GATT/WTO and FTA Policy

# Quantitative growth in trade



Source: KITA(each year)



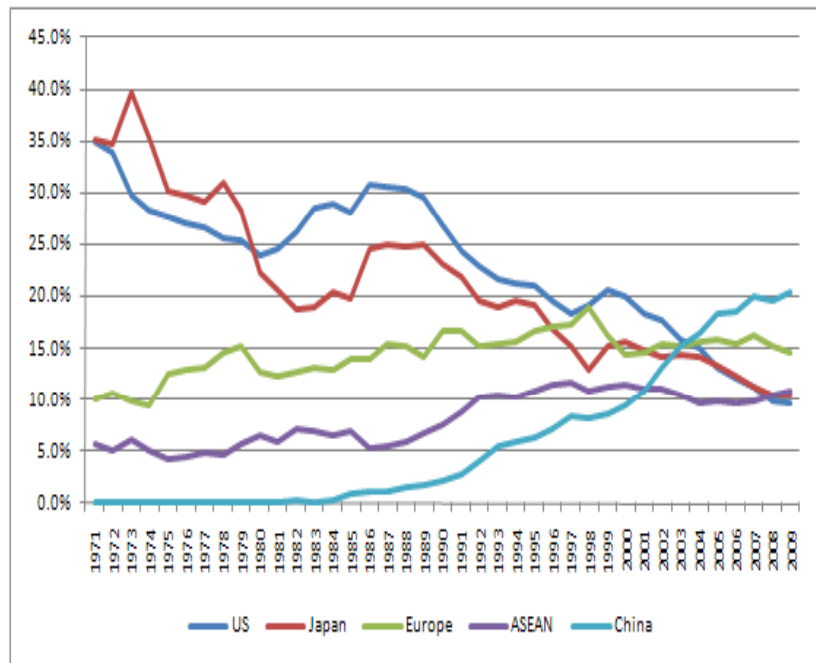
Source: KITA(each year)

- Before the 1960s, Korea’s trade volume was insignificant
- Since the export-driven policy from 1961
  - Trade volume increased rapidly
- Trade Balance
  - Korea experienced a problem of chronic trade deficits
- Korea’s Trade Dependency Ratio
  - Korea’s economic growth was driven by rapid trade growth

# Korea's Trade Structure Change

## Trade partner by country

- Trade dependence on the US and Japan **fell** over the time
  - In 1971, the US(49.8%) and Japan(24.5%); in 2008, the US(11%), Japan(6.7%)
- Trade partners became **more diverse** (China, Europe, ASEAN...)



Source: KITA

## Trade partner by region

- Exports **less** to advanced countries
- Exports **more** to developing countries; ASEAN; Europe; Middle Eastern Countries
- Exports **less** to North America
- ✓ Korean companies are relying more on international production and global outsourcing

<Share change in Korea's trade>

Share(%)	1971	2009
<b>Advanced</b>	<b>82.5</b>	<b>38.6</b>
<b>Developing</b>	<b>17.5</b>	<b>61.4</b>
Asia	32.7	52.5
<b>Japan</b>	<b>24.5</b>	<b>6.0</b>
<b>China</b>	<b>0.0</b>	<b>23.9</b>
ASEAN	2.8	11.3
Europe	8.2	15.4
North America	52.5	11.3
<b>US</b>	<b>49.8</b>	<b>10.4</b>
Middle East	0.9	6.6
Africa	2.5	2.3
others	0.0	0.0

Source: KITA

# Korea's Trade Structure Change

- Product Composition of Trade
  - 1960s : labor intensive industries(clothes, textile...)
  - 1970s : heavy chemical industries(steel, ship...)
  - 1980s : capital and technology intensive industries(semi-conductor, automobiles...)
  - But no marked change in import patterns

**<Trend in products composition of Korea's export>**

Share(%)	1962	1972	1980	1985	1990	1995	2000	2005	2009
Primary Industry Goods	72.3	11.1	7.7	5.2	5.0	4.9	2.8	1.5	2.6
Industrial products	27.7	88.9	92.3	94.8	95.0	95.1	97.2	98.5	97.4
-light	-	67.4	48.4	37.7	38.5	22.5	16.2	8.9	6.5
- heavy industrial	-	21.5	43.9	57.1	56.5	72.7	81.0	89.6	90.9

Source: KITA

# Progress in Trade Policies: Before the 1960s

- Economic, political and social constraint holding Korea back before the 1960s
  - High inflation around the time of the liberation from Japan
- In 1950s, the key policies for the Korean economy were
  - **The aid from the US and UN**
  - **Import substitution industrialization**
- The government focused on measures to reduce the trade deficits,
  - The policies helped protect domestic import-substitution industries, but also impeded exports
  - Korea needed to export more as Korea relied heavily its development on the aid and foreign investment
- The first Korea's Trade Law(Dec 1957) was introduced to put the framework of trade support system in place

# Progress in Trade Policies

## - Systemization of Export Support System(1960s~1970s)

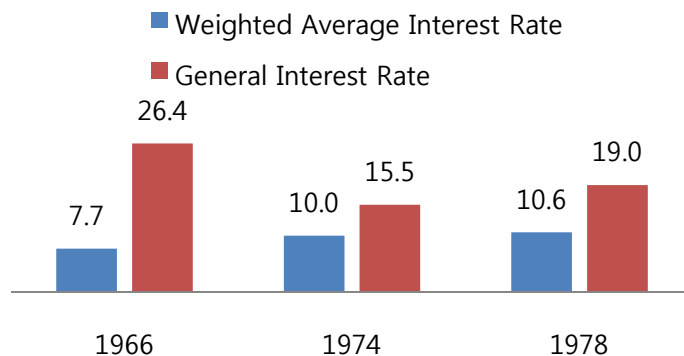
<Trend in export Support Financing>

Unit: KRW 1 billion

	1966	1974	1978
1.the size of short term export support financing	4.8	359.5	883.5
export financing	3.6	267.9	836.7
2. the size of long term export support financing	1.2	247	776.2
3. (2/(1+2)) : (Unit: %)	19.7	40.7	46.8
4. domestic credit	118.8	2,862.50	8,082.50
5. (1+2)/3 : (Unit: %)	5.1	21.2	20.5

Source: BOK, Nam(1980), p.47

<Comparison of Interest Rates>



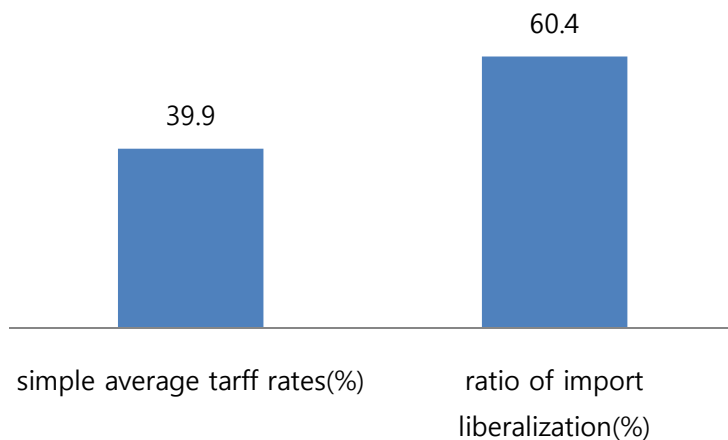
Source: BOK, Nam(1980), p.47

- **A big policy shift** in trade policy in the early 1960s
  - From import substitution to export promotion
  - in 1964: “the Comprehensive Export Promotion Plan”
- The plan included...
  - Tax, financial, administrative incentives, etc
- Yet, key policy changes in the plan included
  - reforms of the **exchange rate system**
  - **financial sector**
- Tax benefits for exports included...
  - reducing taxes on raw materials
- The ‘**Export Free Zone**’ in 1969 at the Masan Port Area in the South Sea

## Import Restrictions Policy(1960s~1970s)

- Despite the export promotion policy in 1960s, imports were strictly controlled
- High Average tariff(maintained in 1960s) and Special Tariff (1964~1973)

<1967 tariff rates and ratio of import liberalization>



Source: KITA

## Import Liberalization Policy(1980s)

- When the government's restrictive import policy faced inefficient protective structures of the domestic industry
  - **Strengthening the competitive market system in 1980s**
- The **'Import Liberalization Five Year Plan'** was carried out over the period 1983-1988

	1983	1988
simple average tariff rates(%)	23.7	18.1
ratio of import liberalization(%)	80.3	95.2

Source: KITA

- One notable feature was the **'Import Liberalization Notification System'**
  - To improve **the credibility of the government**
  - **Careful and strategic policy consideration and step-by- step approach**

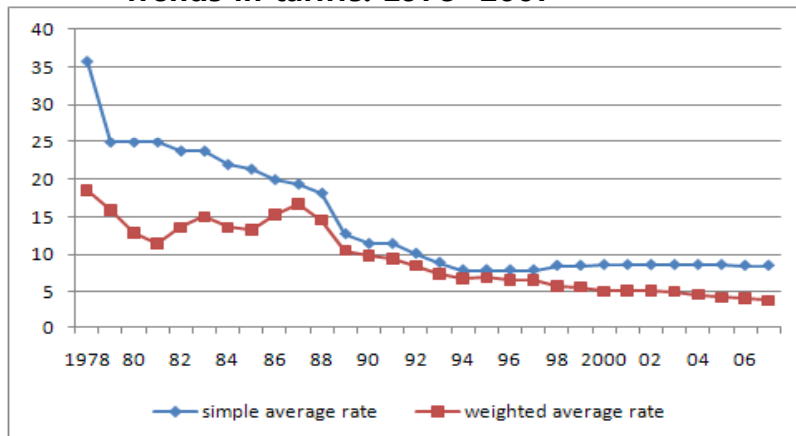
# Progress in Trade Policies towards the Positive Market Openness

- International trade system and reduction in tariffs

- ✓ Responding to trade conflicts: Late 70s ~ mid 90s : reducing tariff(since comprehensive liberalization)
- ✓ UR, DDA, and FTAs played an import role in reducing tariffs( Mid 90s ~ present)

- In 1995, the ratio of import liberalization : 99 percent
- Since Uruguay Round, Korea strengthened its policy stance of 'Openness'
- In 2000s, Korea stays **fully tuned** to the policy stance of '**Positive Market Openness**'

<Trends in tariffs: 1978~2007>



Source: KITA

change in concessions	before UR	after UR
concession ratio in manufacturing (%)	9.5	93.8
average concession tariff rate(%)	31.2	10.1

# Other trade support system

- **The Export Insurance System**

- Introduced in 1969 as part of the export promotion policy

- **KOTRA(Korea Trade-Investment Promotion Agency)**

- was established in 1962 as a national trade promotion organization
- facilitated rapid export-led economic development

- **KITA(Korea International Trade Association)**

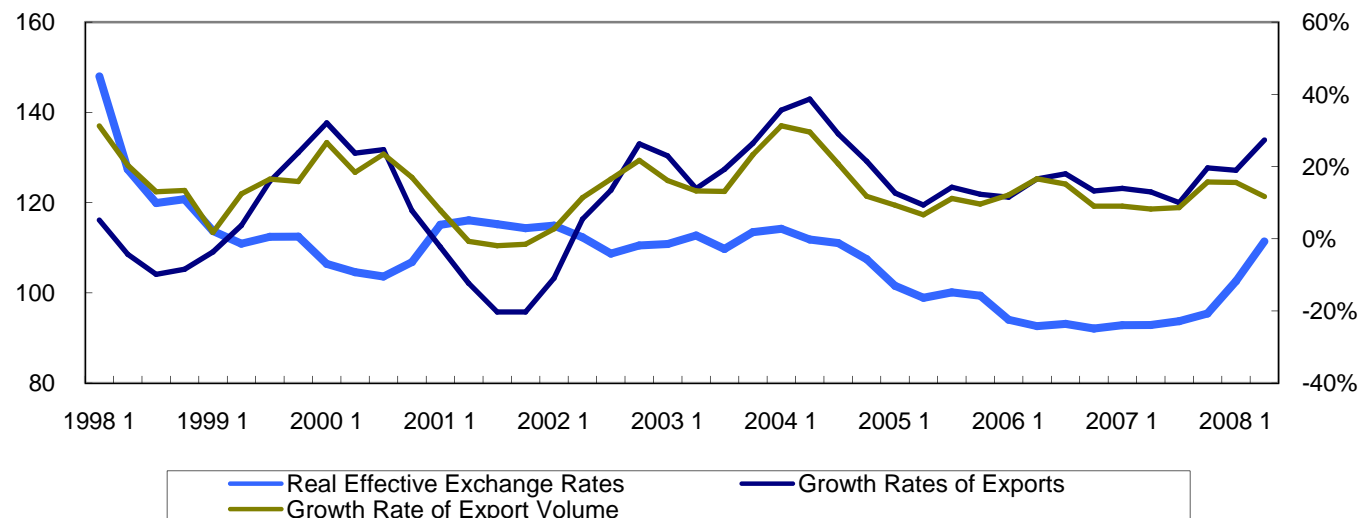
- founded in 1946 to represent the interests of Korea's international traders.
- Played a critical role in expanding overseas markets

- **Export-Import Bank of Korea**

- In 1976, was established to provide medium to long-term credit for exports and imports
- Facilitated economic cooperation with foreign countries and supported export loans and trade finance

# Exchange Rate and Trade

- Exports : a driving force in Korea's economic growth
  - The exchange rate was a significant variable in affecting exports
- The current account balance due to a change in exchange rate was determined by **'exchange rate elasticity of exports and imports'**
- Since December 1997, Korea adopted the free floating exchange rate system
  - Since 1997, **while real effective exchange rates** have continued to show a downward trend, Korea's exports by value or quantity have **rather maintained a high growth of about 20 percent**
  - **Since 1997, exchange rate elasticity of exports continued a downward trend**



Source: Chung(2008)

# Progress in Trade: GATT/WTO

## GATT/WTO

- Since UR, Korea's tariff reduction had been the highest among many countries except Japan
- Market opening strengthened Korea's competitiveness
- Korea gained huge benefit of the multilateral trade order
- Now, Korea plays an important role to promote the multilateral trade agreement such as DDA

## Korea's position on DDA's agenda

- **Agriculture**
- **Market Access for Non-Agricultural Product** : to support a Swiss formula, vertical approach for addressing NTBs
- **Service** : further liberalization of infrastructure service
- **Rules** : to prevent misuse and overuse of antidumping measures, and caution the disadvantage of prohibiting subsidies
- **TRIPS** : pragmatic approach
- **Trade and Environment** : to enhance the mutual supportiveness of trade and environment

# Progress in Trade Policies: FTA

- **Rationales of Korea's FTA strategy**

- To expedite the economic reforms and advance the economic system across the board
- To expand trade and investment
- To Increase the economic efficiency and the foreign credibility
- To pursue political stabilization in the peninsula
- To securing resources and expanding its foreign markets

- **Principles of Korea's FTA Strategy**

- Multi-track and simultaneous negotiations
- Comprehensive and high-level FTAs in terms of commitments
- Broadly supported FTAs in terms of procedural legitimacy

- **Current status of Korea's FTA**

<b>Concluded</b> ( 7 FTAs signed; 5 FTAs effectuated )	✓Chile (Effectuated in Apr . 2004) ✓Singapore (Effectuated in Mar. 2006) ✓EFTA (Effectuated in Sep.2006) ✓ASEAN (Goods trade :Effectuated June 2007, Service trade :Effectuated in May 2009, Investment:: Effectuated in Sept. 2009)
	✓The U.S. (concluded in Apr. 2007) ✓India (Effectuated in Jan.2010) ✓The EU (Concluded in July 2009)
<b>Under negotiation</b>	Canada (began in July 2005); Mexico (began in Feb. 2006); GCC (began in July 2008); Australia (began in June 2009); Peru (began in Mar. 2009); Colombia (began in Dec .2009); Japan (began in Dec .2003), interrupted in Nov. 2004)
<b>Under examination</b>	China (joint study); Korea-China-Japan (agreed to launch a joint study); Mercosur (joint study); Turkey (joint study finished); Russia (joint study); Israel (joint study); SACU (agreed to begin a joint study between private sectors)

# Commitment areas in FTAs Korea concluded

	Korea-Chile	Korea-Singapore	Korea-EFTA	Korea-ASEAN	Korea-India	Korea-US	Korea-EU
Tariff Elimination	○	○	○	○	○	○	○
Non Tariff Barriers				△	△	○	○
Elimination of Quantitative Restrictions	○	○	○	○		○	○
Safe guard	○	○	○	○	○	○	△
Anti-dumping and Countervailing Measure	○	○	○		○	△	○
Rule of Origin	○	○	○	○	○	○	○
Investment (establishment)	○	○	○	○	○	○	○
Customs Administration	○	○	○	○	○	○	○
Service	△	△	△	○	○	○	○
MRA	△	○	○	△		○	△
SPS	○	○	△	△		○	○
TBT		○	△	△		○	○
Government Procurement	○	○	△			○	○
Intellectual Property Rights	△	△	△	○	○	○	○
Competition Policy	○	△	△		○	○	○
Dispute Settlement	○	○	○	○	○	○	○
E-Commerce		○				○	○
Movement of Personnel	○	△			○		○
Environment						○	○
Labour						○	○

Note: ○ reflected, △ partly reflected or agreed on further discussion

## Concession rates and the rates of year zero in FTAs Korea concluded

FTA		Tariff Elimination	Total	Industrial Goods	Forest Goods	Marine Goods	Farm Goods
Korea-Chile	Korea	Concession	99.8	100	100	100	98.5
		Year0	87.2	99.9	58.2	69.5	15.6
	Chile	Concession	99	99.8	100	100	94.2
		Year0	41.8	30.6	100	99	92.9
Korea-Singapore	Korea	Concession	91.6	97.4	82.9	56.2	66.6
		Year0	59.7	68.8	53.7	13.8	16
	Singapore	Concession	100	100	100	100	100
		Year0	100	100	100	100	100
Korea-EFTA	Korea	Concession	99.1	100	100	88.4	84.2
		Year0	86.3	92.3	45.5	27.1	15.8
	EFTA	Concession	100	100	100	100	100
		Year0		100	100	100	35-55
Korea-ASEAN	Korea	Concession	99.2	100	100	100	94.1
		Year0	90.8	96.6	60.4	60.8	63.2
	ASEAN	Concession	99.2-100				
		Year0	89.9-100				
Korea-India	Korea	Concession	93.2			80.3	55.2
		Year0	88.6			10.3	7.7
	India	Concession	85.3			92.8	59.7
		Year0	71.5			0	2.1
Korea-US	Korea	Concession	99.8	100	100	100	99
		Year0	78.2	90.6	26.8	25.4	37.9
	US	Concession	100	100	100	100	100
		Year0	81.3	87.9	73	72.8	58.7
Korea-EU	Korea	Concession	99.6	99.5		93.7	97.2
		Year0	81.7	90.7		12.3	42.1
	EU	Concession	99.6	100		100	98.1
		Year0	94	97.3		40.8	91.8

Source: authors' calculation from each FTAs

# **Korea's Investment Policies**

## **Inward and Outward FDI**

# Inward Foreign Direct Investment : The Evolution of Policy

## ✓1<sup>st</sup> Step : Introduction Period(1960~1983)

- Foreign direct investment in Korea was allowed in 1962
- The Korean government depended on foreign loans rather than FDI in its development strategies

## ✓2<sup>nd</sup> Step : Liberalization Period(1984~1997)

- The Korean government changed its FDI policy from a positive list system to a negative list system In July 1984
- With Korea Joining the OECD, the government took further liberalization steps on FDI : to open up the service industry, to allow (friendly) M&A by foreign firms

## ✓3<sup>rd</sup> Step : Promotion Period(1998~ )

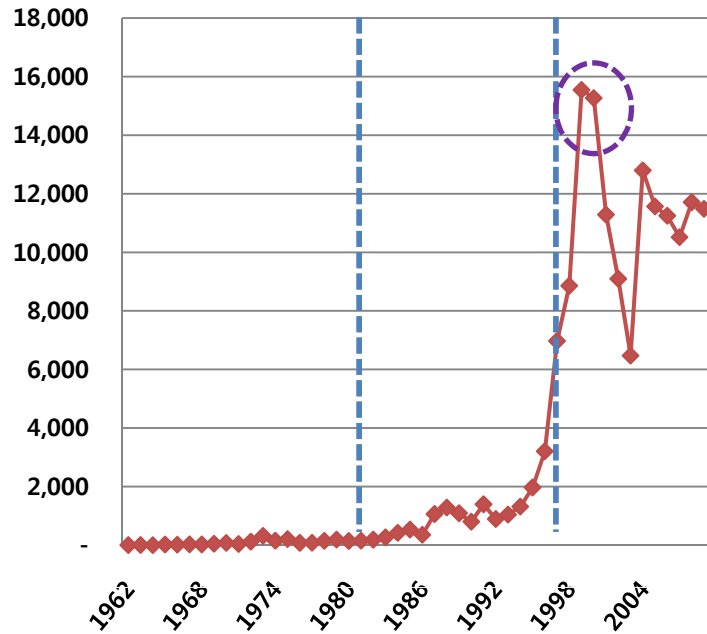
- After the foreign exchange crisis, the Korean Government promoted FDI by enacted "The Foreign Investment Promotion Act" in 1998
- Designated "Free Economic Zones (FEZs)" : Incheon, Pusan-Jinhae, and Kwangyang (2003), Hwang hae, Saemankeum-Kunsan and Daegu-Kyungbuk (2008)

# Inward Foreign Direct Investment

## : Trends in Inward FDI

- FDI into Korea was minimal until the mid-1990s, but it has increased dramatically since Korea joined the OECD
- Based on accumulation, by country, **the U.S. is the largest foreign investor in Korea**, followed by Japan, Netherlands, Germany and U.K.

<Inward FDI (Unit :Million \$)>



Source: Ministry of Knowledge Economy

<FDI trends among 10 largest foreign investors>

(Unit : Billion won, %)

	1970	1980	1990	2000	2005	2008	'62~'08 Total
Total	76	143	803	15,265	11,566	11,705	149,013
U.S.	45 (59.5)	71 (49.3)	318 (39.6)	2,921 (19.1)	2,690 (23.3)	1,328 (11.3)	40,327 (27.1)
Japan	21 (28.1)	43 (29.7)	236 (29.3)	2,452 (16.1)	1,881 (16.3)	1,423 (12.2)	21,952 (14.7)
Netherland	1 (1.2)	2 (1.3)	36 (4.5)	1,775 (11.6)	1,150 (9.9)	1,224 (10.5)	16,979 (11.4)
Germany	1 (1.6)	9 (6.0)	62 (7.8)	1,627 (10.7)	705 (6.1)	685 (5.9)	8,404 (5.6)
U.K.	0 (0.1)	2 (1.6)	45 (5.6)	86 (0.6)	2,308 (20.0)	1,231 (10.5)	8,052 (5.4)
Malaysia	-	-	-	1,408 (9.2)	211 (1.8)	53 (0.5)	6,961 (4.7)
France	-	-	22 (2.8)	616 (4.0)	85 (0.7)	538 (4.6)	5,697 (3.8)
Singapore	-	-	14 (1.7)	297 (1.9)	389 (3.4)	916 (7.8)	5,479 (3.7)

Source: Ministry of Knowledge Economy

# Inward Foreign Direct Investment

## : Economic Effects of FDI

- FDI also had a crucial role in building up **foreign exchange reserves** in the aftermath of the 1997 crisis
- FDI proved to **increase production** in Korea
  - From 1999 to 2006, the percentage of output by foreign-invested companies out of total output rose from 8.1% to 13.4% in manufacturing and from 4.1% to 9.9% in services

### <Contribution by Foreign-invested Companies in Manufacturing Production>

(Unit : Billion won, %)

		1999	2000	2001	2002	2003	2004	2005	2006
Output	Total	464,790	533,373	536,165	606,461	654,268	761,576	827,721	884,306
	Foreign Invested Companies	37,648	62,938	64,876	69,743	80,475	95,197	106,776	118,497
	Ratio	8.1	11.8	12.1	11.5	12.3	12.5	12.9	13.4

### <Contribution by Foreign-invested Companies in Services Production>

(Unit : Billion won, %)

		1999	2000	2001	2002	2003	2004	2005	2006
Output	Total	339,585	378,709	379,675	450,613	407,738	426,239	512,237	547,758
	Foreign Invested Companies	13,923	20,829	31,513	36,049	43,628	49,443	54,809	54,228
	Ratio	4.1	5.5	8.3	8.0	10.7	11.6	10.7	9.9

Source: Ministry of Knowledge Economy

# Outward Direct Investment : The Evolution of Policy

## ✓1<sup>st</sup> Step: Introduction Period(1968~1974)

- Outward FDI discouraged

## ✓2<sup>nd</sup> Step: Development Period(1975~1979)

- Limited Permission

## ✓3<sup>rd</sup> Step: Encouragement Period(1980~1985)

- Prior permission abolished

## ✓4<sup>th</sup> Step: Boost Period(1986~1993)

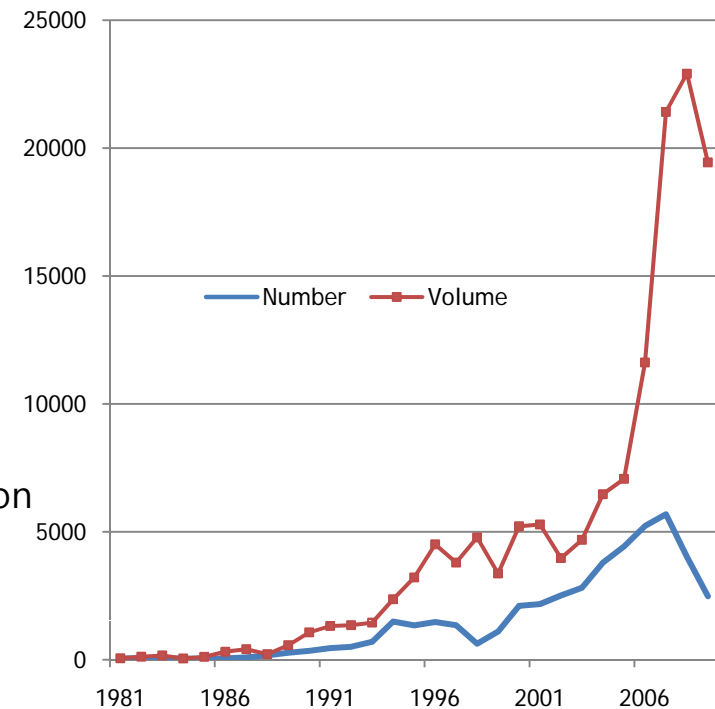
- From 1986, switching from restrictions to the liberalization of capital outflows

## ✓5<sup>th</sup> Step: Liberalization Period(1994~ )

- Following further liberalization measures since 1994, overseas direct investment has grown rapidly

## <Korean Outward Direct Investment>

(Unit: USD million, number)



Source: Korea Export-Import Bank

# Outward Direct Investment

## : Trends in Outward Direct Investment

- **The number of foreign subsidiaries** established by Korean firms increased dramatically since 2005, reaching 21.7 billion dollars in 2008
- **Korean multinational enterprises have been the main drivers** of investments overseas, including cross-border M&As
- **Asia has attracted 56 billion dollars, which represents 48% of total investments** from Korea between 1968 and 2008, compared with 23% for North America and 15% for Europe

### <Korean Outward Direct Investment by Region>

	Amount of Investment (USD million) , %					1968-2008
	1981	1990	2000	2005	2008	
Total	57	1,069	5,282	6,954	21,808	116,324
Asia	5.5 (9.6)	366.2 (34.2)	1,646 (32.0)	4,139 (60.0)	10,809 (50.0)	55,969 (48.0)
Middle East Asia	3.4 (6.0)	40.3 (3.7)	31 (1.0)	43 (1.0)	179 (1.0)	1441 (1.0)
North America	33.451 (58.7)	454.8 (42.5)	1,463 (28.0)	1,293 (19.0)	5,097 (23.0)	27,012 (23.0)
Latin America	1.0 (1.7)	66.8 (6.2)	1,506 (29.0)	542 (8.0)	1,617 (7.0)	9,424 (8.0)
Europe	1.5 (2.6)	81.9 (7.6)	292 (6.0)	654 (9.0)	2,988 (14.0)	18,023 (15.0)
Africa	0.9 (1.6)	26.5 (2.4)	156 (3.0)	129 (2)	292 (1)	1,688 (1)
Oceania	11.3 (19.7)	32.4 (3.0)	90 (2.0)	154 (2.0)	730 (3.0)	2,766 (2.0)

Source: Korea Export-Import Bank

# **Assessment and Challenges**

# We conclude the policies are ‘successful, and effective to growth

## Export-Oriented Development Strategy

- **Export-oriented growth strategy was a main factor of Korea’s **successful** economic development.**
  - Korea, Singapore, and Malaysia recorded annual growth rates of 6.4-8.0% during 1965-2006.
- **Korea’s export-oriented economic policy **was effectively combined** with import restriction policy and government intervention**

## Comprehensive Liberalization Policy

- **Gradual market liberalization and **clear market signaling** were keys**
- **Investment Liberalization **has to continue****
  - Korea stays **relatively closed towards** inward foreign investment.
    - As of 2009, Korea ranked 52<sup>nd</sup> in the share of FDI stock in GDP(0.18%) among 55 major countries(IMDB).
  - **Korea should continue to make its domestic market more investment-friendly**

# We believe we need to address the challenges ahead to move forward

## Investment-DDA-FTA-National Consensus Building

- **The agenda for future trade policy is closely related to whether Korea can make its domestic market investment-friendly.**
- **To strongly pursue DDA negotiations**
- **To continue FTAs and to do it with whom**
- **To build an effective internal negotiation mechanism and national consensus**

## Market opening-Reform-Safety net-the G20

- **To continue efforts for market opening**
  - More liberalization in agricultural and service industries
- **To expedite reform of the domestic economy**
  - Improve systems of fair competition
- **As the liberalization policy moved forward, safety net building became important issues.**
- **To successfully hold the G20 meeting, held in Korea in November 2010**
  - to demonstrate its commitment to stable recovery of global economy as well as sustaining global trade liberalization.

Thank you very much

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