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A New Perspective
on U.S.–Korea Economic Relations

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A New Perspective on U.S.–Korea Economic Relations

The Honorable Chang-yuel Lim

I would first like to thank The Heritage Foundation for its kind invitation to speak today. It is always a pleasure for me to visit Washington, where I spent five very enjoyable years in the mid-1980s working for the International Monetary Fund and the World Bank.

In those days, there was widespread speculation that the United States was losing its competitive edge, so I must say that it is quite encouraging to find the U.S. economy today continuing the longest expansion in its history.

The U.S. economy recorded an exploding growth rate of 5.6 percent during the first quarter of this year. For a mature economy like that of the United States, it surely is an extraordinary achievement. Moreover, an unemployment rate of 4.9 percent, the lowest since 1973, together with an inflation rate of a mere 3.0 percent at present, suggests that the future is even more promising.

With the economic worries currently facing us in Korea, I can assure you that this offers great encouragement for us.

This is my first opportunity to address a meeting at The Heritage Foundation, and I have been greatly looking forward to it. My remarks this afternoon will address three broad topics: the current situation of the Korean economy, Korea's trade and economic policies, and the U.S.–Korean economic relationship.

Korea's Economic Situation

Why, you may ask, should it matter very much to an American audience what state the Korean economy happens to be in? Twenty years ago, a strong South Korean economy was important to the United States as a capitalist showcase and as an anti-communist bulwark. But today, and for many years to come, the Korean economy is important to Americans as a market for U.S. goods, services, and capital. I imagine that very few Americans realize that Korea is the fifth-largest market for U.S. exports—larger than France or Italy—and the fourth-largest market for U.S. agricultural products.

During the past year alone, U.S. exports to Korea and Korean investment in the United States created tens of thousands of American jobs and \$33 billion in sales for U.S. companies. American banks, stockbrokers, and insurance companies operating in Korea enjoy growing business opportunities and profits.

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Investment, moreover, is no longer a one-way street in which capital flows west across the Pacific. Now Korean companies increasingly are taking a stake in the U.S. economy. Just recently, for example, Hyundai Electronics and Samsung Electronics began construction of semiconductor plants in Oregon and Texas, respectively. Their investment stake in these projects eventually will total \$2.6 billion.

For these reasons, the state of the Korean economy should be a matter of considerable interest to Americans, particularly American businessmen and policymakers.

Basically, there are two schools of thought regarding the current state of the Korean economy: the optimists and the pessimists. The optimists believe that the fundamentals of the Korean economy are sound, and that the current economic difficulties are merely cyclical and thus manageable. The pessimists, however, attribute our current problems to fundamental structural weaknesses in the Korean economy rather than to business cycle reasons. Let me now present some essential facts and statistics that we need in order to put this argument into perspective.

Last year, Korea's gross domestic product (GDP) growth fell to 7.1 percent, and this year it could reach as low as 5 percent. By the standards of most countries, these would be considered fairly healthy growth rates. Yet from our perspective, it is a "recession," as we are accustomed to annual growth rates of almost 8 percent over the last three decades. We Koreans are concerned that these reduced growth rates will complicate our efforts to expand the full benefits of development to all our citizens. And the concern is even more severe because the current slowdown is leading to unemployment, which has risen to 3.4 percent currently from 2 percent last year. In a country like ours, with limited social welfare schemes, this is a matter of serious worry.

Most worrisome of all is Korea's current account deficit, which reached \$24 billion last year, or about 4.8 percent of GDP. This was our worst ever, and more than double the estimate made at the start of the year. I understand that U.S. policymakers are concerned about the U.S. current account deficit as well, which was 2.3 percent of GDP last year. But the GDP value of Korea's deficit was more than twice that ratio, so I hope Americans will appreciate our dilemma.

This deficit has helped boost foreign debt to \$105 billion, or approximately \$2,000 per capita. Some Koreans who recall the severe foreign debt crunch of the early 1980s, when the average per capita debt was \$1,000, feel there is particular cause for concern. As demonstrated in the case of other countries, a heavy debt burden can seriously threaten long-term sustainable development.

The combination of these indicators has led the general public, as well as the Korean business sector, to regard the situation as a crisis. In response, some private organizations have called on the general public to moderate its consumer behavior. This so-called frugality campaign has caused some concern among our trade partners.

It is important to me, during this visit, to try to provide some context for this "frugality campaign." Fundamentally, Koreans increasingly understand that the country's current consumption patterns should be rationalized. There is growing awareness, for example, about the massive increases in our consumption of energy and our general lack of energy efficiency. Since we produce no basic energy resources, this situation is creating a serious drain on our competitiveness. Our energy imports increased more than twofold between 1990 and 1996, and

our energy consumption is 1.8 times as large as that of Japan in producing one unit of manufactured goods. We also are seeing declining use of public transportation, the use of more and bigger personal cars, an enormous wastage of food, and a lack of effective recycling.

Faced with this situation of skewed consumption patterns, and confronted with a stressful economic period, the Korean people are drawing on a cultural tradition of what, in this country, is called “belt tightening.” A more rational pattern of consumption is in the long-term interest of Korea’s economic health, and thus in the interest of the United States and others in the international community.

So I hope that our American friends can take a broad view of what the Korean people are trying to achieve. For my part, I want to assure you that the Korean government is committed to ensuring that this campaign is not intended as discriminatory behavior, or in any way to discourage the competition which is so central to our future economic success.

Korea’s Trade and Economic Policies

A new team of economic ministers, including myself, was appointed to office in March of this year. You might be curious about the economic management philosophy of the new economic team. If I may summarize, that philosophy is reliance on the principles of market economy which stress minimum government intervention and promotion of competition domestically as well as internationally. We believe that this policy direction offers the best prospects for ensuring the Korean economy’s long-term competitiveness.

First, we are placing top priority on improving the current account over achieving a high growth rate. The Korean government pursues macroeconomic policies in such a way as to stabilize consumer prices and encourage national savings through the stable management of aggregate demand. The government has decided to reduce fiscal spending by \$2.5 billion this year and has frozen salaries for senior government officials. These policies will affect domestic production and imports alike.

This, for me, is a critical point about our current economic policy direction. The government has no intention either of taking discriminatory measures to restrain imports or of providing protection to domestic firms losing competitiveness. We understand clearly that the long-term solution to the deficit problem lies in increased international competitiveness for Korean industry. Therefore, we will assist—with the help of domestic and foreign investment—in creating dynamic, competitive new industries on which to build the future of our economy.

Second, we will maintain and even accelerate the pace of trade liberalization. As you doubtless know, Korea is the newest member of the Organization for Economic Cooperation and Development (OECD). As such, we will make a concerted effort with our fellow OECD members to promote free trade policies comparable to those of other member countries.

Third, we will continue strengthening the market mechanism through deregulation and reform of financial markets. Indeed, I believe that deregulation is the key to revitalizing the nation’s economy. By lifting the administrative burden from the private sector, deregulation helps business to cut costs, rationalize production, and streamline management structures.

The financial sector is proving to be the toughest nut to crack in our deregulation drive, but reform in this area should receive a major boost from the work of the Presidential Commission on Financial Reform, appointed in January. The Commission is set to issue its final report in the

second half of this year. This report will supply the blueprint for the next phase of financial reform and deregulation. It is expected that some of the key recommendations will address the need for greater transparency of financial supervision and more flexible rules on mergers and acquisitions.

We also are doing more to meet the concerns faced by foreign investors in Korea. For example, foreign investors are now permitted to finance not only fixed investment, but also operating funds at interest rates applied in international financial markets. In another incentive, we are providing low-rent or no-rent arrangements for high-tech foreign firms at national industrial parks.

In addition, we are working to address the interest of both domestic Korean companies and foreign investors in a stable and flexible labor market. While the process of developing the new law clearly involved some rough spots late last year, we are confident that we have achieved a final version which meets the concerns of all parties and will place the flexibility of the Korean labor market on par with that of labor markets in the United States and West European countries. As a result of our new labor law, we already have seen a significant decline in labor disputes and much better cooperation between unions and management.

We are especially pleased that foreign investors—above all, Americans—seem to be getting the message. Last year, U.S. companies increased their investment stake in Korea by 35.8 percent. In the first quarter of this year, U.S. investment was up nearly 800 percent over the same period of 1996, reaching \$838 million.

The U.S.–Korea Economic Partnership

This leads me directly to my next topic: namely, the status and future of the U.S.–Korea economic partnership.

During the latter half of the 1980s, the United States recorded annual deficits in its trade with Korea, reversing the trend of previous decades. Korea took assertive action that helped to correct the imbalance by, among other measures, appreciating the Korean won by 24.3 percent between 1985 and 1990, liberalizing its import market, and dispatching buying missions to the United States.

But now, as we all know, Korea suffers a trade deficit with the United States of \$11.6 billion. This figure is bigger than Korea's largest trade surplus with the United States—\$9.6 billion, recorded in 1987—and accounts for more than half of Korea's total trade deficit.

During my visit here, I hope to convince U.S. policymakers that, just as Korea acted to address U.S. deficit concerns several years ago, it is now in the long-term interest of the United States to help Korea reduce its own deficit to a more manageable level.

I also hope to discuss with my counterparts that some current U.S. trade policies do not appear to be fully in keeping with the multilateral trade regime. On this point, I must note with regret, for example, that the U.S. government has yet to decide whether to revoke antidumping measures against Korean color TVs and DRAMs. In the case of color TVs, the antidumping order has been in place since 1984, but the order remains in place even though no Korean color TVs have been exported to the United States since 1991. The Korean government also takes the view that, as has been the case in the past, the three consecutive *de minimis* dumping

determinations on Korea's DRAMs should result in revocation of the case when the third and final determination is issued in July.

We also have concerns about recent developments in exchange and financial markets. For example, the exchange rate between the U.S. dollar and the Japanese yen has especially large implications for Korea's trade position. The yen has depreciated against the dollar by 30 percent since mid-1995 despite the significant level of U.S. deficit with Japan, while the Korean won has depreciated against the dollar by 15 percent for the same period. Since 60 percent of Korean products compete head-to-head with Japanese products, the relative advantage conveyed by the yen's value has a major, if indirect, negative impact on Korea's price competitiveness in the U.S. market.

At the recent meeting, the G-7 finance ministers and central bank governors agreed that "exchange rates should reflect economic fundamentals—and significant deviation from fundamentals are undesirable." They therefore will "monitor developments and cooperate as appropriate in exchange markets." We appreciate the renewed attention to this issue and hope that the United States will continue to play a leading role in making some significant corrections.

I believe firmly that a more balanced trade expansion is essential to the long-term health of our bilateral relationship. As the United States is our major trading partner, we hope that American businessmen and policymakers will share our concern about the bilateral trade imbalance.

I speak frankly about these matters because I believe that mutual trust is the foundation of economic cooperation. That is why I have come here to the United States on my first overseas visit since my appointment as trade minister two months ago.

Given the huge trade volume between the United States and Korea, it is hardly surprising that trade disputes sometimes will occur. What is most important is how to resolve them. We believe that the best way to do so is through low-profile consultations, rather than highly publicized confrontations. During my time here, I look forward to solidifying relationships with my U.S. counterparts that will help both of us approach trade relations in this constructive way.

Trade will continue to be the linchpin joining our two economies, but I believe that one of the fastest growing areas of the future will be industrial cooperation. In this regard, let me note that our new industrial policy emphasizes development of venture businesses and high-tech industry. I understand that the United States successfully promoted high-tech venture business in the 1980s and 1990s. Korea is endowed with well-trained manpower, and various programs are being prepared to assist the start-up and growth of such companies. Some of these offer special incentives for foreign participation. This would seem an especially promising area for technical and financial tie-ups between U.S. and Korean venture companies in the years ahead.

In broader terms, the U.S. and Korean economies are particularly well matched. Korea's major industrial asset is its powerful manufacturing base, whereas the greatest industrial strength of the United States is its high technology. This combination makes for a natural and highly profitable economic partnership.

In order to accelerate the pace of industrial cooperation, our two governments agreed to establish a mixed public and private-sector Committee on Business Cooperation (CBC). This committee, which will be launched in the second half of this year, will coordinate and assist the efforts of bilateral private-sector bodies that already have been set up within specific industries.

If properly implemented, it will, I believe, provide powerful momentum for expanded industrial cooperation between the United States and Korea.

The United States and Korea work together as partners not only bilaterally, but also in regional and multilateral economic forums such as the World Trade Organization, the Asia-Pacific Economic Cooperation (APEC) forum, and, since last October, the OECD. For Korea, this constitutes a change from just a decade ago, when we tended to be rather passive with regard to such international bodies. Today, however, we recognize the necessity of playing a productive role in global economic affairs commensurate with the size and status of our economy. It is in the mutual interest of both our countries to help strengthen the multilateral institutional framework.

A recent example of Korea-U.S. cooperation at the multilateral level is the Information Technology Agreement (ITA) initiated by the United States. Korea moved quickly to back this proposal, both ratifying the ITA and joining the World Semiconductor Council. Last month, under the terms of the Agreement, we reduced our tariff rate on semiconductors from 8 percent to 4 percent.

At the regional level, the United States and Korea both recognize the enormous importance of Asia-Pacific economic cooperation to the future of their economies. Accordingly, we have worked together closely in APEC to reduce barriers to intra-regional trade and investment.

Over the long term, the strength of the relationship will depend on what private-sector businesspeople make of it. The government will do all it can to remove obstacles and provide incentives, but it can never supply the energy and impetus that drive a successful economy. That can come only from businesses operating in a free market environment.

In closing, let me say that I am especially grateful for this opportunity to share my thoughts with this distinguished audience. My goal is to ensure that the excellent cooperation that exists between the United States and Korea in the sphere of security affairs also will affect every aspect of our economic relations.

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