SAIS | US-KOREA 2010 YEARBOOK

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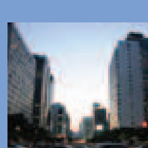

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INTRODUCTION

By Jae-Jung Suh
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Korea had many challenges in 2010, ranging from the global financial crisis to Iran's nuclear program to North Korean refugees in the South. UN Security Council Resolution 1929 against Iran, for example, posed to Seoul the challenge of striking the right balance between its economic interests and the security imperatives of nonproliferation. The global financial crisis, which began in 2008, continued to pose challenges to Korea's economy as it sought to contain negative consequences while looking for opportunities to maintain a healthy rate of growth. On the Korean peninsula, the *Cheonan*'s sinking and the shelling of Yeonpyeong Island not only increased the already high tension between the two Koreas, but also created a new set of diplomatic challenges for South Korea's relations with China and the United States. Furthermore, Seoul faced the internal challenges of *inter alia* working with over 20,000 North Korean refugees, helping them settle in a different society to which they were not accustomed.

These challenges did not present only difficulties, however. They also created opportunities for innovative responses that would shape Korea in unexpected ways. When Seoul chose to implement the UN resolution on Iran, it came up with a carefully calibrated set of measures that would convey Seoul's seriousness without unduly sacrificing business interests. The lessons the Korean government and businesses learned from the 1997 Asian Financial Crisis added to the intellectual, as well as economic capacity to absorb the difficulties created by the global financial crisis 10 years later. Korea's economic growth landed it a seat on the OECD's Development Assistance Council, providing Korea with fresh prospects to explore how Official Development Assistance might lead to mutually beneficial relationships between Korea as a new donor nation and recipient nations in Africa and other regions. Furthermore, Korea's rising stature brings with it the potential to enter new industries—such as the lucrative medical tourism industry—and the need to promote the nation in a new light.

The 2010 Edition of the SAIS U.S.-Korea Yearbook samples some of these important challenges and opportunities that Korea faced that year, and analyzes how each were handled. While there is no doubt that people will render divergent evaluations of Korea's responses, it is equally doubtless that Korea has emerged a different country as a result of its efforts to rise to the challenges and exploit these new opportunities. Our authors chronicle an important chapter in Korea's evolution in the following pages, which I hope all will appreciate.

YEARBOOK OVERVIEW

The 2010 Edition of the SAIS U.S.-Korea Yearbook is split into four chapters: Security and Alliance Politics, Trade and Development, Government and Business, and Identity and Society. The following provides an overview of the various issues covered in each chapter.

CHAPTER I: SECURITY AND ALLIANCE POLITICS

The Incredible Shrinking Crisis: The Sinking of the Cheonan *and Sino-Korean Relations*, by Jeremy Chan

When the South Korean naval ship *Cheonan* sank on March 26, 2010, under much speculation over a North Korean torpedo attack, so too did the hopes of many South Koreans for President Lee Myung-bak's policy of strategic "neglect" toward Pyongyang, not to mention aspirations for peace on the Korean Peninsula. Yet less than one year later, just as relations between the two Koreas appeared to be taking a turn for the better, North Korean artillery shells began falling on Yeonpyeong Island on November 23, 2010. This attack sent inter-Korean relations back into a crisis stage. As the first such attack on South Korean territory since the end of the Korean War in 1953, the Yeonpyeong Island shelling provoked outrage among a Korean populace that was noticeably ambivalent in the aftermath of the *Cheonan* sinking. As the denouement of the *Cheonan* incident made clear, however, it would be naïve to assume that much has changed on the Korean peninsula as a result of these two attacks. This is not the case, however, for relations between Seoul and Beijing, which remained amicable after the *Cheonan* sinking, but have since soured over the Yeonpyeong Island shelling. In particular, the two attacks have illuminated three emerging trends on the Korean peninsula: China's role as the ultimate arbiter for future crises between the two Koreas; Beijing's ongoing prioritization of its strategic interests above its economic ones; and South Korea's continued strategic vulnerability *vis-à-vis* North Korea as a result of its policy of deference over deterrence.

Realism and Liberalism in Economic Sanctions: An Analysis of South Korea's Sanctions on Iran in 2010, by Soo Kook Kim

After the United Nations Security Council (UNSC) adopted UNSC Resolution 1929 in June 2010 against Iranian support of terrorist groups, the United States individually asked South Korea to cooperate in sanctioning Iran. At the demand of the United States, South Korea announced a new set of sanctions on Iran in September 2010, which caused economic troubles in Korea. This paper fundamentally questions why South Korea put sanctions on Iran and whether or not it was a successful course of action. Does South Korea show liberalism by pursuing the virtue of peace and alliance instead of materialistic gains? Or is Seoul's decision a realistic outcome from a close cost-benefit calculation? In order to answer those questions, the paper will first scrutinize the measures of South Korean sanctions on Iran, examine their bitter impacts on South Korean economy, and lay out South Korea's quandary regarding consistency with nonproliferation, the U.S.-ROK alliance, possible economic retaliation from Iran, and U.S.-led economic retaliation. Finally, it will conclude that South Korea's sanctions on Iran were a successful approach to apply liberalism based on realistic calculations.

***The Lightbulb or the Bomb? The Politics of Spent Nuclear Fuel in South Korea*, by Jeannette Lee**

The importance of nuclear power plants is growing apace in South Korea and the Lee Myung-bak government is eager to expand its study of cutting-edge nuclear technologies tied to electricity generation. The United States, which works closely with South Korea on nuclear issues, is reluctant to allow such research to move forward because of its potential to create atomic weapons. This paper describes the historical, political, and economic bases for the differences in opinion between these longtime allies.

CHAPTER II: TRADE AND DEVELOPMENT

***Another Korean FTA with Latin America:¿Sí o No?*, by Lubomir Sokol**

Historically, South Korea and Latin American countries have not been major trading partners. However, several political, social, and economic developments in the past 10 years have reshaped their interactions, resulting in a boom in interregional trade. This growth can be attributed to a number of factors ranging from the adoption of neoliberal economic policies in many Latin American countries to Korea's growing need for mineral resources. In response to this increase in trade, Korea has pursued free trade agreements (FTAs) with a few Latin American countries, starting with Chile in 2003 and Peru in 2010. Korea has since expressed interest in pursuing FTAs with important regional entities including Mexico and the Mercosur trading bloc. This paper examines Korea's Latin American trade agenda and how its decisions to sign or not sign FTAs with key countries impact the Korean economy.

***Korea's ODA to Africa: Strategic or Humanitarian?*, by Rob Folley**

South Korea's growing economy, expanding role on the global stage, and history of rapid development, have made it an increasingly important provider of international aid and development assistance. Seoul's aid to Africa, in particular, has greatly expanded in recent years, reflecting both humanitarian goals and strategic interests in the continent. While these development programs are partially driven by a humanitarian interest in replicating Korea's development success abroad, they are also shaped by Korea's interest in securing energy and other resources from Africa. This paper provides an overview of Seoul's development assistance programs in Africa, and examines the scope of Korea's economic and resource-oriented interests, concluding that a middle ground, balancing humanitarian and strategic goals, can be reached.

CHAPTER III: GOVERNMENT AND BUSINESS

***Korea and the Great Recession: The Effects of* Chaebol *Reform on South Korea's Recovery from the 2008 Financial Crisis*, by Kate Chekan**

While South Korea was equally as affected by the global financial crisis as its Western counterparts, the nation's economy recovered much more quickly. Why did this happen? Was South Korea in a better position to recover from the crisis in 2008 because of the lessons learned from the 1997 Asian Financial Crisis? This paper seeks to answer this question by looking at the history of Korea's *chaebol* (conglomerates) and how legislation after the 1997 crisis changed their structure and function.

***FDI in Korea: The Permanent Achilles' Heel?*, by Andrew Noh**

The South Korean economy stands as a model for many developing countries around the world. Not only did it rise up from the ashes of the Korean War and survive the 1997 Asian Financial Crisis, but it has maintained its position in the global economy through the greatest financial crisis since the Great Depression. Yet for all its accomplishments, the Korean economy has one glaring weakness when compared to its regional economic rivals: a dangerously low level of foreign direct investment (FDI). This was not always the case. Korea was once an attractive destination for foreign capital, especially in the years immediately following the Asian Financial Crisis. However, in January 2010, the Bank of Korea announced that FDI in Korea had reached a historic low, painting a grim picture of foreign investor confidence in Korea, and even suggesting that there is something seriously wrong with Korea as an investment destination. This paper finds that Korea is indeed subject to regulatory and governance mismanagement, and will need to weaken the economic domination of the nation's *chaebol* if it is to attract foreign investment on a regionally comparable level.

***Sustaining Medical Tourism in South Korea*, by Kristen Handley**

South Korea's breakthrough in the medical tourism industry launched during 2007 with 16,000 foreign patients. In the year 2010, 60,000 foreign patients are expected to travel to South Korea for medical services. Anticipating 100,000 foreign patients by the year 2012, this rapidly growing trend will solidify South Korea's prominent role in the medical tourism industry. Interest in medical tourism has been steadily progressing among patients, particularly with mounting health care costs in countries such as the United States. The global medical tourism industry is expected to gross $100 billion by 2012. Clearly, there is profit to be made by providing medical care to foreigners. South Korea is cultivating this lucrative business while competing among other Asian nations to further expand its comparative advantages. This paper will explore Korea's fledgling—but flourishing—medical tourism industry, as well as the challenges that will need to be effectively addressed for Korea to be competitive in this specialized niche industry.

CHAPTER IV: IDENTITY AND SOCIETY

***Searchers and Planners: South Korea's Two Approaches to Nation Branding*, by Regina Kim**

South Korea, an economically advanced and highly modernized country that suffers from an undeservedly weak national brand, has been eagerly pursuing various measures to improve its image abroad. Currently, there appears to be two main forces of nation branding in Korea: the Korean government's official nation branding campaign and the private sector-driven Korean Wave (termed *Hallyu* in Korean). While both have the same effect of contributing to the enhancement of Korea's national brand, they differ greatly in their approach to nation branding. The government's nation branding campaign employs a more or less top-down method (the "planners" approach), in which plans and decisions are made by a government council and subsequently implemented by various agencies. The Korean Wave, on the other hand, is a market-driven phenomenon that has been generated mainly by the efforts of private sector companies to respond to consumer demand for Korean pop culture (the "searchers" approach). This paper examines the strengths and weaknesses of both approaches and suggests the need for a more integrated approach in which the public and private sectors, along with help from the general public, cooperate more closely in a complementary and effective manner.

***The North Korean Refugee Policy of the Lee Myung-bak Government: Nationalism and Multiculturalism*, by Narae Choi**

The expanding population of North Korean refugees in South Korea presents a challenge to policymakers in Seoul. North Korean refugees are in many ways cultural outsiders, often lacking the skills and socialization necessary to succeed in South Korea's dynamic capitalist economy. At the same time, the rhetoric of ethnic solidarity shapes much of the public discourse on North Korean refugees, and their integration into South Korean society is seen by many as a precursor to the challenges that unification will ultimately present. South Korean government agencies have therefore dealt with North Korean refugees as both one more migrant group in an increasingly multicultural society, and as ethnic kin in a category of their own. This paper examines the tensions between these two policies, analyzing the Lee administration's approach to the subject by looking in detail at three ministries involved in North Korean refugee support.

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CONTRIBUTORS

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CHAPTER I: SECURITY AND ALLIANCE POLITICS

The Incredible Shrinking Crisis: The Sinking of the *Cheonan* and Sino-Korean Relations

By Jeremy Chan

I. INTRODUCTION

While the sinking of the South Korean naval corvette *Cheonan* in March 2010 ratcheted up tensions on the Korean peninsula to their highest level in years, China found itself thrust into the unfamiliar position of playing regional power broker, torn between supporting its rapidly expanding economic ties with South Korea (ROK) on the one hand and its strategic interest in regime survival in North Korea (DPRK) on the other. In the end, China (PRC) predictably hedged toward the latter, shielding the North against international condemnation at the UN Security Council, but managing to do so in a manner that did not earn the lasting ire of South Korea. That China was able to successfully pull off this delicate balancing act and defuse tensions on the peninsula in the process, suggests that the *Cheonan* incident was less of a flashpoint than a flash in the pan. A similar balancing act has been considerably harder for China to strike, however, in the aftermath of the latest North Korean attack in November 2010 on Yeonpyeong Island, a sparsely inhabited South Korean island situated in highly contentious waters in the Yellow Sea near North Korea.

While the *Cheonan* sinking proved to be more important not for what was lost, notably 46 South Korean lives, but for what was salvaged; the Yeonpyeong Island shelling has seen a downturn in PRC-ROK relations which was noticeably lacking after the *Cheonan* incident in March. China's inability to placate angry South Koreans this time around speaks to differences in the nature of the two attacks, but also to a growing consensus that the two Koreas will never break out of their crisis-recovery cycle until China decides that it is in its own interest as well.

After both the *Cheonan* and Yeonpyeong incidents, the preexisting U.S.-ROK and PRC-DPRK alliances were strengthened, with China shielding North Korea from censure by the UN Security Council after the *Cheonan* sinking and U.S.-ROK forces holding large-scale military exercises after both attacks. More surprisingly, the PRC-ROK partnership, which has built up economic linkages in the past few years that have helped to mitigate conflict, also emerged from the *Cheonan* sinking largely unscathed. The same, however, has not held true in the aftermath of the Yeonpyeong Island attack, with both Seoul and Washington spurning Beijing's calls for an emergency return to the negotiating table. Subsequent large-scale military exercises by U.S.-ROK forces in the Yellow Sea were also explicitly directed at Pyongyang, and implicitly at Beijing.

What's more, just when inter-Korean relations appeared to be on the verge of taking a surprising turn for the better, with Lee Myung-bak moving away from his policy of strategic "neglect" of the North Korea question, the Yeonpyeong Island attack renewed the two countries' diplomatic freeze. Much speculation has surrounded the possible motivations for North Korea's most recent attack, the majority of which relates to the coming power succession from Kim Jong Il to his third son, Kim Jong Un, but Pyongyang has clearly indicated that it was not particularly interested in reconciling with Seoul, nor was it deterred by South Korea's futile response to the *Cheonan* sinking.

If anything, South Korea's willingness to excuse North Korea's misbehavior in March, as well as Beijing's unflagging support for the regime in Pyongyang, left the South vulnerable to another attack. That even a show of force by the United States in the form of joint military exercises could not deter more brazen North Korean attacks demonstrates that China, rather than the United States, is the linchpin for continued "stability" on the Korean peninsula, and that Beijing will play an increasingly central role in deciding the fate of the two Koreas.

China's entire approach to resolving the latest downturn in inter-Korean relations, which has consisted of measured public statements calling for restraint and stability, stands in marked contrast to U.S. efforts at deterrence. This is partly explained by China's emerging view of itself as a leader and a "neutral" peacemaker in defusing crises on the peninsula, exhibited in Beijing's recent suggestion that all relevant parties should return to the Six-Party Talks, which have remained dormant since North Korea's last nuclear test in 2009. Meanwhile, the United States has felt compelled to reassure and stand by one of its staunchest allies in Asia, conducting large-scale joint military exercises with South Korean forces after the *Cheonan* sinking and again after the Yeonpyeong Island attack. The latter exercises, which featured a U.S. aircraft carrier battle group, were officially held as a means of defending against further North Korean provocations, but their location in the Yellow Sea near waters that China claims as its own territory was also a shot across the bow at Beijing, which had loudly objected to earlier plans to hold exercises in the same waters in July. In a recent visit to Japan, U.S. Admiral Mike Mullen even suggested that Japan may take part in future U.S.-ROK exercises as a sign of solidarity and growing concern over the rise of China's influence in North Korea.

While the United States and China took decidedly different diplomatic tactics in response to the two attacks, they have both remained remarkably consistent in their approach to the peninsula and have achieved similar outcomes, as China managed to draw its allies in Pyongyang closer to Beijing, and the United States saw its once-flagging security alliance with South Korea reinvigorated. At the same time, the adversarial U.S.-DPRK relationship, which had very little to lose as a result of another round of brinksmanship, saw both sides turn up their rhetoric. For their part, however, the parties in the PRC-ROK relationship could ill afford direct confrontation over the latest attacks, as both countries would stand to lose a great deal in the event that economic relations soured.

This may partially explain why the United States and North Korea could opt to continue their pattern of viewing the other antagonistically, but both China and South Korea have had to strike a delicate balance between their competing security obligations on the one hand and their economic interests on the other. What is most unusual about the outcome of the *Cheonan* sinking then is not so much that security interests trumped economic ones in the case of China, but that the PRC-ROK partnership registered little damage from a crisis that had set the two Koreas on the brink of war.

That South Korea has been far less accommodating of China's equivocation over the Yeonpyeong Island attack, however, speaks to a growing frustration in Seoul with Beijing, as well as a growing recognition that deference to China may only serve to undermine efforts at deterrence on the peninsula. Ultimately, South Korea may have come to realize only too late that all roads to Pyongyang lead through Beijing, and Seoul's plodding response to the *Cheonan* sinking may even have precipitated the subsequent attack on Yeonpyeong Island.

II. THE CRISIS THAT WASN'T

While the Korean peninsula has reentered a crisis phase since the Yeonpyeong Island shelling, relations between the two countries had actually improved considerably by the eve of the attack. This brief thawing of tensions between the two Koreas only months removed from the *Cheonan* sinking was as improbable as it was short-lived. The two Koreas perpetually seem to find themselves in a crisis-recovery loop, in which relations bend without breaking, and cooler heads eventually prevail. But for a brief moment in March and April, the sinking of the *Cheonan* was feared to be the final nail in the coffin for peace on the Korean peninsula. The *Cheonan* attack was merely the lowest point, however, in a steadily downward trajectory in inter-Korean relations that, since 2008, had witnessed the end of the previous administrations' Sunshine Policy (1997–2007), the collapse of the Six-Party Talks, and another round of North Korean nuclear tests. In contrast to previous crises between the two Koreas, however, in which Seoul seemed far less concerned about the possible outbreak of war than either Washington or Tokyo, many South Koreans came to view the *Cheonan* provocation differently. The conservative government in Seoul, which had previously advocated a policy of strategic "neglect" of the North Korea question, was facing local elections in June, and common wisdom held that a show of strength by the government was a winning strategy for the ruling party. Indeed, in response to the sinking, which Seoul officially blamed on a North Korean torpedo in a presidential announcement on May 24, South Korea placed a restrictive trade embargo on North Korea, resumed broadcasts of "psychological warfare" propaganda across the DMZ, and sought international condemnation of Pyongyang by the UN Security Council. North Korea, for its part, vehemently denied any involvement in the attack, responding that the allegations were "South Korean slander," cutting off nearly all ties with South Korea, and threatening all-out war if North Korea were to be punished for a crime it claimed not to have committed.

As the rhetoric on both sides heated up and relations between the two Koreas veered dangerously close to war, both the South and the North sought the support of China, which continued to call for stability and restraint on the Korean peninsula. ROK President Lee Myung-bak paid a visit to Shanghai in May as part of the opening of the 2010 World Expo, where he met with Chinese President Hu Jintao and asked for China's cooperation in the ongoing *Cheonan* investigation. Lee's request, however, went unheeded, and his visit was overshadowed only a few days later by the arrival of North Korean leader Kim Jong Il in Beijing. As Victor Cha noted in a May 25 column in the *Chosun Ilbo*, "Only three days after President Lee Myung-bak met with President Hu Jintao in Shanghai and discussed the *Cheonan* investigation, Hu stood smiling and with open arms embracing Kim Jong Il. Despite Lee's entreaties, Hu did not even have the courtesy to let the South Korean president know that he would host Kim." How central of a role the *Cheonan* incident played in this May meeting between Hu and Kim, not to mention what concessions were made by North Korea in return for Chinese support at the UN, remains unclear, but after receiving the leaders from both Koreas, China opted to continue its policy of advocating for restraint on the Korean peninsula rather than blame the North for the attack.

The flurry of diplomatic competition between the two Koreas over Chinese support has only highlighted China's evolving role on the Korean peninsula, from one-time antagonist to principal arbiter, as well as its increasingly untenable position as the lone supporter of North Korea. Indeed, rather than bolstering its profile in the region, China's newfound role as mediator between the two Koreas has the potential to divide the country between its short-term strategic and long-term economic interests. This reality was underscored in August, when Kim paid another visit to China after much of the anger over the *Cheonan* sinking had subsided, presumably to seek Beijing's approval of North Korean succession plans that will see absolute authority kept within the Kim clan for a third generation. This visit underscored the fact that, while it once appeared as though China's "reform and opening up" would necessarily compel North Korea down a similarly incrementalist path, something that Chinese diplomats are surely lobbying for behind the scenes, recent history, including the Yeonpyeong Island attack, suggests that the recalcitrant North may just as soon force China to risk harming its economic partnerships in order to save the Hermit Kingdom.

All of the efforts by South Korea after the *Cheonan* sinking to seek Chinese and international support, however, have been noticeably lacking in the aftermath of the Yeonpyeong Island shelling. This is partly a function of North Korea's unquestioned perpetration of the attack, and also recognition by Seoul that Beijing will stand by its allies in Pyongyang even in the face of undeniable proof. Furthermore, while Chinese media reports have been slow to condemn the attack, they have also attempted to give credence to Pyongyang's stated position that its actions were a defensive response to South Korean encroachment into North Korean waters. This may explain South Korea's growing impatience with China's empty calls for "restraint" on the peninsula, particularly as Beijing's allies in Pyongyang continue to exhibit precious little of it.

III. CHINESE RESTRAINT

In the immediate aftermath of the *Cheonan* sinking, the United States was able to come quickly to the defense of South Korea, demanding an apology from Pyongyang and conducting a series of joint military exercises with South

Korean forces in July and August as a show of solidarity. China, meanwhile, was left to claim that the real culprit of the sinking was still undetermined, and yet subsequently acted as if finding the party responsible for the attack was beside the point. According to one report in China's state-run organ *People's Daily,* Chinese Foreign Minister Yang Jiechi urged restraint from his South Korean and Japanese counterparts at a tripartite meeting in May, insisting only that "China hopes that the nations involved value the peace and stability of the Korean peninsula and this region, take a long-term view, and maintain dispassionate self-control so that they can handle related issues smoothly." This emotionless language was largely reiterated in October in China's statement to the UN General Assembly, in which Beijing drily added that "the current situation on the Korean peninsula remains complex and sensitive."

Part of China's reluctance to apply pressure on the North in the wake of the *Cheonan* sinking no doubt stemmed, in part, from its skepticism about the findings of the international commission that somewhat speciously blamed the attack on a North Korean torpedo, but China's ultimate decision to shield the North from international condemnation was largely predetermined by its overriding interest in securing regime survival in Pyongyang. While China claimed that the international investigator's findings were inconclusive, it reportedly refused repeated invitations to participate in the investigation itself. Moreover, China never made any clear statement regarding what, if any, threshold would have constituted conclusive evidence, and it presumably was not in Beijing's interests to be too specific on this point.

While the world may never know definitively whether North Korea had any involvement in the *Cheonan* sinking, the fact that North Korea openly shelled Yeonpyeong Island only a few months after vehemently denying any involvement in the March attack would seem to render the *Cheonan* culprit a moot point. Nevertheless, China's handling of the *Cheonan* incident clearly indicated that its strategic interest in maintaining the status quo on the Korean peninsula trumped both its substantial economic ties with the South and its much-discussed role as a "responsible stakeholder" in the international community.

Undeterred by China's foot-dragging over the findings of the international investigation in May, however, President Lee emphasized the importance of bringing the matter of the *Cheonan* before the world, saying in an address on Korean radio that same month, "We have to find the cause in a way that satisfies not only our people but also the international community." In June, South

Korea finally took its case before the UN Security Council, of which China is a permanent veto-wielding member, and was rebuffed when the watered-down presidential statement that emerged on July 9 made no mention of North Korea by name. This was seen as a victory of sorts for Pyongyang, whose diplomats reportedly celebrated the Security Council's announcement with their Chinese counterparts, and a blow to Lee's diplomatic efforts. By using its veto power on the Security Council somewhat curiously to condemn the attack while refusing to condemn the attacker, China sought to strike a delicate balance between its competing interests on the Korean peninsula, but it dealt an undeniable blow to South Korean hopes for international consensus in the process, and laid the groundwork for Seoul's split from Beijing after the Yeonpyeong Island attack.

Outside diplomatic circles, however, Beijing's equivocation over the *Cheonan* incident was greeted with a collective shrug on the streets of Seoul, which has been known to host raucous demonstrations in the past few years over far more innocuous issues such as the Korea-United States Free Trade Agreement (KORUS FTA) and the presence of U.S. military bases in Korea. That South Koreans reacted with neither great surprise nor indignation to China's balancing act indicates an awareness on the part of South Koreans that their neighbor's defense of North Korea was done out of its own national interest.

To the extent that it was expressed at all, South Korean outrage over the *Cheonan* incident was directed first and foremost northward, followed by a smaller but vocal contingent that remained critical of President Lee's handling of the matter. Conservative media outlets ran customary editorials excoriating China for its continued Cold War mentality *vis-à-vis* the North, as well as its refusal to realize that its economic future lay with the far more dynamic South, but public opinion found the Lee Myung-bak government a far more accessible scapegoat. The poor performance of the ruling conservative party in local elections in June further underscored the perception that South Korean people were more dissatisfied with the performance of their own government than with the role that China had to play in denying North Korea's involvement in the *Cheonan* sinking. Moreover, at no point did demonstrations in Seoul over the *Cheonan* incident rival past public protests, which indicated a sense of ambivalence on the part of the South Korean public toward North Korea's involvement in the *Cheonan* sinking, as well as one of resignation toward China.

Yet, even as China was deftly able to win this particular diplomatic battle, Beijing's continued defense of Pyongyang puts China on course to lose the public relations war, as the recent outpouring of Korean anger over the

Yeonpyeong Island attack illustrates. That much more vocal demonstrations have taken place on the streets of Seoul in November is proof that South Koreans view the shelling of civilian residences differently than the sinking of a naval ship. While Beijing still has not received as much blame for the attack as Pyongyang has in these recent demonstrations, China's ability to maintain its balancing act in the Korean peninsula appears increasingly untenable. As the developmental "race" between the two Koreas has turned into a rout, calls mount for China to use its near monopoly-like influence over North Korea to prove that it can act as a "responsible stakeholder" in the global community. What's more, the rising ability of China to dictate terms on the Korean peninsula, as well as Beijing's claims over disputed waters with Japan and in the South China Sea, have effectively made many of its neighbors long for the return of U.S. influence to the region. Indeed, the most immediate impact of China's equivocations over the *Cheonan* sinking and the Yeonpyeong Island attack may have been a strengthening of the U.S.-ROK security alliance, which had been on the decline in recent years, although only time will tell if this will represent a permanent shift in the alliance. More worrying still for Beijing, however, is a growing consensus in East Asia that China's defense of North Korea is proof that the country's rise is not necessarily a force for peace in the region, as evidenced by a December 6 meeting between the top diplomats of the United States, South Korea, and Japan, at which a "unified position" on North Korea was announced.

IV. DETERRENCE OR DEFERENCE?

If the Yeonpyeong Island attack has solidified the enduring importance of the U.S.-ROK alliance to regional stability, the *Cheonan* sinking was where it all began. The same month that saw North Korea escape censure by the UN Security Council also witnessed both U.S. Secretary of State Hillary Clinton and Secretary of Defense Robert M. Gates pay special visits to Seoul, where they met with their Korean counterparts and promised unwavering U.S. support for Seoul in its efforts to "maintain a robust combined defense posture capable of deterring and defeating any and all North Korean threats." In a joint statement released on July 21 that followed the "2+2 meeting" of the U.S.-ROK foreign and defense ministers, the two countries "called upon North Korea to refrain from further attacks or hostilities against the ROK and underscored that there would be serious consequences for any such irresponsible behavior."

The annual U.S.-ROK joint military exercises, which included the USS *George*

Washington aircraft carrier and 8,000 soldiers in an apparent show of strength, were also held in July, and plans were announced to conduct an additional series of exercises over the ensuing months. While the exercises were meant primarily as a show of unity and as a means of deterring further North Korean aggression, the North felt compelled to threaten a "retaliatory sacred war" in response to the drills. Furthermore, the exercises also included an undercurrent of provocation directed toward Beijing, which repeatedly and vocally objected to plans to conduct U.S.-ROK military exercises in the Yellow Sea to the west of Korea, large parts of which China claims as its own territorial waters.

This show of unified force by the United States and South Korea, however, did not deter further North Korean adventurism, and may have contributed to feelings of strategic insecurity in Pyongyang that precipitated the shelling of Yeonpyeong Island, in what Pyongyang claims was a response to South Korean naval exercises on the morning of the attack that saw shots being fired into North Korean waters.

In noticeable contrast to the U.S.-ROK alliance, however, which registered a sizable uptick in saber-rattling after the *Cheonan* sinking, China's far more measured response to the attack spoke to an increasing reluctance on its part to defend the North against mounting criticism from the United States and South Korea. Indeed, China's influence over Kim Jong Il's regime is often overstated, as is its patience in dealing with the unpredictable North. China would clearly have preferred that the North not engage, for example, in nuclear tests in either 2006 or 2009, not to mention this latest series of provocative attacks against the South in 2010. The fact that both of these events occurred at all suggests that China has less sway over policymaking in the North than is commonly presumed. For their part, however, many U.S. officials seem to believe that pressuring Beijing may be a more effective means of bringing about eventual change in Pyongyang. One such official, Admiral Robert F. Willard, the commander of the United States Pacific Command, told the *New York Times* in July, "If I have a concern *vis-à-vis* China, ... it is that China exert itself to influence Pyongyang so that incidents like the Cheonan don't happen in the future." Since the Yeonpyeong Island attack, both the United States and South Korea have stepped up their efforts to convince China that it is also in Beijing's interest to apply more pressure on Pyongyang.

Yet, to the extent that China appears to be nothing more than the first country informed of North Korean policy after it has already been carried out, the ability of Beijing to restrain Pyongyang from further provocations in the future is anything but guaranteed. What's more, China's recent effort to get all parties to return to the defunct Six-Party Talks over nuclear disarmament suggests that Beijing is neither comfortable with nor prepared to assume the role of sole negotiator for North Korea. While this admission does not diminish the fact that the China-DPRK relationship has dramatically improved since its nadir right after the 2006 nuclear test, the North has proven itself very capable of defying even its most important ally. This may partially explain China's enthusiasm for sharing the burden of dealing with North Korea, as well as China's attempts to deflect criticism that it is enabling Pyongyang's continued defiance of the international order.

At the same time, South Korea's initial willingness to carry on its economic partnership with China after the *Cheonan* sinking as if nothing had happened speaks to a pragmatism on the part of Seoul that borders on deference. In an ironic twist to the *Cheonan* saga, the relatively muted response by South Korea following its diplomatic snubbing at the hands of the Security Council would seem to suggest that increasing economic engagement has made the South more reluctant to cross China than the supposed Chinese "client state" in North Korea, a reality that no doubt has informed Chinese foreign policy making. PRC-ROK trade has been an engine of growth for both countries over the last decade, and China now far outranks Japan and the United States as the South's largest trading partner, which may explain the reluctance of South Korea to harm trade relations with China in the name of pressuring China to reconsider its own long-term objectives on the Korean peninsula.

According to the WTO, South Korea currently ranks as China's third-largest source of imports and its fifth-largest destination for exports, meaning that both countries would stand to lose considerably from deterioration in bilateral relations, but only South Korea has acted as if its strategic interests have been taken hostage by its economic ones. As the Yeonpyeong Island attack painfully illustrates, rather than deterring further North Korean adventurism by creating a credible deterrent threat, South Korea's feeble response to the *Cheonan* sinking may only have emboldened Pyongyang.

The South's defensive strategy following the *Cheonan* sinking, which is better described as threat mitigation than threat prevention, implied that the country was willing to suffer small-scale attacks such as the one at Yeonpyeong Island in order to prevent the outbreak of war. Seen through this prism, China's ability to balance its competing interests on the Korean peninsula is simply a byproduct of South Korea's tacit unwillingness to forcefully retaliate, or even to risk harming its economic partnership with China.

While this strategy seemed to be a political winner in South Korea after the *Cheonan* sinking, when historically and ethnically complicated feelings toward the North combined with doubts over the North's involvement in the attack, South Koreans were quick to blame the Lee Myung Bak government this time around for not acting more forcefully after the Yeonpyeong Island shelling. The four South Koreans who perished in the Yeonpyeong Island attack were far fewer than the 46 who died in the *Cheonan* sinking, but the shelling included South Korean residences for the first time since 1953 and killed two civilians in the process, raising hackles among South Koreans, who protested that their government should have done more to retaliate. Yet, the fact that South Koreans have been willing in the past to excuse away misbehavior by their recalcitrant neighbors to the north suggests that acrimony over the Yeonpyeong Island attack will also quickly subside.

Feelings of fraternity and pathos certainly influenced the rapidity with which the two Koreas made motions to set their differences aside and restart relations on the peninsula after the *Cheonan* sinking, and may also have contributed to the curiously timed announcement in August by the Lee Myung-bak government that it was considering instituting a "unification tax" that would help cover the costs of eventual unification with North Korea. While Lee did not elaborate in August on either the specifics of his proposal or the policy considerations that motivated his decision, the timing of the announcement—less than one month removed from large-scale U.S.-ROK joint military exercises—could not have been more unexpected, and signaled that the South Korean government had moved beyond saber-rattling.

That South Korea's conservative government was showing signs of willingness to return to the negotiating table on the eve of the Yeonpyeong Island attack made North Korea's decision to shell the island all the more curious. Only days before, Pyongyang had revealed the sophistication of its uranium enrichment facilities to a visiting American nuclear scientist, which also served to put the brakes on any nascent momentum to return to the Six-Party Talks. What Pyongyang hoped to achieve through this latest outburst has baffled strategists in South Korea, China, and the United States alike, and undermined belated efforts by Beijing to call for an emergency meeting of the relevant parties. For its part, North Korea's propaganda machine has claimed that the loss of civilian lives at Yeonpyeong Island, "if true, ... [is] very regrettable," and continues to maintain that the shelling was only retaliation for shots fired earlier in the day by South

Korean forces across the disputed Northern Limit Line (NLL).

Yet, even as the Yeonpyeong Island attack has delayed progress indefinitely on reopening the lines of communication between Pyongyang and Seoul, or Washington for that matter, the greatest lesson learned from the *Cheonan* sinking may be that no act of North Korean intransigence is unforgivable.

V. THE SHORTEST WINTER

Since reaching their lowest point in years after the sinking of the *Cheonan* in March 2010, inter-Korean relations began to show significant signs of recovery within half a year. In September, South Korea announced that it was sending some $8.5 million in humanitarian aid northward, including 5,000 tons of rice and 10,000 tons of cement. This was a small, but symbolic amount, which represented the first aid donation of any kind since the Lee Myung-bak administration took power in 2008. The aid was officially sent as a result of devastating floods in Sinuiju, a city near the border with China, but political and diplomatic considerations surely influenced the timing of the decision. North Korea, in return, agreed to release a fishing vessel and its South Korean and Chinese crew that Pyongyang claimed had drifted into its territory.

What role, if any, China played in brokering this latest thaw in inter-Korean relations is still unclear, but reports have indicated that North Korea initially demanded greater amounts of rice and cement in return for the ship and its crew, only to be convinced by Beijing to accept the smaller quantity in order to move relations forward. This news was followed by an announcement that reunions between families divided during the Korean War would also resume. The exchange program, which had seen some twenty thousand Korean people meet their relatives stranded on the other side of the 38th parallel since 2000, had been suspended along with most other forms of communication after the *Cheonan* sinking. In fact, the only project that was left untouched during the *Cheonan* crisis was the Kaesong Joint Industrial Complex, which is located across the border in North Korea and is seen as the most important symbol for eventual Korean reunification. Therefore, the report that talks were underway before the Yeonpyeong Island attack about opening another industrial park in North Korea similar to the one at Kaesong is further indication that inter-Korean relations are capable of improving nearly as rapidly as they can deteriorate.

If anything, the speed and degree with which relations recovered on the Korean peninsula after the *Cheonan* sinking may have emboldened North Korea to try its hand at another provocation. Rather than causing irreparable damage to hopes for reunification, the *Cheonan* crisis seemed to momentarily bring the two sides closer together, and convinced the Lee Myung-bak government to reconsider its policy of strategic "neglect" of North Korea. Lee had pursued a hard line toward North Korea since he came to power more than two years before the *Cheonan* sinking, and many people inside and outside of South Korea blamed this policy for North Korea's recent misbehavior. That Lee initially maintained this hard line approach toward the North in the months immediately after the sinking, only to change tactics after a resounding defeat of his ruling party in local elections in June, which was quickly followed by South Korea's diplomatic disappointment at the hands of the UN Security Council, shows an awareness on his part that a harder line toward North Korea may have been a losing strategy. Any positive momentum toward reopening negotiations with Pyongyang, however, was promptly lost in the November attack.

The rapid change of heart in Seoul's behavior toward Pyongyang may be explained by South Korea's own attempt to balance between the more confrontational tactics of Washington and the more restrained and nuanced approach of Beijing. Indeed, the ease with which South Korea was able to scale down its rhetoric and transition to a more conciliatory posture is proof that the *Cheonan* sinking was far less of a flashpoint for conflict than a flash in the pan, although subsequent North Korean hostilities would seem to indicate that Pyongyang remains more interested in provocation than conciliation for the moment. For the time being, all indications are that inter-Korean relations in the aftermath of the Yeonpyeong Island attack will follow the same crisis-recovery cycle witnessed after the *Cheonan* sinking, with an initial hardening of rhetoric, which will be followed by rapid conciliation and then inevitably renewed crisis.

VI. CONCLUSION

In the months immediately following the sinking of the *Cheonan*, tensions understandably ran high in South Korea, and calls mounted for a response of some kind. The Lee Myung-bak government was able to withstand these initial pressures as it conducted a protracted investigation into the causes of the sinking, believing that a deliberate process would be the key to reaching international consensus. In the end, however, no amount of credibility could be lent to the international committee's findings to convince China to blame the alleged torpedo attack on North Korea. The ensuing drama, which saw the

United States rally to South Korea's defense and the two Koreas engage in a war of words, only underscored the importance of China's refusal to blame Pyongyang for the attack. Indeed, no amount of saber-rattling on the part of the United States, or entreaties on the part of South Korea, could move China away from its policy of empty calls for restraint on the Korean peninsula. That China ultimately prioritized its strategic interest in maintaining the status quo in North Korea over its substantial economic ties with the South is not particularly shocking, but Seoul's willingness to quietly accept this betrayal was a worrying indication that South Korea was not prepared to risk endangering its economic relationship with its largest trading partner in order to confront Beijing. In the wake of the Yeonpyeong Island attack, however, it appears as though South Korea has changed its approach to China. No longer is Seoul attempting to curry favor with Beijing; rather, Seoul has redoubled its security alliance with Washington, increased its rhetoric toward the North, and snubbed Beijing's efforts to restart Six-Party negotiations.

Indeed, the recent downturn in relations between Seoul and Beijing over the Yeonpyeong Island attack suggests that South Korea may finally be waking up to the reality that all roads to Pyongyang lead through Beijing. Beijing's balancing act during the *Cheonan* crisis showed not only how China continues to view its competing obligations on the Korean peninsula, but how South Korean deference to China in its coddling of the regime in Pyongyang might undermine efforts at deterrence against further North Korean adventurism. Seen through this prism, the Yeonpyeong Island attack was shocking for its timing and its brazenness, but not for its occurrence. South Korea has proven itself willing to endure any number of small-scale attacks in the past, including the *Cheonan* sinking, and it remains to be seen whether the latest Yeonpyeong Island provocation will substantially alter the crisis-recovery pattern that has come to define inter-Korean relations. If the *Cheonan* incident is used a model, then recovery may come more rapidly than anyone expects; if it is used as a cautionary tale, however, then inter-Korean relations may be in for more tensions ahead.

Most likely, substantive change on the Korean peninsula will only come about once Beijing feels sufficient motivation to end its support of the regime in Pyongyang. The current rift in PRC-ROK relations notwithstanding, it would appear that neither South Korea nor China is ready to consider fundamentally altering its approach to the other, which suggests that North Korea may continue to take advantage of this interest asymmetry. As China continues to call for restraint on the peninsula and a return to the Six-Party Talks, and tensions in

South Korea inevitably subside, however, a thaw in inter-Korean relations similar to the one seen after the *Cheonan* sinking appears likely. Whether anything substantial will result from further negotiations, however, may depend more on Beijing than Pyongyang. China's substantial interests on both sides of the 38th parallel suggest that Beijing will play a central role in brokering any peace between the two Koreas, and the ultimate destiny of the two Koreas will depend more on China than either side has completely prepared for.

Realism and Liberalism in Economic Sanctions: An Analysis of South Korea's Sanctions on Iran in 2010

By Soo Kook Kim

"When a country like Japan or South Korea or China or Russia—all of whom have commercial dealings with Iran—make these decisions, they do so at great cost to themselves."
~ Barack Obama, in an interview with BBC Persian

I. INTRODUCTION

On June 9, 2010, the United Nations Security Council (UNSC) adopted UNSC Resolution 1929 (hereafter, "UNSCR 1929"), which puts additional sanctions on Iran on top of UN Resolutions 1737 (2006), 1747 (2007), and 1803 (2008). The resolution was targeting Iranian companies and officials that were allegedly supporting terrorist groups and transferring prohibited weapons. Within two months, the U.S. Department of Treasury announced the release of a new list of 21 Iranian businesses and several individuals involved in terroristic acts prohibited by Resolution 1929. At the same time, Robert Einhorn, the U.S. State Department's special adviser for nonproliferation, visited Seoul and Tokyo, accompanied by Daniel Glaser, Treasury's deputy assistant secretary for terrorist financing. On August 2-3 in Seoul, they met with the Ministry of Foreign Affairs and Trade (MOFAT), the Ministry of Strategy and Finance (MOSF), and the Blue House, calling for Seoul's cooperation in banning economic ties between South Korea and Iranian blacklisted entities.

In response to the United States' appeal, South Korea announced on September 8 a new set of sanctions on Iran under UNSCR 1929. The U.S. president, Barack Obama, lauded South Korea's action of joining international efforts to strengthen sanctions against Iran to pressure the Islamic country to abandon its suspected nuclear weapons ambitions. It is the first time that South Korea has voluntarily taken harsh measures against Iran. Aside from the obligatory UN sanctions, it has kept a balanced position between its strong, decades-old alliance with the United States and economic considerations with its biggest trading partner in the Middle East. Iran, South Korea's fourth-largest crude oil supplier, accounted for nearly 10 percent of South Korea's oil consumption last year. Key South Korean businesses, including LG, Hyundai, Samsung Electronics, Hanjin Heavy Industries, and Daewoo Shipbuilding, have signed billion-dollar contracts with Iran in recent years.

However, breaking the balance between Iran and the United States posed a conundrum for the Korean government as it weighed conflicting domestic and foreign interests. Internally, a great deal of speculation rose about Korea's economic troubles that might result from sanctions on Iran. Internationally, however, South Korea was required to join UNSCR 1929. In addition, it also desired to maintain a viable alliance with the United States. From the South Korean perspective, the economic loss was a tangible, short-term impact of the sanctions, whereas the result of the alliance weakening and failure to meet international obligations were long-term and less tangible.

This paper fundamentally questions why South Korea put sanctions on Iran. It also questions whether or not it was a successful course of action. In order to answer the questions, it borrows classical international relations concepts of realism and liberalism, although with narrowed meanings. In this paper, "realism" refers to the calculation of materialistic and strategic gain and loss. Conversely, "liberalism" means the pursuit of a greater cause in spite of materialistic damages.

At first sight, South Korea appears to have given up economic gains for other reasons. Does South Korea, then, show liberalism by pursuing the virtue of peace and alliance instead of materialistic gains? Or is Seoul's decision a realistic outcome from a close cost-benefit calculation? This paper will first discuss the measures that South Korea has taken in this regard, examine the impact of Iranian sanctions on South Korea, and then move on to South Korea's quandary regarding its decision and its relevance to other issues of U.S.-ROK relations. Finally, it will conclude with an answer to those questions as well as suggestions for the ROK government.

II. WHAT ARE THE SOUTH KOREAN SANCTIONS AND THE UN RESOLUTION?

South Korea's sanctioning measures are largely formulated in accordance with that of UN resolutions. Major details in the measures are the following: a proliferation-sensitive nuclear and ballistic missile programs–related embargo;

a ban on the export and procurement of any arms and related material from Iran; a ban on the supply of the seven categories of conventional weapons and related materials to Iran; and travel bans and asset freezes on designated persons and entities (see table 1).

These new measures are also in line with measures imposed by Japan and the European Union. Although the degree of sanctions that Washington demanded from Seoul remains unclear, Washington was reportedly not satisfied with the UN measures, which were merely recommendations. Sources say that Washington asked each ally to put bilateral sanctions on Iran. Presumably, this is the reason Einhorn and Glaser went to Seoul. Einhorn reported during a press conference in Seoul in August, "We suggested to the South Korean government that they take a look at what the Europeans have done, and look at that as a kind of very positive example, and to consider whether it could adopt similar kinds of measures." In response to the U.S. request, South Korea adopted comprehensive measures against Iran, including particularly extensive sanctions in the energy sector. South Korea banned investment and construction in petroleum and gas development in Iran, which was not specified but only vaguely mentioned in UNSCR 1929.

It is certain that Korea took a parallel step with the United States within the context of international cooperation. Foreign Ministry spokesman Kim Young-sun said that the sanctions further reinforced UNSCR 1929, the latest in a series of measures taken by the international community in an effort to halt Iran's nuclear program. He explained, "South Korea expects Iran to join international efforts for nuclear nonproliferation and take steps to faithfully implement its obligations under the relevant UN Security Council resolutions."

Table 1. List of Republic of Korea (ROK) Measures

	Details of ROK Measures	Relevant Provisions of UNSC Resolution 1929
Finance	Designation of 102 entities and 24 individuals – Severe penalty on Bank Mellat Seoul	Provisions 11, 12, 19, 22 Annex of Resolution 1929
	Prior authorization scheme (for over €40,000) and prior reporting requirements (for over €10,000) for financial transactions with Iran	Provision 21
	Prohibition of the opening of new branches of Iranian banks in the ROK and vice versa	Provisions 23, 24
	Prohibition of the establishment of new correspondent banking relationships with Iranian banks	Provision 23
	Gradual termination of existing correspondent banking relationships with the Iranian banks subject to financial sanctions	Provision 23
	Prohibition of the sale or purchase of national bonds (if there are reasonable grounds to believe such activity could contribute to Iran's proliferation-sensitive nuclear activities and the development of nuclear weapons delivery systems)	Provision 21
	Prohibition of the provision of insurance and reinsurance (if there are reasonable grounds to believe such activity could contribute to Iran's proliferation-sensitive nuclear activities and the development of nuclear weapons delivery systems)	Provision 21
Trade	Reduction of export guarantees to Iran	Preamble and Provisions 21, 22
	Prohibition of the export of strategic items, including dual-use items	Provisions 8, 9, 13

Transportation & Travel	Strengthening of inspections on vessels or aircrafts to and from Iran that are suspected of carrying prohibited items	Provisions 14, 15, 16
	Prohibition of the provision of services to Iranian vessels or cargo aircrafts suspected of carrying prohibited items	Provision 18
	Prohibition of the access to domestic airports of cargo aircrafts operated by Iranian carriers (if there are reasonable grounds to believe such activity could contribute to Iran's proliferation-sensitive nuclear activities and the development of nuclear weapons delivery systems)	Provision 14
	Travel ban on the individuals designated pursuant to the UNSC resolutions	Provision 10
Energy	Prohibition of new investment, technical, or financial services and construction contracts in petroleum resources/gas development; restraint and caution when performing existing contracts	Preamble and Provision 22
Steps Necessary for the Implementation of the Measures	Opening of a won-denominated account	
	Implementation of "Guideline on Trade with and Investment in Iran," "Guideline on Contracts for Overseas construction with Iran," and "Guideline on Settlements in Relation to Iran"	Provisions 21, 22

III. BITTER IMPACT ON KOREA

As the Iran sanctions are an ongoing issue, it is hard to measure how large the impact has been on South Korea. The impact can be roughly analyzed in three dimensions—short-term, mid-term, and long-term. These distinctions were made in accordance with statistical findings and through interviews with government and bank personnel.

Short-Term: Direct Economic Hardships for South Korean Firms

Even before South Korea announced sanctions, South Korean firms were suffering from UNSCR 1929 and the U.S. sanctions toward Iran. Early in August, a survey conducted by the Korea Federation of Small and Medium Business showed that more than half of Korea's small firms trading with the Middle Eastern country have already suffered a loss. This was because of the announcement of U.S.-led sanctions against Iran, the Comprehensive Iran Sanction, Accountability, and Divestment Act of 2010 (CISADA). CISADA, signed by President Obama on July 1, includes new provisions designated for foreign firms currently doing business with Iran.

With concerns spreading about CISADA, Korean small businesses have voluntarily halted 31.5 percent of exports to Iran. These preemptive measures taken by domestic firms brought a great loss to the economy. For instance, a trading firm was left holding unsold inventory worth several hundred million *won* because it was unable to open a credit account. Others complained about the inability to collect export payments from Iran. In a *JoongAng Daily* article in August 2010, one company official complained, "We had plans to export $1.03 million worth of automobile components to Iran but due to difficulty in settling payment, we are left with nothing but to break the contract."

According to the article, local companies—especially in steel, chemicals, and automobiles—have encountered difficulty sending money to and from Iran since the July UN sanctions on the country. Some local banks have stopped transactions with Bank Mellat, the only Iranian bank operating in Korea, to prevent potential criticism from the international community.

After South Korea put the sanctions into law, economic damage expanded further. According to a report from the Korea Trade-Investment Promotion Agency (KOTRA) released on October 17, Korean companies are not receiving payment for goods—equivalent to approximately 250 billion *won*—since South Korea implemented sanctions against Iran. The report was based on a survey of 301 Iranian export businesses and found that these sums are not recoverable and should be considered as a direct loss. Among the 301 companies surveyed, 73.8 percent (222) suffered a loss of business and 21 percent (63) of the companies are facing bankruptcy. "Companies are complaining that the government should let them carry on their business with Iran as long as the deals are not related to weapons of mass destruction or nuclear bombs," said Kim Yong-suk, chief of the Middle East team at KOTRA. He estimates some 2,000 Korean firms will be affected by the international sanctions. "Not all, but many of Korean exporters to Iran have used Bank Mellat for receiving payments," he continued, "[and] small firms are more vulnerable because they do not have financial firewalls like big firms do."

Furthermore, Congressman Kim Jae-kyun from the Democratic Party argued on October 17, that Korean SMEs would not be able to get receivables of roughly

$225 million from Iran. In addition, an annual deficit of around $655 million is expected due to the export halt towards Iran. In the short-term, it is clear that South Korean firms are experiencing direct economic hardships resulting from the trade restrictions.

Mid-Term: Possibility of Losing Biggest Trading Partner in the Middle East

In 2009, South Korea's trade with Iran reached $10 billion. South Korean firms are concerned that limits on business with Iran will greatly undermine their long-term opportunities in the petrochemical, construction, and plant export industries. The Iranian ambassador in Seoul said on August 7 that "South Korea has 25 business conglomerates and 2,000 small and mid-sized companies operating in Iran. If the bilateral economic ties come to a halt, it will have a negative impact on some 150,000 South Koreans who will lose their jobs." Ambassador Mohammad Reza Bakhtiari emphasized the noneconomic relations between the two: "The two countries will celebrate their fiftieth anniversary of establishing diplomatic ties next year. [Just as there] is a 'Teheran Road' in Seoul, Iran also has a 'Seoul Park' and 'Seoul Bridge.' The South Korean dramas are very popular in Iran. I don't want to see our two countries' relationship backpedal because of this incident."

Recent trade statistics between the two countries show a slight decline in trade after the sanctions against Iran were implemented (see tables 2 and 3). In table 2, net exports decreased by 19.6 percent in August. When the Korean government announced sanctions in September, trade fell by an additional 39 percent. However, taking into consideration the large declines in trade of 49.5 percent in February 2009 and 47.6 percent in April 2009, before sanctions were announced, it is hard to judge whether the fall in trade from August to October 2010 was a direct result of sanctions. Additionally, cumulative trade statistics indicate that Korean exports actually declined throughout all of 2009, whereas in 2010, the rates are positive even after accounting for the sanctions.

Table 2. South Korea's trade (export) with Iran (net)

Year 양식의 맨 위 Month 양식의 맨 아래	Iran		Year 양식의 맨 위 Month 양식의 맨 아래	Iran	
	Total amount (in $1,000)	**Increase rate (%)**		**Total amount (in $1,000)**	**Increase rate (%)**
2009-01	259,479	-24.1	2010-01	366,998	41.4
2009-02	264,554	-49.5	2010-02	372,667	40.9
2009-03	270,106	-32.6	2010-03	427,642	58.3
2009-04	267,764	-47.6	2010-04	439,117	64
2009-05	293,155	-28.5	2010-05	491,876	67.8
2009-06	365,889	22.5	2010-06	457,221	25
2009-07	324,440	-10.9	2010-07	363,272	12
2009-08	308,588	8.6	**2010-08**	**248,125**	**-19.6**
2009-09	392,883	83.8	**2010-09**	**239,800**	**-39.0** 양식의 맨 아래
2009-10	361,003	35.5	**2010-10**	**326.390**	**-9.6**
2009-11	366,259	5.3			
2009-12	517,777	36.3			

Table 3. South Korea's trade (export) with Iran (cumulative)

Month	2009		2010 (1~09)	
	Value (in $1,000)	Increase rate (%)	Value (in $1,000)	Increase rate (%)
01	259,479	-24.1	366,998	41.4
02	524,033	-39.5	739,665	41.1
03	794,139	-37.3	1,167,307	47.0
04	1,061,902	-40.3	1,606,423	51.3
05	1,355,058	-38.1	2,098,299	54.8
06	1,720,947	-30.8	2,555,520	48.5
07	2,045,387	-28.2	2,918,793	42.7
08	2,353,975	-24.9	**3,167,039**	**34.5**
09	2,746,858	-18.0	**3,406,838**	**24.0**
10	3,107,861	-14.0	**3.733.229**	**20.1**
11	3,474,120	-12.3	-	-
12	3,991,897	-8.1	-	-

As it has been only four months since the sanctions came into effect and as the data fluctuates each month, it is too early to conclude that the sanctions actually led to a significant change in the amount of trade between Korea and Iran. Although statistical data to date did not show a significant decline of trade between the two nations, Lee Hu-myung, director of the International Finance Bureau at MOSF, estimates the damage to be between $7 and 15 billion. This figure includes the mid-term decline of exports to Iran, the drop in crude oil imports from Iran, and the fall in orders in construction and shipping sectors.

Long-Term: China's Strategy

In the long-term, the damage to Korean industries is more serious than its short-term or mid-term impact due to external factors. China, which has invested heavily in Iran despite international sanctions, has said it opposes the new sanctions on Iran by the United States and its allies, calling for more dialogue with Iran to address its uranium fuel. These statements have caused potential trouble for Korea and Japan. *Foreign Policy* magazine recently reported that

China has approached the Iranians with the hopes of taking over many former Korean and Japanese business contracts. Senators Jon Kyl and Chuck Schumer pointed out that the China National Petroleum Company (CNPC) replaced the Japanese firm Inpex and agreed to invest around $2 billion to develop Iran's South Azadegan oil fields last year. Because of the Chinese strategy to quickly fill in where the sanctions have left open business opportunities, the financial damage on the Iranian side has been significantly cushioned by the Chinese, while the full burden has been felt by both Korean and Japanese businesses.

The Korean Institute for International Economic Policy (KIEP) says that South Korea's comparative advantage in the petrochemicals, plant, and construction sectors in dealing with Iran will largely decline due to the sanctions. The halt of those businesses in Iran can be an opportunity for China to learn skills in the construction and shipping industries. China had not been able to receive contract orders from abroad because of South Korea's superior technology in those fields. Since last year, China started to build value-added vessels, such as very-large crude carriers (VLCCs) and LPG vessels, which used to be the specialty of South Korean shipping companies. Given the present dynamic, it is highly possible that China will soon take the place of South Korean construction and shipping industries, by learning skills during their work in Iran. A South Korean government source explained that in the long-term, Korea may lose the market for shipping companies in the world.

IV. WHAT HAS SOUTH KOREA CONSIDERED?

Consistency with Nonproliferation

The biggest issue in the South Korean consideration of the sanctions on Iran was the nonproliferation of nuclear weapons and weapons of mass destruction (WMD). The nonproliferation effort for South Korea has two unique meanings. First, Korea has an important place in the global fight to curb the spread of nuclear weapons, materials, and technologies. According to Kwon Hee-seog at the Center for Non-proliferation Studies at Monterey Institute of International Studies, Korea has been a staunch supporter of the global nuclear nonproliferation regime, upholding the values of democracy, free-market economy, and human rights. He argued in the U.S.-ROK Workshop on Nuclear Energy and Nonproliferation in January 2010 that "[r]elying on the international trade and investment for its economic prosperity, the country has everything to lose and nothing to gain when the global nonproliferation regime fails significantly."

Second, South Korea cannot be distant from the global nonproliferation effort, as it itself faces a huge threat of proliferation—North Korea. This view was strongly supported by MOFAT and the Grand National Party in the ROK National Assembly. Kwon believes that:

> Having been under the constant North Korean nuclear menace over the past two decades, Seoul foremost seeks to disarm North Korea of all nuclear weapons and existing nuclear programs, and rejects any attempts to develop or possess nuclear weapons elsewhere in the world. By taking a firm stance against the potential break-out cases worldwide, Korea often had to weather the substantial fallouts from defending the nonproliferation regime.

The issue of sanctions on Iran emerged along with the consideration of resuming the Six-Party Talks with North Korea on the issue of nonproliferation. Also, Korea was looking forward to holding the G-20 Summit in Seoul in November, where the top 20 nations show their cooperative efforts in terms of global norms. With regard to the global status of South Korea and its ongoing considerations with North Korea, the participation of South Korea in the sanctions against nuclear proliferation would have been crucial in terms of consistency.

Preserving a nonproliferation stance for Korea could show a complete inclusion in the international community and its rising responsibility in the global context. The *Wall Street Journal* (*WSJ*) welcomes Korea's participation in the sanctions against Iran. Acknowledging the initial unbalanced position that South Korea and Japan held, an editorial stated: "South Korea's recent announcement that [it will] implement United Nations Security Council Resolution 1929 is worth cheering." Following laudatory comments, the *WSJ* reports that "the Lee Myung-bak administration realizes that it can't be a responsible global actor while simultaneously propping up rogue states. That means it is growing up as a democracy." Moreover, U.S. President Barack Obama asserted that "[t]he reason [South Korea and Japan are] doing it is not simply because we're pressuring them. The reason they're doing it is because they, too, see a threat of destabilization if you have an Iranian regime pursuing nuclear weapons and potentially triggering an arms race in the region that could be dangerous for everybody." The U.S. Treasury and State Departments also gave the U.S. allies credit by acknowledging the sanctions are "not without cost." Korea's decision to sanction Iran plants a seed of trust within the participants in the sanctions—

the European Union, Canada, Australia, Japan, the United States, and others—that Korea is also taking on responsibility to support this cause.

U.S.-ROK Alliance

Interestingly, the U.S. Treasury, the South Korean Embassy, South Korea's Grand National Party, and MOFAT univocally assert that the sanctions are not imposed in the context of the U.S.-ROK alliance, but only in compliance to the UN resolution. However, it may not be possible to really separate sanctions compliance from alliance issues. The Sejong Institute, a leading think tank in South Korea, analyzed four reasons to adopt restrictions against Iran in terms of a "mature alliance."

First, Iran's theocratic regime that operates in an undemocratic way carries potential threats to international society. Therefore, the justification for sanctions, in the eyes of the U.S.-ROK alliance, comes from two sources: Iran's antidemocratic regime and its possession of WMD. Second, Iran is a country that has an intimate connection with North Korea. Since 1983, Iran and North Korea's symbiotic relationship has continued while Iran has been financing North Korea's fund for developing missiles. Additional nuclear technology exchanges between Iran and North Korea have also forced the United States and Korea to put sanctions on Iran. Third, South Korea's rising status in the world is accompanied by expectation of its meeting certain requirements of global society, especially those imposed by the United Nations. Showing such global responsibility should be considered in the broad context of the U.S.-ROK alliance. Lastly, a direct relationship between the United States and South Korea will be enhanced by cooperation on the Iran issue.

As the South Korean sanctions seem to be closely related to the U.S.-ROK alliance, issues relevant to the alliance were raised domestically after the government announced the implementation of the sanctions. The most attention was put in the *Cheonan* incident in March 2010, but the KORUS FTA and the G-20 Summit in November in Seoul were also addressed. Many suspected that the decision to impose sanctions on Iran stimulated North Korea aggression just several months later. They believe that South Korean participation in sanctioning Iran will bolster the North Korean nuclear program and its provocative acts. Also, some newspapers address the ratification of KORUS FTA as a motivation for sanctions. As President Obama announced that he wanted the free trade agreement to be finalized before the G-20 Summit, it was thought that imposing sanctions would create an amicable atmosphere between the United States and South Korea. For those people who claim that the FTA and sanctions are closely related, the sanctions on Iran can be seen as a stepping stone for future coordination with the United States.

Regarding the relevancy with other issues, both governments firmly state that they want to insulate other issues from the Iran sanctions. A top U.S. Treasury official indicated that the United States already confirmed the result of the *Cheonan* incident investigation, so this incident has not affected the sanctions. He separated the sanctions from the KORUS FTA as well, by saying that South Korea's participation in sanctioning Iran means nothing but a continuation of international efforts for nonproliferation; therefore Korean sanctions on Iran should be considered in the context of nonproliferation only. Similarly, Counselor Ham Sang-wook at the ROK Embassy in Washington affirms that the sanctions, the *Cheonan* incident, and the KORUS FTA do not bear any relevance on one another.

However, opinions vary even between government institutions. MOFAT, which was pushing the government to follow the cause of nonproliferation, insisted that the sanctions and U.S.-ROK relations were separate issues. Conversely, MOSF, which preferred to maintain economic ties with Iran, argues that the sanctions were highly influenced by the U.S.-ROK security alliance. Director Lee Hu-myung at MOSF expressed his opinion that this cooperation will lead to a positive atmosphere for future issues relevant to U.S.-ROK relations.

Overall, KORUS FTA and the *Cheonan* incident may have been a background for deliberation, although it may not have directly influenced the decision making. Korea's participation certainly promoted the image of Korea within the U.S. government and strengthened their strategic ties. It led to a relatively more favorable mood for other issues. When the Yeonpyeong incident—a North Korean artillery shelling on a South Korean island—occurred in the late November 2010, the United States sent substantial naval support to assist South Korea. This demonstrates how firm the 50-year alliance between the United States and Korea is, built upon numerous instances of mutual cooperation, including the case of the Iran sanctions.

Possible Economic Retaliation from Iran

Based on past experiences with Iran regarding its nuclear power development, South Korea would have seriously contemplated the possibility of retaliation by Iran. In November 2003, Korea participated in informal consultations on the draft resolution, which strongly deplored Iran's past failures and breaches of its safeguards obligations. When Korea upheld its adoption at the IAEA Board, Iran selected a few countries, including Korea, and warned of closing off business dealings with these countries.

Again in August and September 2005, the IAEA Board adopted two successive resolutions that found Iran in noncompliance and then reported the case to the UNSCR. Subsequently, Iran reacted angrily by expressing its concern and displeasure to Seoul. As a result, for an extended period of time, Iran delayed the issuance of a permit to import critical goods for Korean companies working in the country. This did substantial damage to the companies' business interests, according to the Islamic Republic News Agency (IRNA) and other Iranian media on September 29, 2005. As such, Korea sustained its moral position to buttress the nonproliferation regime and to share in the responsibility of maintaining global security.

This year, Iran warned about the consequences of sanctions, but it did not specify the option of retaliation. The Iranian ambassador in Seoul warned South Korea in August by saying, "Iran's economy is rapidly expanding. There are many other international companies that can replace South Korean companies in Iran. So, countries that sanction Iran will end up sanctioning themselves." The warning was less threatening than the previous responses, and surprisingly, there has been no retaliation to date. Possible reasons behind Iran's behavior, according to Counselor Ham, are the trust built between the two nations since 2005 and the magnitude of the Korean cultural influence on Iran. Due to the improved Korean-Iranian relationship, the Iranian government may have reconsidered the option of retaliation against Korea. Also, Iran may have decided to talk directly to the United States rather than react to each American ally. Although several circumstances prevented retaliation from Iran, South Korea would not have been able to erase the memory of economic reprisal when considering UNSCR 1929.

Prevention of U.S.-Led Economic Retaliation

Unsatisfied with UNSCR 1929, the U.S. State Department announced CISADA, passed overwhelmingly by Congress, signed into law on July 2010, and effective from September 29. On September 30, the State Department imposed sanctions on the Switzerland-based Naftiran Intertrade Company (NICO), based on CISADA, due to its involvement in the Iranian petroleum sector. Also, on September 27, the Government Accountability Office (GAO) released a new report that identified 16 companies in the world as having sold petroleum products to Iran between January 1, 2009, and June 30, 2010. Of those 16, the GAO reported that five have shown no signs of curtailing business with Iran, making them potential targets of CISADA. *Foreign Policy* reported that "there are some positive signs, however, that international pressure is having an effect on companies' willingness to do business in Iran." According to *Foreign Policy*, several firms from Switzerland, the Netherlands, France, India, and the United Kingdom told the GAO that they are halting their refined petroleum business with Iran. Thus, the influence of CISADA has been very powerful in the world.

As mentioned previously, the impact of CISADA on domestic banks and firms was beyond expectation. South Korean banks and firms voluntarily discontinued dealings with Iran, even though they were legal, because they were afraid of the possible repercussions from the United States. Many large domestic firms found an alternative route, such as through Dubai, to maintain business with Iran. However, small and medium-sized enterprises (SMEs) were unable to make similar adjustments and were forced to stop contracts.

If the South Korean government continued to trade with Iran, according to CISADA, the United States would likely have retaliated. As a result, South Korea would likely have given up a portion of the U.S. market and would have faced a different set of economic troubles. Thus, regardless of whether it decided to adopt or reject sanctions on Iran, Korea would have faced certain economic loss. As a result, the most realistic calculation for Korea was to comply with the UN resolution to show its global responsibility and to maintain a strong U.S.-ROK alliance.

V. CONCLUSION: LIBERAL BUT REALISTIC

In order to minimize the cost and maximize the benefit, the government should provide relief measures for domestic firms that are suffering from the sanctions. Measures already taken to alleviate economic shocks are largely two-fold. First, the Korean government opened *won*-denominated accounts in two banks, namely Woori Bank and Industrial Bank of Korea (IBK) (see table 1). The *won*-denominated account procedure can be explained in a simple way: the Iranian Central Bank opens the *won*-denominated accounts in Korean banks so that Korean firms can put money in those accounts and Iranian firms can withdraw money from there, and vice versa. Since most of transactions through Iranian banks are blocked by the UN resolution, South Korea and Iran developed an alternative method to clear their transactions legally. Both MOFAT and MOSF highly appreciate the opening of the *won*-denominated accounts, describing it as a win-win strategy. With these accounts, firms can legally continue their activities with Iran, and the government can check the South Korean–Iranian transactions that have been opaque. Park Yong-joon, the director of foreign exchange business at Woori Bank, said that Woori Bank first opened the *won*-denominated account on October 1, 2010, and the major domestic companies such as SK and Hyundai Oil Bank started to deposit money in those accounts starting October 18. On October 26, a *won*-denominated credit of 8.6 billion *won* (approximately $6.2 million) came into Korea from Iran through the account.

Second, on August 25, the South Korean government announced a financial rescue plan for companies that may have been adversely affected by sanctions on Iran. Under the plan, the government provided small firms with 18-month rollovers on maturing loans. Previously this rollover was only six months. It also offered new loans of up to 500 million *won* for three years at low interest rates. An official at the financial regulating body said the rescue plan should be seen as a gesture of goodwill to Iran. "Its message is that the Korean government is helping firms doing business with Iran, which are struggling not because of Korea's own sanctions but because of sanctions imposed by other countries." However, those measures have little influence on small firms as there was no way to compensate them for critical lost business. It appears that companies have relied more on the *won*-denominated account than on the financial aid measures.

The government should develop further measures to recover trade between the two countries and revitalize domestic SMEs. The Ministry of Knowledge Economy claimed on August 26 that it will provide export support measures aimed at SMEs, but they have not been implemented yet. Export support measures such as the Entrepreneurship and Small Business Development Fund and the Fast Track program—rapid assessment of export insurance and accident claims—should be taken into consideration. Director Park from Woori Bank also suggests permitting a greater variety of transactions with Iran, including transactions such as transferring students' expenses, humanitarian aid, and dealings between embassies.

In conclusion, South Korea's sanctions on Iran were a successful approach to apply liberalism based on realistic calculations. Realistically, South Korea partially lost the Iranian market due to its sanctions on Iran. However, there are several factors that mitigate the actual damage. First, due to the impact of the UN Resolution and CISADA, Korea firms and banks were already losing market share even prior to the Korean government's announcing restrictions. Regardless of the South Korean sanctions, a substantial degree of loss occurred domestically. Second, the *won*-denominated accounts in Woori Bank and IBK allowed normal transactions between the two countries starting in October. In addition, South Korea also prevented the possible loss of the American market. In sum, the South Korean economic loss from imposing sanctions is less significant than it appears. The most significant loss can be attributed to the Chinese strategy of overtaking South Korea's dominant position in the Iranian market.

From the liberal perspective, South Korea's decision marks a victory. Korea proclaimed that it is a supporter of nonproliferation despite the economic repercussions. At the expense of its sacrifice, Korea firmly held the alliance, showed global responsibility, and experienced greater inclusion into the international community. As a result, the calculation behind the South Korean sanctions on Iran turned out to be both liberalistic as well as realistic.

The Lightbulb or the Bomb? The Politics of Spent Nuclear Fuel in South Korea

By Jeannette Lee

I. INTRODUCTION

Flip on a light switch anywhere in South Korea and chances are good that the glow from the bulb is powered by nuclear energy. The peninsular country is one of the most prolific nuclear fuel producers in the world. In a mere three decades, 20 nuclear power reactors have sprung up along the coastline from Ulchin on the East Sea to Yonggwang in the west. Together these reactors power the four nuclear plants that account for nearly 35 percent of domestic electricity.

Yet, the ROK's nuclear energy future is uncertain. With a population of 50 million and a total area equivalent to the state of Indiana, South Korea faces a dearth of sites in which to store the unavoidable and hazardous byproducts of nuclear power generation. The government estimates that by 2016, the storage pool for radioactive waste, known as "spent fuel," at its Kori plant near Busan will have reached maximum capacity. If the adjacent nuclear plant cannot find another domestic storage facility that will accept its fuel, it will have to shut down. Officials at the Korea Atomic Energy Research Institute (KAERI) estimate that pools at three other nuclear plants will reach capacity within the next decade. The dangerous nature of spent fuel precludes the option of exporting the material. The risks to global nuclear security and the financial cost of physically safeguarding the material would simply be too high. Without resolution of the storage issue, the gradual shuttering of plants could seriously debilitate the ROK's nuclear industry, according to KAERI scientists.

Several nations, including France and Japan, have reduced the amount of space needed to store spent fuel through "reprocessing," or feeding the radioactive waste back into the reactors. Reprocessing might be a viable option for South Korea, but for the Jekyll-and-Hyde nature of nuclear power, every type of reprocessing technology in current commercial use produces a grade of plutonium waste pure enough to fuel atomic weapons.

Reprocessing is so fundamental to creating weapons of mass destruction that the Republic of Korea vowed to abstain from the practice in a 1992 nuclear agreement with North Korea. Instead, KAERI scientists are championing a new, commercially unproven technology called "pyroprocessing," which they claim will be proliferation-safe. The Barack Obama administration in the United States, however, has expressed reluctance about allowing South Korea to proceed with pyroprocessing research and development. The American position can appear rather puzzling given the history of good relations between the two countries. The United States and South Korea are longtime allies that recently finalized a landmark free trade agreement and are both signatories of the Nuclear Non-Proliferation Treaty (NPT). Since the 1970s they have regularly exercised a bilateral agreement to collaborate on nuclear research in the civil sector. In fact, the pyroprocessing concept that South Korea so badly wants to pursue was first developed by scientists in an American government laboratory and freely shared with the ROK.

This paper will describe how inconclusive science, the North Korea factor, insufficient trust between allies, and an imbalance in economic imperatives underlie the disagreement over whether America should approve South Korea's desire to research and develop the pyroprocessing of spent fuel on a scale that would feasibly lead to use of the technology in the ROK's nuclear power plants. It will ultimately examine the most feasible policy options available thus far and make recommendations to each government on how best to proceed. The topic is a timely one. As of October, the United States had agreed to conduct joint pyroprocessing research with South Korea while the countries work toward revising their civil nuclear pact before it expires in 2014. The research is scheduled to span a 10-year period and will presumably lead the United States to a final decision over whether to allow South Korea to continue its pursuit of pyroprocessing technology. Thus, it is highly possible that the pyroprocessing issue will not be resolved in time to alter the terms of the civil nuclear pact.

II. INCONCLUSIVE SCIENCE AND THE PROLIFERATION QUESTION

On October 25, 2010, a delegation led by Cho Hyun, South Korea's deputy foreign minister for multilateral and global affairs, met with a U.S. delegation headed by Robert Einhorn, special advisor for nonproliferation and arms control at the State Department. The purpose was to begin a formal renegotiation of the bilateral agreement struck in 1972, and amended in 1974, concerning the cooperative development of peaceful nuclear energy technologies and applications.

South Korea sees the renewal of the agreement, which expires in 2014, as an opportunity to secure an amendment that would allow it to research and develop pyroprocessing technology. The United States has not staked out a firm position, but so far appears less than convinced about the wisdom of such an amendment. South Korea has no choice but to accede to U.S. demands; if the agreement lapses, South Korean firms would have to halt their plans to continue reactor-building with U.S. partners, both in Korea and abroad. The agreement is crucial for the continuation of South Korea's nuclear industry. It lays out the prices, quantities, and other terms for enriched uranium shipments into South Korea, and its language indicates that the ROK's nuclear industry would not be nearly as advanced as it is today without the approval and assistance of the United States.

U.S. negotiators signaled a degree of open-mindedness by agreeing to begin preparing for a decade-long joint study of spent-fuel disposal options, "including pyroprocessing." The U.S. commitment to participate in such research, which will happen in conjunction with the negotiation process, will give South Korea the opportunity to make its case for the technology. The research is warranted because pyroprocessing is a nascent technology and no one can say for sure whether it differs all that dramatically from reprocessing. However, the study will last for ten years, indicating that the United States is in no hurry to change the terms of the civil nuclear pact.

The vastly simplified description of reprocessing goes something like this: uranium, plutonium, and, sometimes, other radioactive elements are separated out from spent fuel and fed back into a facility to generate more electricity. This very same process of separating plutonium was originally developed and used to build atomic weapons, which is why nonproliferation experts oppose it. Pyroprocessing is supposed to eliminate the problem of separating pure plutonium by extracting from the spent fuel plutonium mixed with uranium and other heavy elements—rather than pure plutonium—and feeding them all back into the reactor. The United States (as well as nonproliferation activists in South Korea) argues that it is still very easy to separate pure plutonium from the mix. Because pyroprocessing is a relatively new idea, the proliferation dangers it poses are still open to interpretation. And so, where South Korea sees lightbulbs, the United States sees the bomb.

Without conclusive findings, the science of pyroprocessing is currently an instrument of politics. On the South Korean side, officials argue that the plutonium product from pyroprocessing is simply not pure enough to produce weapons of mass destruction. In an op-ed in 2009, Park Seong-won, a former vice president at KAERI, went so far as to assert that pyroprocessing is "proliferation resistant" and "differs completely from conventional spent fuel reprocessing." To further distance the two technologies from one another, South Korea insists that the correct synonym for pyroprocessing is "recycling" spent fuel, not "reprocessing." Taking the environmental analogy even further, they assiduously emphasize the untapped potential of pyroprocessing as a way to check the ROK's steadily increasing greenhouse gas emissions and its heavy dependence on hydrocarbons.

The Obama administration has made no official pronouncement regarding pyroprocessing, but various American nuclear policy experts say the administration favors the following viewpoints: pyroprocessing is no different from reprocessing, and South Korea possesses the nuclear infrastructure and expertise to extract weapons-grade plutonium from the pyroprocessing product fairly easily.

Given that even the most indisputable science is vulnerable to political controversy, it is not surprising that the lack of white-coat consensus regarding pyroprocessing leaves ample room for a wide range of views. But the United States and South Korea are not choosing opposite sides simply because the scientific void allows for it.

III. THE BOMB: STRONG BILATERAL TIES DO NOT ASSUAGE U.S. SKEPTICISM

The Korean War, fought in the early 1950s, forged what the United States and South Korea termed a "blood alliance" between the two nations. In practical terms, this has translated into a highly coordinated military relationship, with North Korea as the common and most worrisome enemy. South Korea has also sent troops to take part in U.S. war efforts in Iraq and Afghanistan. In addition, the two nations share common political systems and in 2007, signed a free trade agreement. The close bilateral ties, however, have not been enough to sway the United States in the pyroprocessing debate.

For one thing, the United States prioritizes nuclear disarmament, nonproliferation, and security above its bilateral relationship with South Korea. America's crackdown mentality regarding nuclear bombs and the materials used to make them naturally shifts its policy focus toward the threat aspect of reprocessing. The United States places a very high priority on preventing antagonistic states and nonstate actors from acquiring the specialized chemicals and other materials necessary to engineer nuclear weapons. The law of probability underpins the U.S. argument for minimizing the reprocessing of nuclear fuels: the more plutonium is recovered from spent fuel and the more widely that plutonium is distributed throughout the world, the greater the risk of its diversion to states that do not have nuclear weapons. South Korea's proximity to the antagonistic nuclear state of North Korea makes America all the more cautious. American administrations tend to believe that allowing South Korea to develop pyroprocessing would make North Korea and Iran more resistant to dismantling their nuclear programs and could cause unease in the region if China and Japan suspect South Korea of pursuing weapons.

The strength of the alliance represents no guarantee, from the American viewpoint, that South Korea will quash any ambitions to establish a nuclear arsenal. Other countries have already used reprocessing technology to attain nuclear status, against the wishes of the United States. The most notorious case involves India. Once upon a time, the United States actually encouraged other countries to reprocess spent nuclear fuel. Under the "Atoms for Peace" program of the 1970s, the United States transmitted reprocessing capabilities to India, which used the resulting plutonium to explode its first atomic bomb. (The spin doctors in New Delhi called it a "peaceful nuclear explosion.") North Korea's development of nuclear weapons can also be traced to reprocessing in nuclear power reactor plants. And a U.S. government report from 1993 warned that Israel, which is highly secretive in regard to its nuclear arsenal, likely possessed "plutonium derived from a secret reprocessing facility."

South Korea, for its part, is not guiltless. The occasional surfacing of nuclear ambitions in Seoul also explains the Obama administration's wary stance. South Korea secretly began a nuclear program in the mid-1970s, but had progressed no further than the preliminary stages when the United States discovered it and convinced President Park Chung-hee to abandon it. At the time, South Korea had intended to use the facilities in its young civilian nuclear power program to paper over its effort to develop a weapon. In 1982, South Korea separated a small amount of plutonium from irradiated depleted uranium. Then, in 2004, Seoul admitted to the International Atomic Energy Agency that its scientists had secretly enriched uranium and purposely concealed the information from international inspectors. (Researchers had separated uranium-235, the isotope necessary for atomic weapons, from heavier uranium-238.) South Korea carried out the experiments despite signing both the Nuclear Non-Proliferation Treaty of

1970 and an agreement with North Korea in 1992 to rid the peninsula of nuclear weapons. The ROK's activities have, unsurprisingly, caused enough skepticism in the Obama administration to question South Korea's reasons for pursuing pyroprocessing.

Aside from its own doubt regarding the ROK's motives, the United States believes North Korea would respond unfavorably should the civil nuclear agreement allow the South to pyroprocess. North Korea has exhibited jitteriness in the past when it has felt that South Korea has overstepped its bounds in the nuclear technology arena. Based on this behavior, American nuclear policymakers foresee the following scenario: pyroprocessing in the South would produce a stockpile of weapons-grade fissile material south of the 38th parallel and stoke paranoia in the North that South Korea is developing nuclear weapons. Feeling threatened, North Korea would then cling to its weapons program with even greater tenacity, and denuclearization talks would go nowhere.

Indeed, Pyongyang harbors long-held suspicions regarding the ROK's nuclear weapons aspirations. The South Korean revelations to the IAEA in 2004 reportedly derailed the George W. Bush administration's efforts to negotiate with Iran and North Korea over abandoning their nuclear weapons programs. Responding to the findings, a spokesperson for the North Korean Foreign Ministry said that Pyongyang "can never sit at the table to negotiate its nuclear weapon program unless the truth about the secret nuclear experiments in South Korea is fully probed." The Bush administration had actually been partnering with South Korea to conduct pyroprocessing research in the mid-2000s, but stopped in 2006, reportedly because the research was a sticking point in denuclearization negotiations with North Korea. The United States appears unlikely to budge on this point. "It is difficult to imagine that the United States would agree to South Korean pyroprocessing until the North Korean nuclear issue reaches a satisfactory resolution," Fred McGoldrick, a former chief U.S. representative to the International Atomic Energy Agency, wrote in 2009.

America must also consider the fact that the ROK's other regional neighbors would prefer South Korea to remain a nonnuclear state and would likely voice some dissent should the United States allow South Korea to proceed with large-scale pyroprocessing research. The civilian side of the nuclear industry is growing in East Asia and complicating the relationships between states in the region. Japan is a nonnuclear state but carries out reprocessing. China possesses nuclear weapons capabilities and is researching reprocessing. The ROK's neighbors could interpret its push to pyroprocess as a roundabout way to develop latent nuclear capabilities, thus complicating U.S. relations with every other country in East Asia. “China, Japan, and North Korea would be deeply suspicious of a decision by South Korea to reprocess,” said one U.S. nuclear expert.

IV. THE LIGHTBULB: SOUTH KOREA’S BID FOR ENERGY INDEPENDENCE

Despite living under immediate threat of nuclear destruction, South Korea, for a variety of reasons, has embraced the upside of nuclear energy far more readily than has the United States. South Korea considers the development of homegrown nuclear power generation essential to tempering its heavy dependence on energy imports, to growing its economy, and to reducing greenhouse gas emissions. Unlike the United States, South Korea seems to believe that any regional tensions caused by pyroprocessing can be managed or overcome.

Energy consumption in South Korea has closely tracked the upward trajectory of its economy. Four decades ago, GDP per capita was comparable to the poorer countries of Africa and Asia, but by 2004, South Korea had become one of the world’s largest economies. Rapid growth has transformed South Korea into the tenth-largest global consumer of energy products, almost all of which comes from abroad. Domestic energy resources are practically nonexistent in South Korea. Natural gas fields number exactly one, and the country has no proven oil reserves. It produces only a small amount of fairly low-quality coal.

As a large energy importer, South Korea is extremely vulnerable to volatility in global energy markets. The economic havoc wreaked by the Arab oil embargos of the 1970s instilled in the country a sense that self-reliance is crucial to the security of its energy economy. Nuclear power is the only kind of energy South Korea can currently produce in amounts large enough to keep pace with economic growth and provide a buffer against oil-price spikes. South Korea also views nuclear energy as critical to reducing the country’s greenhouse gas emissions, which were the ninth-highest in the world as of 2008. Since its first nuclear plant opened in 1978, South Korea has grown its nuclear generation capacity into the sixth-largest in the world, according to the U.S. Energy Information Administration. Domestically produced nuclear power makes up 14 percent of the ROK’s total energy mix, and Korea Hydro and Nuclear Power Company, which operates every nuclear plant in the country, intends to build another twelve reactors by 2022. Despite the fact that it imports all the uranium used to fuel its nuclear plants, the government considers nuclear power South Korea's "only reliable domestic energy resource." The market for uranium is highly volatile. For example, today prices range between $40 and $60 per pound, down from $138 per pound in 2007.

In the past 30 years, South Korea has transitioned from being a net importer of nuclear power plant technologies to exporting design technologies and core nuclear power plant equipment, including nuclear reactors and steam generators. Eager to increase its comparative advantage, South Korea has stated its intent to capture 20 percent of the world market for nuclear reactors by 2030. "The nuclear power-related business will be the most profitable market after automobiles, semiconductors, and shipbuilding," the Ministry of Knowledge Economy stated in a 2010 report. If successful, South Korea would become the third-largest nuclear exporter in the world, behind the United States and either France or Russia. Target markets include the United Arab Emirates, Turkey, India, Jordan, South Africa, China, and Vietnam. South Korea's prospects appear promising. It recently bested leading U.S. and French firms to win its first major nuclear export agreement: a four-year, $20 billion deal to export reactors to the UAE. Backed by the national government, the ROK consortium, led by Korea Electric Power Corporation, reportedly offered a better price and more aggressive construction schedule than did competitors. Underscoring the importance of the contract to South Korea, President Lee Myung-bak flew to Abu Dhabi during the award deliberations and later attended the signing ceremony in December 2009 with UAE president Sheikh Khalifa bin Zayed Al Nahyan. South Korea also won a $132 million contract in 2010 to construct a research reactor in Jordan.

The ROK's economic and energy security interests in the nuclear sector are thus driving its side of the pyroprocessing debate. Like the United States, it wants regional stability, and good bilateral relations, but domestic energy imperatives weigh heavily in its calculus. In order for its nuclear export industry to thrive, Seoul argues, the United States must allow it to conduct research and development on a variety of peaceful nuclear technologies, including pyroprocessing. An October 2010 editorial in the *Korea Herald* espoused this view and pointed out that South Korea "is the only player among the countries capable of exporting nuclear power plants that lacks the ability to reprocess spent fuel." South Korea is also hoping to expand its nuclear technologies to power desalinization plants and is studying the feasibility of building a nuclear plant in Indonesia that would produce both potable water and electricity.

Domestic political pressures also play a role. Although officials from KAERI say there are no polls that confirm the claim, ROK officials cite public opposition to expanding spent-fuel storage sites as a reason for pursuing pyroprocessing. Citizens tend to oppose any plans to hold spent fuel in above ground or subterranean facilities because they believe such facilities are hazardous to human health and the environment. Negative attitudes toward nuclear storage facilities tend to drive down the value of surrounding real estate. It is also important to note that an anti-nuclear activist community does exist in South Korea, but has been largely ignored by the Lee government, which has renewed the nation's emphasis on nuclear power and made it a key part of its energy policy.

The domestic stakes are high enough to put South Korea on a different track from the United States in the pyroprocessing debate. South Korea and the United States have no quibble over the goals of ensuring regional stability, minimizing the proliferation of nuclear weapons, and maintaining a healthy bilateral alliance, but the ROK's expansion of its self-reliant energy policy lies beyond the scope of U.S. interests. South Korea thus faces the quandary of having to balance the preferences of its most important military ally with securitizing its energy supply.

V. NUCLEAR CHIAROSCURO: BALANCING THE LIGHT AND DARK ASPECTS OF ATOMIC ENERGY

The mere existence of an alliance cannot, of course, prevent disagreement and doubt over pyroprocessing, but the bond between the two countries nevertheless functions as ballast in the debate. Military and economic ties, along with the general culture of cooperation between the two nations, ensure that the dialogue will remain civil. As the deadline for renewing the nuclear agreement nears, the two nations have begun to draw upon the alliance to fashion a resolution that satisfies both sides.

For South Korea, this means referencing the alliance to remind the United States that it is trustworthy and that its pyroprocessing research would be intended solely to minimize the proliferation risk caused by reprocessing spent fuel. As one ROK scientist put it: "It doesn't matter whether we have the ability to make a nuclear weapon or not. What's more relevant is whether South Korea would actually make the nuclear weapons."

South Korea points to the fact that six countries—not all of which have as strong an alliance with America—already reprocess their spent fuel and as a result are producing enough weapons-grade plutonium each year to fuel thousands of weapons equivalent in power to the bomb dropped on Nagasaki. (Those countries are Japan, France, the United Kingdom, Russia, India, and the Netherlands.) China, meanwhile, is researching a pilot reprocessing program. Moreover, the United States historically has allowed states to build their reprocessing programs, and even gone so far as to assist them, despite the potential negative ramifications for global nonproliferation. In 1988, the United States ratified an agreement authorizing Japan to reprocess spent fuel and use plutonium commercially, knowing that doing so "may have implications for future agreements between the United States and other countries that use nuclear materials of U.S. origin." One U.S. official said, presciently, that the Japan deal "set a bad precedent for North and South Korea that will complicate U.S. discussions on reprocessing with them." South Korea has indeed been sensitive to the inconsistency of U.S. nuclear policy. Japan's reprocessing program "has been a major source of suspicion and envy in South Korea," according to one American nuclear nonproliferation expert. More recently, a U.S. deal with India has presented South Korea with another example of American double standards. In 2008, India and the United States finalized an agreement formulated during the Bush administration that gives India advance consent to reprocess nuclear material of U.S. origin at a new national facility. The India deal gives South Korea an especially solid argument for winning an amendment in the civil nuclear agreement to allow it to research pyroprocessing. Here is why: aside from its 60-year history as a U.S. ally, South Korea is a signatory of the NPT, along with 186 other states. In contrast, India has refused to sign the NPT and only recently, in 2005, signed an alliance agreement with the United States.

As negotiations have unfolded over pyroprocessing, South Korea has presented the United States with evidence of its lack of nuclear weapons ambitions and reminding America of the longstanding ties between the two countries. The ROK argues that the pursuit of weapons of mass destruction would jeopardize its trade relationships by angering the consumer nations that contribute to its positive trade balance. China, the United States, and Japan, none of whom wants to see a nuclear-armed South Korea, are the three largest consumers of ROK semiconductors, telecom equipment, cars, and other exports. Recently, an official from the Korean Institute for National Unification (KINU) told American nuclear experts and government officials that "if we decide to go nuclear, we will anger the international community and they will impose sanctions and other punishments." He also noted that Seoul "realizes our energy and nuclear security will be halted if there is a proliferation issue." The same official said that the upcoming international nuclear summit, which will be hosted by Seoul in 2012, is further evidence that South Korea "stands on the front line of stopping nuclear terrorism" and will "create conditions to strengthen and solidify our alliance." Seoul also affirmed its stance against nuclear proliferation at a conference in March 2010, where government officials vowed that South Korea "actively supports the move towards a nuclear weapons free world" and "fully upholds international efforts to revitalize the NPT regime." The Lee government has made sure to distance itself from advocates of "nuclear sovereignty," who argue that recent nuclear tests by North Korea justify the ROK's development of its own nuclear weapons. Pyroprocessing advocates classify the technology as "peaceful nuclear sovereignty" to emphasize that weapons production is not the end goal.

South Korea has also moved to directly address its recent nuclear weapons infractions. South Korea argues that its undeclared uranium enrichment and plutonium separation activities discovered by the IAEA in 2004 were relatively minor and "had nothing to do with systematic efforts to develop nuclear weapons." The experiments "were conducted by a few scientists out of 'scientific curiosity,'" and "all related equipment was destroyed." The government said it cooperated fully with the IAEA's inspection and "took measures to prevent similar incidents from recurring." Ultimately, the IAEA board of governors concluded that South Korea deserved nothing more than a verbal rebuke. Following an investigation, the IAEA announced that the ROK's failure to report its activities was "of serious concern," but noted that "the quantities of nuclear material involved have not been significant."

Recognizing that North Korea's nuclear aspirations pose a major impediment to its pyroprocessing goals, South Korea has offered to help the United States in encouraging North Korean denuclearization. Unlike the United States, South Korea seems to believe that developing the ROK's pyroprocessing capabilities and convincing North Korea to stand down from its nuclear weapons program are not mutually exclusive goals. At a joint U.S.-ROK nuclear energy workshop in December 2010, a KINU official stated, somewhat naively, that the international nuclear summit, which Seoul is scheduled to host in 2012, will intimidate North Korea into reconsidering its nuclear weapons buildup. South Korea also seems to think that bulldozing more money into North Korea will help to do the trick. "It is important to convince North Korea that nuclear weapons do not help its security," the government said in a statement in 2010. "South Korea is willing to offer massive economic aid (to the North) to help economic development and social stabilization."

Aside from agreeing to host the nuclear summit, South Korea has already begun to take on new global nonproliferation commitments and is encouraging other countries in a more forceful manner to promise not to engage in enrichment and reprocessing. Its imposition of sanctions on the nuclearizing state of Iran is tangible evidence that it is trying to win American trust in the nonproliferation arena.

South Korea, then, is taking full advantage of the alliance in its bid to compel the United States to amend the nuclear agreement. The United States, however, has been less candid over its desired policy. As the dominant member of the alliance, the United States will ultimately decide what sort of nuclear research South Korea can pursue. Its options range from turning South Korea down flat to agreeing to the amendment and allowing the ROK to go ahead with research, unimpeded. The decision to recommence joint pyroprocessing research indicates that the American side is keeping all options open, as it has yet to settle on a final position.

VI. POLICY SUGGESTIONS: JOINT RESEARCH, OTHER STORAGE, OTHER ENERGIES, AND CONSIDERING NORTH KOREA

Decisions about how to source energy are usually domestic, but the dual nature of nuclear power demands global oversight and consensus. South Korea's domestic energy and economic goals must be weighed within the context of international nuclear security, but neither should the ROK be forced to relinquish an inordinate amount of sovereignty over its energy policy. With the United States holding so much control over the future of South Korea's nuclear energy industry, it has an obligation to do more than say no. Instead, it should help South Korea develop solutions. With these principles in mind, the United States should take full advantage of the alliance by working in tandem with South Korea to solve its nuclear energy problem as a partner, not dictator. Beyond these philosophical reasons, the United States will need to consider the diplomatic ramifications of whatever course it takes. It will not win much goodwill with the South Korean public if it imposes a blanket ban on pyroprocessing research and development. Already, the public is none too pleased that reprocessing is allowed in Japan, but not in South Korea.

The long history of alliance and the language of the civil nuclear agreement makes a joint approach relatively easy in the cultural and logistical senses. But how might the countries update the terms of their nuclear partnership? The United States might require South Korea to explore, or assist it in exploring, alternative options for disposing of nuclear fuel in conjunction with pyroprocessing. The United States itself stopped reprocessing in the 1970s after India's atomic bomb test made obvious the potential for nuclear proliferation. The American nuclear industry has since found alternative ways to handle nuclear waste. When their spent-fuel cooling pools reach capacity, American nuclear plants transfer any fuel that has been submerged for at least five years in the pool to above ground "dry cask" storage facilities, which resemble giant silos. The dry casks themselves are steel cylinders welded or bolted closed with a layer of additional steel, concrete, or other material to provide radiation shielding. Some of the most vocal and influential American nuclear energy experts argue that South Korea should follow the U.S. example and start building dry-cask storage facilities next to their nuclear reactors.

Besides the downside of heightened nuclear proliferation risk, many U.S. experts believe that neither reprocessing nor pyroprocessing is the most economic or efficient way to manage spent fuel. Frank von Hippel, an influential physicist and nuclear policy expert at Princeton University, has written that dry-cask storage costs about $100 per kilogram of spent fuel, whereas reprocessing (as practiced by Japan) costs about $2,400 per kilogram. Von Hippel also calls the storage of spent fuel in pools or containers "a far more proliferation-resistant management strategy." He writes that reprocessing makes weapons-grade plutonium relatively easy to steal because the radiation emitted by the plutonium is not strong enough to penetrate the walls of a portable, water-bottle-sized canister. Three of these canisters can hold enough plutonium for one atomic weapon. A spent fuel rod, by contrast, is toxic enough to kill a human standing a meter away within an hour. The lethality of spent fuel may make it proliferation-resistant, but it is also what pits the South Korean public against the construction of any more spent fuel storage facilities.

South Korea should not completely ignore the option of dry-cask storage, but given the shortage of land available for storage on the peninsula, the United States should give the ROK some leeway in researching options for reusing spent fuel. Spent fuel takes about 300,000 years to decay to the point where it is no longer hazardous, meaning that dry-cask storage would serve as an intermediate, not permanent, solution. At the same time, the United States might encourage South Korea to slow its ambitious schedule of adding more domestic nuclear plants. South Korea plans to bring another twelve reactors online by

2022, with the goal of generating nearly half of the nation's electric power supply from nuclear sources. Whether or not the United States decides to allow South Korea to conduct long-term pyroprocessing research, the process should be completely transparent. Any relevant facilities should be designed, managed, and operated under mutually acceptable nonproliferation conditions and meet agreed safeguards criteria. The collaborative process may allow the United States to discover solutions to some of the impasses encountered by its own nuclear power industry.

Because nuclear energy is so contentious and requires South Korea to constantly be seeking permissions from the United States, South Korea should dramatically expand its development of other, less controversial, fuel options that would give it more control over its own energy policy. South Korea, through its high-tech, shipbuilding, and auto industries, has proven its prowess as an innovator. Thus, it should not be reticent about funneling more money into researching less dangerous alternative fuels, such as solar, wind, and ocean-generated power. Energy efficiency in buildings and vehicles, which the U.S. Department of Energy deems the most effective way to reduce fossil fuel consumption, would also achieve the ROK's goal of relying less on hydrocarbon imports and reduce the need for nuclear-generated electricity. It has already committed $7.75 billion to an offshore wind project, and plans to increase the share of renewable energy in its total energy consumption to 11 percent by 2030 and 20 percent by 2050. South Korea could further bolster its renewable energy sector by developing an export market for such technologies.

Whatever decision the United States ultimately makes, it must take North Korea into account. Leaving pyroprocessing out of the equation, it is unlikely that North Korea will give up its nuclear weapons program anytime soon. The upcoming leadership succession from Kim Jong Il to Kim Jong Un is already causing the DPRK to act more belligerently as the new regime attempts to show that it is not weak. Tensions on the peninsula are higher than they have been in decades, following the Yeonpyeong Island artillery exchange initiated by North Korea in November 2010. In regard to pyroprocessing, the current North Korea situation can bolster both sides of the debate. On the one hand, if North Korea is going to cling to its weapons program regardless, then allowing South Korea to conduct pyroprocessing research will have no effect on the DPRK's actions and should therefore be allowed. On the other hand, the situation is so delicate that neither the United States nor South Korea should risk making it worse. Either way, North Korea will remain highly relevant to the ultimate decision on pyroprocessing.

CHAPTER II: TRADE AND DEVELOPMENT

Another Korean FTA with Latin America: ¿Sí o No?

By Lubomir Sokol

I. INTRODUCTION

Historically, South Korea and Latin American countries have not been major trading partners. However, several political, social, and economic developments in the past 10 years have reshaped their interactions, resulting in a boom in interregional trade. This growth can be attributed to a number of factors ranging from the adoption of neoliberal economic policies in many Latin American countries to Korea's growing need for mineral resources. As a result of this increase in trade, Korea decided to pursue signing free trade agreements (FTAs) with a few Latin American countries in order to avoid the extra costs that both countries incurred through existing trade restrictions. It ratified its first FTA with Chile in 2003 and went on to sign another with Peru earlier in 2010. Furthermore, Korea has expressed interest in signing an FTA with important regional entities including Mexico and the Mercosur trading bloc.

This paper seeks to examine the reasons why South Korea chose to sign an FTA with Chile but not with Mexico. Through a series of case studies, it will assess the discernable differences signing and not signing FTAs has on Korea's economy. Finally, based on these case studies, it will offer recommendations as to whether or not Korea should pursue an FTA with Mexico and other regional powers.

II. THE PROLIFERATION OF FTAS IN EAST ASIA

Following the Asian Financial Crisis of 1997, several East Asian nations, including China, Japan, and Korea, realized the need to address areas of trade and investment in order to sustain their economy's growth and its overall stability. The governments of all of these countries intended to use FTAs to address these mounting issues. There are three other main factors, apart from the crisis, that triggered the proliferation of FTAs throughout the East Asian region. First, was the belief that trade and foreign direct investment (FDI) could help further eliminate "cross-border impediments" and thus deepen the economic connections between nations, including broadening supply chain and production networks. Second, European and North American regionalism worked to motivate countries in East Asia to improve their own economic integration by expanding economies of scale and strengthening bargaining power. The creation of the North American Free Trade Area (NAFTA) and the expansion of the European Union have both contributed to this phenomenon. Finally, the stagnation of the WTO Doha Round presented bilateral FTAs as a suitable avenue of trade liberalization.

The Japanese government thought an excellent way to address its economic integration issue would be through signing FTAs. In 2002, Japan signed its first FTA with Singapore. This FTA went into effect later that year and caused considerable worries for other regional actors, including Korea. These countries believed Japan's first-mover advantage in regard to FTAs would lead to a perpetual cycle of FTA signing by Japan. They feared this proliferation of Japanese FTAs would decrease the competitiveness and market access of their own goods in the world market. In turn, Korea decided its best move would be to launch its own FTA strategy.

III. BACKGROUND OF THE KCFTA

Korea first hinted at signing its first FTA on November 5, 1998, when its External Economic Coordination Committee (EECC) passed a resolution stating that Korea will work towards signing an FTA. Following this decision, the EECC targeted Chile as its first FTA partner because of Chile's complementary industrial structure, its prior experience with FTAs, and the size of its economy. Chile primarily exports natural resources, such as copper, and imports finished goods. The opposite is true for Korea. Prior to the signing of the FTA, Chile's export of nonmanufactured goods constituted nearly 90 percent of its total exports, whereas nearly 85 percent of Korea's exports were manufactured goods. Chile also possessed extensive experience with FTAs. Prior to entering into FTA negotiations with Korea, Chile had already secured FTAs with three other potentially valuable trading partners for Korea including the EU, Mexico, and the Mercosur trading bloc. It was also in the process of signing the Chile-U.S. FTA. Upon completion of the Korea-Chile FTA (KCFTA), Korea believed it would be able to use the knowledge gained from this agreement in negotiations with other, strategically more important, trading partners, such as the United States or Japan. Finally, Chile was chosen due to the small size of its economy. In 2001, its GDP was $66.5 billion compared to Korea's $423 billion. Korea assumed this fact would give it an advantage over Chile in terms of bargaining power. Additionally, Korean officials believed a small complementary economy would provide relatively few problems during the negotiation process.

The first round of the KCFTA negotiations commenced in December 1999, following a joint announcement at an APEC conference earlier that year. The first four rounds were completed by December 2000, and contained about 80 percent of the final version of the KCFTA. Three more rounds of KCFTA negotiations took place that year, however, due to the failure to reach a compromise in regard to tariff elimination on agricultural goods and manufactured goods, the ensuing two years presented serious difficulties for the FTA. South Korea was keen on protecting its domestic agricultural base; specifically it wanted to exclude apples, pears, grapes, and rice from the agreement, while Chile insisted on the abolishment of tariffs on all agricultural goods within a 10-year period. In 2002, talks resumed, producing two additional rounds of negotiations, in which both parties were able to agree to a mutually acceptable tariff concession schedule. By February 2003, the KCFTA was signed by both governments, but only after the language of the agreement was agreed upon. The Chilean Congress ratified the KCFTA unanimously in January 2004. In Korea, the agreement encountered opposition from representatives from rural districts. This development delayed the ratification of the KCFTA three times, until the National Assembly ultimately approved it on February 16, 2004. The agreement was accepted by a vote of 162 in favor of the KCFTA and 71 against it. The KCFTA went into effect on April 1, 2004, at which time 66 percent of Korean exports were able to enter Chile tariff-free.

IV. CONTENTS OF THE KCFTA

The KCFTA was designed to reduce costs of doing business between two highly complementary economies. Korea’s main exports to Chile include automobiles, mobile communication equipment, and electronic goods. Chile’s exports comprise mainly raw materials such as copper and lumber. The agreement embraces manufactured goods, as well as investment, services, government procurement, and intellectual property rights. It also contains five time periods for tariff elimination on Korean exports to Chile: immediate, and five, seven, ten, and thirteen years. Goods featured in the thirteen-year category include a six-year grace period for Chile to completely abolish its existing tariffs. Sixty-six percent of Korean exports were able to enter the Chilean market on a tariff-free basis immediately. By 2014, nearly 90 percent of Korea’s exports to Chile will enter the country without any tariffs. The remaining items are considered to have a comparative advantage against Chile's national industries and were either included in the thirteen-year window or excluded altogether. The extra three years were included in order to give the underproductive Chilean industries more time to improve their competitiveness with Korean goods. Within this category are textiles, footwear, and polyethylene. A small amount of Korean exports remain excluded from the KCFTA, including refrigerators, washing machines, and retreaded tires. The Chilean government believes Korean exports of these items would cause a sufficient distortion in its domestic market and has thus chosen to exclude them.

Chilean exports to the Korean market face six tariff schedules: immediate abolishment, and five, seven, nine, ten, and sixteen years (with a six-year grace period). Nearly 88 percent of Chile's non-copper exports were able to enter the Korean market tariff-free after the five-year mark. Copper cathodes, which make up 41.9 percent of Chilean exports to Korea, however, will not be free of tariffs until 2014. This coincides with the time period when most of the controversial agricultural products such as grapes will be able to enter the Korean market tariff-free.

V. RESULTS OF THE KCFTA

Upon the enactment of the KCFTA in 2004, Korea's trade with Chile realized a sudden surge in volume. Overall trade between the two countries increased nearly four-fold from 2003 to 2007. Korea's exports to Chile rose from $698.6 million in 2003 to over $3.1 billion by the end of 2007, while its imports climbed from a level of $1.1 billion in 2003 to $4.2 billion in 2007. The previous amount exported to Chile averaged approximately $540 million from 2000 to 2003. Chile quickly became the fifth most popular export location for Korean products by January 2007. However, this tremendous growth rate of Chilean exports to Korea, combined with a substantial increase in the international price of copper over the same period, resulted in a widening of Korea's trade deficit with Chile.

Foreign Direct Investment (FDI) doubled within a year after the KCFTA went into effect but essentially remained relatively insignificant for both sides. After the signing of the KCFTA, there has been a shift in the composition of Korea's exports to Chile. While consumer goods, such as cellular phones and electronics, declined slightly from 23.1 percent to 21.7 percent of total exports;

intermediate goods realized a significant increase, from 53.5 percent in 2006 to 70.5 percent of total exports in 2007. Capital goods such as machinery and equipment declined drastically, amounting to only 7.8 percent of total exports in 2007. While Chilean exports to Korea increased five-fold over the period, they maintained a similar composition throughout. Exports of natural resources, including copper-based goods, represent 80.2 percent of Chile's exports. The rest of its exports are composed of agricultural goods responsible for 1.3 percent of its exports and industrial goods such as foodstuffs, textiles, furniture, and basic chemical products.

As a result of the KCFTA, the market share of Korean products in the Chilean import market rose from 3.0 percent in 2003 to 3.1 percent in 2004 to 3.6 percent in 2005. This highlights the increased competitiveness Korean products have against other countries' goods in the Chilean market.

Investment has also shown a rise after the ratification of the KCFTA. Prior to the enactment of the KCFTA, from 2001 to 2003 both Korean and Chilean investment combined was a measly $6 million. Since the enactment of the KCFTA, the Korean government has funded 107 different projects in Chile totaling $115.6 million. Furthermore, according to the Chilean Embassy in Seoul, investment in the Korean stock market by Chilean private pension funds totaled over $1.2 billion.

The much-feared impact on the Korean agricultural sector has thus far been mitigated by the fact that most Chilean agricultural goods are not set to enter the Korean market tariff-free until 2014. Additionally, Chile typically exports its agricultural products to Korea during the winter in the Northern Hemisphere. During this time there is little to no production of similar Korean products and thus little competition with domestic producers. Chile has also pursued a strategy of diversification with its agricultural exports, targeting many other markets besides Korea. This has prevented a potential flooding of Korea's agricultural market with cheap Chilean exports. Statistically, agricultural products represented only 1.0 percent of the total imports in 2006 and 1.3 percent in 2007, reinforcing the fact that the impact of these goods was extremely limited.

VI. HISTORY OF KOREA-MEXICO TRADE RELATIONS

Mexico's strong liberalization policy started with the signing of the North

American Free Trade Agreement (NAFTA) in 1992 under President Ernesto Zedillo and continued through Vicente Fox's tenure. Following the actualization of NAFTA in 1994, Mexico became a key destination for countries looking to reach the North American market, of which Korea was one. Mexico's trade with Korea increased substantially throughout the decade, and in 1999, it became the top destination for Korea's exports to Latin America. Excluding NAFTA, Mexico managed to be a signatory to 10 FTAs from 1994 to 2001. It is currently the most open economy in the world, having trade agreements involving 41 countries. Nevertheless, in late 2003, due to overwhelming skepticism in Mexico's private sector as to the benefit FTAs offer to the country, then economics minister Fernando Canales declared a moratorium on its FTA agreements. However, the Fox administration then changed its mind and proclaimed that Mexico would be willing to form a Strategic Economic Complementary Agreement (SECA) with Korea. As a result, the Korea-Mexico Joint Experts Group on the Strengthening of Bilateral Economic Relations ("the Group") was formed in April of 2004. The role of the group was to determine whether a SECA would be viable and beneficial to both countries. After several meetings of the Group throughout 2004–5, the Group concluded that a SECA would be a mutually beneficial solution.

In response to the Group's conclusion, three SECA meetings were held throughout 2006. A year-long hiatus followed, and in August 2007, the Calderon administration announced that it had reevaluated its position and expressed its interest to reopen negotiations over an FTA with Korea. The ensuing two rounds of FTA debates produced little substance as the Mexican side was continually worried about the worsening of its trade balance. Mexico believed that a serious trade deficit would develop, similar to the one that formed after Mexico signed its FTA with Japan in 2004.

Another source of contention was agriculture. The Korean side argued for the sensitivity of its agricultural sector and the necessity of safeguards, while Mexico insisted that such actions would exacerbate inequality in trade. Furthermore, according to Kim Chong-sup of Seoul National University, other problematic areas include Korea's steel and chemical exports to Mexico. While these are some of Korea's main exports, Mexico has taken a protectionist stance on them due to strong business lobby opposition. FTA talks broke off yet again, but in 2010, Lee Myung-bak met with his counterpart Felipe Calderon and both confirmed their intentions to restart FTA talks.

VII. TRADE IMPLICATIONS OF AN FTA WITH MEXICO

Unlike Chile, Mexico conducts over 90 percent of its trade with countries with which it has signed an FTA. Mexico's sector structure is similar to that of Chile it mostly exports raw materials such as oil and agricultural products. It imports mostly intermediate, capital, and consumer goods in relatively similar proportions to those of Chile. Although the sectorial makeup in Mexico also includes a significant portion of manufactured goods, nearly all of these are destined for the U.S. market and should be disregarded for the analysis. Korea's chief imports are crude petroleum and machinery, while its top exports are semiconductors, chemicals, and manufactured goods. Overall, the two economies are highly complementary.

The sectorial similarity between Mexico and Chile and the complementary link between the economies of Korea and Mexico led me to choose the KCFTA as the basis of my analysis. One can see the substantial benefits an FTA can have on the economies of both countries through the construction of a simple extrapolation. In order to estimate the growth a potential Korea-Mexico FTA agreement would yield, I took the Korea-Mexico overall trade figure for 2004 ($2.8 billion) and imposed the average growth rate Chile experienced after signing the KCFTA onto this base. Thereafter, I compared this with the growth rate and trade Mexico de facto experienced during this era. According to the WTO, from 2004 to 2009 Korea's average growth rate of overall trade hovered around 9 percent. Even though Mexico experienced an above-average growth rate of 22.1 percent, growth in Korean-Chilean trade during the same period totaled 27.1 percent. This difference of 5 percent per annum, when applied to Mexico's 2003 total trade figure, would result in a 2009 total trade figure of approximately $11.7 billion. Based on this prediction, since 2003, Korea and Mexico have foregone nearly $3.6 billion in total trade by not signing an FTA. I further examined the effect an FTA would have on Mexico's current trade with Korea. By using the aforementioned method and applying it to Mexico's current total trade base of $8.1 billion, I reached a figure of $26.9 billion versus $22 billion with Mexico's previous growth rate. Given these results, the cost of not signing an FTA increases to $4.9 billion in mutual trade by 2014. Additionally, this estimate is a rather conservative one because it factors in the years of the "Great Recession," when global trade declined at an average rate of 12 percent. According to the WTO, global trade is predicted to increase at an average rate of 13.5 percent in 2010—the fastest trade expansion since 1950. If one takes into account that Mexico-Korean trade was increasing at triple the rate of the WTO average before the Great Recession, this only further supports the claim that my previous estimates are indeed conservative.

In my final trade estimation, I decided to correct the data for the Great Recession years of 2008 and 2009. I did so by assuming zero-growth rates of trade during those years and factoring this into the average growth rate for Chile experienced after the KCFTA ratification. This yielded a growth rate of 31.6 percent per annum and an estimated combined trade figure of $32.1 billion by 2014, if Korea and Mexico were to sign an FTA agreement by the end of 2010.

The aforementioned simple extrapolation of growth yields similar conclusions to Cheong Inkyo's calculations in regard to benefits an FTA agreement would pose to both Korea and Mexico. In his computable general equilibrium (CGE) analysis, Cheong determined that Korean exports to Mexico under an FTA agreement would increase by approximately 30 percent, while imports would increase by 25 percent. This would lead to a real GDP growth increase for Korea of 0.01 percent in the short term and 0.03 percent in the long term. Mexico's expected growth in real GDP would be 0.02 percent in the short term and 0.15 percent in the long term. Cheong concludes that a free trade agreement should be signed. He further mentions that trade could further be expanded with increasing trade in final goods and the growing intra-industry trade.

VIII. RECOMMENDATIONS

South Korea's FTA agreements with Chile and Peru were signed, in part, because Korea believed that these agreements would serve as gateways to the broader Latin American market. The Lee Myung-bak administration is now presented with a potential FTA with one of Latin America's largest economies and its largest trading partner in Latin America. Overall trade between Mexico and Korea exceeded $8 billion in 2009. Assuming a Korea-Mexico FTA would yield growth rates in trade and FDI similar to those that followed the signing of the KCFTA, it would be hard to make an argument against the FTA on a purely economic basis.

Moreover, given the current stagnation of the KORUS FTA under the Obama administration in the United States, Korea is still in need of a partner to help it reach the U.S. market. More than 65 percent of its exports to Mexico are intended for re-export to the U.S. market. Although Chile also possesses an FTA with the United States, the NAFTA agreement is more favorable when it comes to the export of manufactured goods, Korea's main export to the United States.

Moreover, given the geographic proximity and the cost of labor, Mexico is much more profitable for Korean exporters looking to reach the U.S. market.

Mexico's current trade deficit with Korea stands at $6.1 billion and declined by over 10 percent in 2009. While Mexico shouldn't disregard the trade deficit issue completely, I believe it shouldn't be overemphasized either. Korea could alleviate Mexico's fears in this regard by addressing the issue from an international trade perspective: Mexico need not worry about its trade deficit as it has a floating exchange rate. This will depreciate its currency, thereby increasing the demand for its outputs and reducing the demand for imports. Alternatively, a large trade deficit would further indicate a stronger Mexican peso. This would naturally give Mexican consumers the ability to buy a larger quantity of Korean goods at relatively lower prices.

Korea should also use its entrepreneurs' serious interest of in Mexico as a bargaining point in FTA talks. Korean FDI in Mexico has continued to climb and increased almost two-fold, from $55.7 billion in 2006 to $160.8 billion in 2008. This FDI has a strong effect on the Mexican labor market, as it provides employment for approximately 40,000 Mexican workers. Moreover, the number of Korean companies based in Mexico has tripled since 2006, reaching 1,400 by the end of 2009. These companies are primarily concentrated in the electronics, steel, and automotive sectors. In addition to the strong existing economic ties between the two economies, Korea should cite evidence from the KCFTA, highlighting the increase in FDI inflows that occurred in the years after the KCFTA went into effect.

If Korea intends to pursue an FTA with Mexico, it should act swiftly and aggressively. Moreover, if Korea has learned something from the KCFTA negotiations, it is that halting talks only gives the opposition more time to mobilize and does little to silence it. During the tumultuous years of the KCFTA several anti-FTA unions joined forces in order to combat the agreement. Among these were the Korea People's Action and Korean Farmers Solidarity, which organized and enacted a massive demonstration of thousands of farmers in front of the National Assembly in November 2003. In order to appease the farmers, the government agreed to a $100 billion package to help modernize Korean agriculture. Although this quelled some of the farmers' protests, most were still left dissatisfied. Moreover, this presented considerable cost in lost trade and FDI to the Korean government, a cost that could have been avoided if such a subsidy package had been presented earlier or if the KCFTA had been signed faster.

Korea does not enjoy the same leverage it possessed with Chile when it negotiated the KCFTA. This is mainly due to the relative importance of Mexico to Korea as a regional partner. Other reasons include the size of the Mexican economy and Mexico's existing trade deficit with Korea. In this regard, Korea should be prepared and willing to make some minor concessions in regard to Mexico's agricultural exports. Korea should look to the Japan-Mexico FTA negotiations, where the same dispute existed, particularly over Mexico's pork imports. In the end, Japan agreed to tariff-free entry of Mexican pork in exchange for a removal of tariffs on Japanese automobiles. Additionally, it was still able to have 50 percent of Mexican agricultural imports exempt from the agreement. Korea could possibly boost the $100 billion allocated towards the modernization of the agricultural sector during the KCFTA in order to appease its politically powerful farm sector. In the end, this may still be a small cost compared to the benefit of increased market share in the Mexican market.

IX. OUTLOOK

Although the state visit by Lee Myung-bak to Mexico in June 2010 produced hope among those in favor of an FTA, the prospects for one remain bleak. The political situations in Korea and Mexico are currently quite different, but look similarly unfavorable in the future. While the Lee Myung-bak administration currently supports a potential FTA and enjoys a majority in the National Assembly, Calderon's National Action Party (PAN) controls only 147 out of 500 seats in the Chamber of Deputies and 52 out of 128 seats in the Senate. The opposing Institutional Revolutionary Party (PRI) has been a fierce critic of Mexico's FTAs and has signaled that it is prepared to vote against an FTA with Korea. The PRI won the 2009 elections for the Chamber of Deputies and is predicted to further bolster its power by winning positions for Los Pinos in 2012. Similarly, Korea is scheduled to have both presidential and National Assembly elections in 2012. It is likely that the strong majority the Grand National Party currently holds in the National Assembly will be considerably eroded, assuming a similar outcome to the 2010 municipal elections. Likewise, it is entirely possible that a candidate from the opposing Democratic Party will win the Blue House in 2012, possibly further hindering a potential FTA.

According to Ko Hee-chae, senior researcher at the Korea Institute for International Economic Policy (KIEP) at this time, a potential Korea-Mexico FTA does not represent Korea's primary bilateral interest. Possible FTA agreements with China, Japan, the United States, and the European Union will be favored over an FTA with Mexico. Simultaneously, Ko believes that the burden currently rests with the Calderon administration in Mexico. He remains confident that if Mexico were to sign an FTA with Korea, there wouldn't be any issues in regard to its confirmation by the Lee administration and the National Assembly.

Cho Seong-dae, chief researcher at Korea International Trade Association, agrees in essence with Ko's assessment, albeit for slightly different reasons. He cites the Mexican business sector's lack of support for the FTA as the main reason behind its current stagnation. He references the business sector's firm opposition to increases in global regionalism and therefore being anti-FTA. Additionally, he mentions that support for President Calderon is low, and until the elections of 2012 there is little chance for change. Cho remains optimistic in regard to the ratification of the KORUS FTA, which he believes will be signed within the next two years. In his opinion, if KORUS is ratified, Korea will no longer need Mexico as an intermediary in order to reach the U.S. market. Cho points out that this will significantly lessen the chances of a Korea-Mexico FTA.

X. CONCLUSION

Korea, like much of East Asia, has taken a turn towards regionalism in the twenty-first century. It did so by pursuing FTAs. It has currently enacted FTAs with three countries directly, Chile, Peru, and Singapore, as well as with two trading blocs, ASEAN and EFTA. Its proliferation of trade with Latin America has been growing, and Mexico remains its largest trading partner in the region, with bilateral trade between the two nations totaling over $8 billion in 2009. While Korea's growth in trade with Mexico has been impressive, it should pursue an FTA as a means to further increase these gains.

An FTA would be the most effective method for spurring further economic and political connections for both Korea and Mexico. Mexico is currently Korea's tenth-largest trading partner, and Korea is Mexico's sixth. Assuming a similar increase in trade would occur upon the signing of an FTA with Mexico, as was the case with Chile, it is predicted that both countries would experience an increase in their economic connection through an FTA. Even under conservative circumstances, the growth in trade between Korea and Mexico should be on average 5 percent greater than the growth realized without an FTA. Furthermore, Cheong Inkyo's CGE analysis shows that an FTA would result in an increase of real GDP in both countries.

Given the current stalemate in the talks with Mexico, South Korea should take into account the costs and benefits of possibly making certain concessions to Mexico. Korea's strongest opposition to FTAs has been in the agricultural sector. This sector has been steadily declining and as of 2003 contributes only about 3.8 percent of Korea's GDP. Assuming its influence will also decline over time, this could favor Korea's bargaining position as it could grant Mexico more concessions in the much-debated agricultural sector. While opposition from the farm sector might wane over time, Korea should also consider the amount of trade it has forgone by not signing an FTA with Mexico up until now. Based on my predictions, this amount will increase, reaching $4.9 billion by 2014. Furthermore, concessions in the steel and chemical industries might be necessary in order to get talks moving. Moreover, Korea should factor the political situations in both countries into its analysis: currently the conservative Grand National Party occupies the Blue House and dominates the National Assembly, making both institutions favorable to signing an FTA with Mexico. Korea will continue to concentrate most of its effort on the KORUS FTA; however, it should be proactive in regard to the potential of a Korea-Mexico FTA regardless of the current improbability of its signing.

Figure 1. Korea's Total Trade with Mexico and Chile

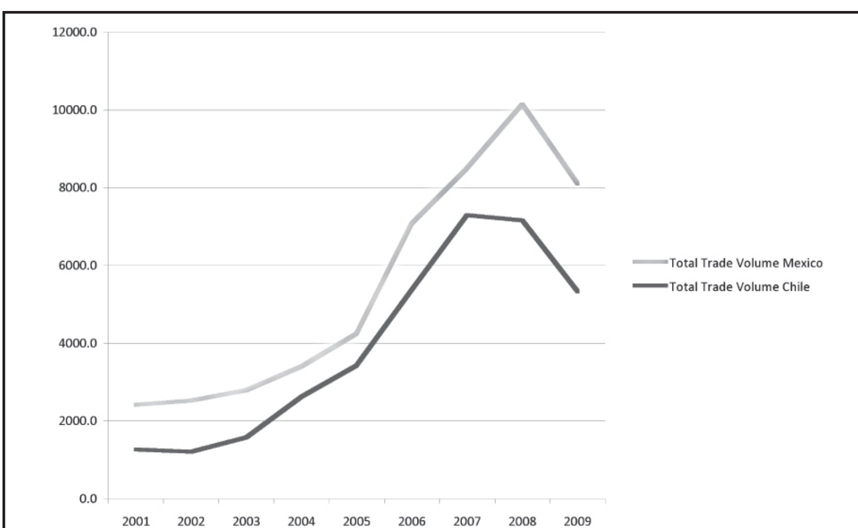
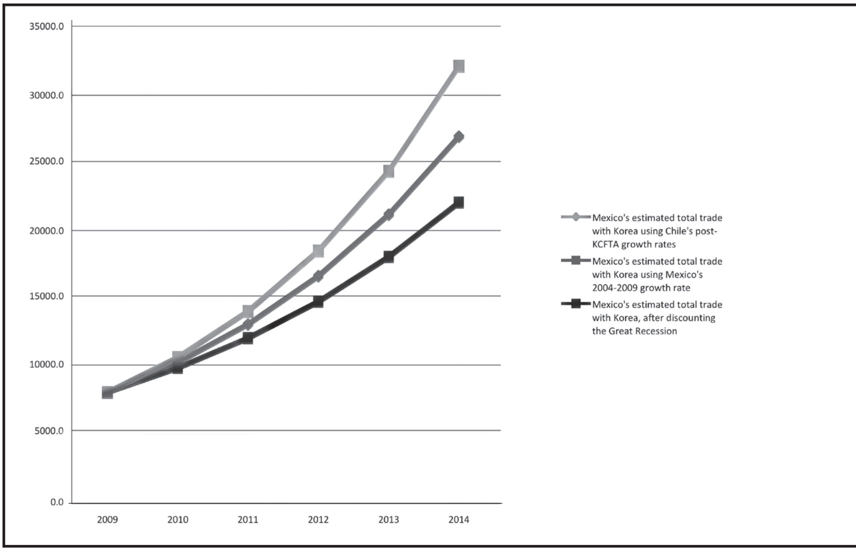


Figure 2. Predictions of Mexico's Total Trade



Korea's ODA to Africa: Strategic or Humanitarian?

By Rob Folley

I. INTRODUCTION

South Korea has been actively expanding its role as a donor on the African continent. In September 2010, in front of ministers from 35 African countries at the third Korea-Africa Economic Cooperation Conference (KOAFEC), Seoul announced a plan to offer $1.09 billion in official development assistance (ODA) to Africa over the next five years, doubling the support it provided from 2005 to 2009. In November 2009, Korea entered into the Organisation for Economic Co-operation and Development (OECD) Development Assistance Council (DAC), marking the end of its half-century role as an aid recipient and the beginning of its efforts to comply with the humanitarian aid goals of the Western donor community. At the G-20 Summit in November 2010, South Korea put long-term development issues such as meeting the United Nations' Millennium Development Goals, raising agricultural production, and building sustainable infrastructure on the agenda, resulting in a new framework for the G-20's future engagement with developing countries, known as the Seoul Development Consensus for Shared Growth. Korea will continue to shape the discussion over ODA in the international community as it hosts the October 2011 Fourth High Level Forum on Aid Effectiveness (HLF-4) in Busan. But while Seoul has taken a leadership role in international development organizations, it also continues to use ODA as a tool to promote national strategic interests in resource security. While reform of Korea's ODA policy and implementation goes forward, its pressing need to secure the energy sources to fuel further economic growth may conflict with strictly humanitarian-based goals.

This paper aims to examine the goals of Korean ODA in Africa and explore the historical, political, and economic factors that shape the balance between Korea's growing dedication to humanitarian-based aid and its need to secure natural resources to further its own economic growth. It concludes that a middle ground can be reached between the two extremes of ODA policy.

II. KOREAN ODA: FROM AID RECIPIENT TO AID DONOR

As the first non-European nation to transition from aid recipient to donor, Korea is unique among OECD DAC members. Its rapid transition is in no small part due to the $12.8 billion in ODA it received from OECD countries after World War II, continuing into the 1990s. This places Korea in a unique position to take a leading role in South-South trade, aid, and investment relations between Africa and other emerging market economies in Asia and South America.

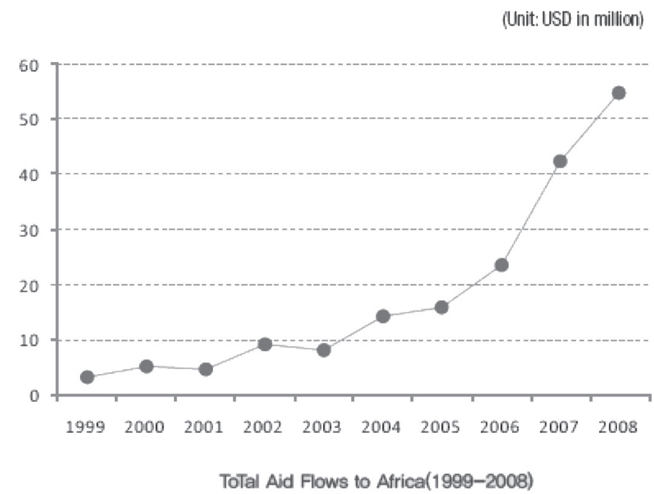
In 2010, Korea's humanitarian-based aid to Africa is growing, but in the 1980s and 1990s, ODA was often tied to national strategic interests and was used as a tool to cultivate support on global issues. In the late 1980s, the Korean government used ODA to gain diplomatic advantage in relation to North Korea as the two struggled to enter the United Nations. In 1990, Korea directed low-interest concessional loans to Nigeria and Ghana as part of a 15-country plan to curry favor from politically influential developing countries for admission to the United Nations. Surprisingly, in this time period North Korea actually had more diplomatic posts in Africa than the ROK, a clear indication of the importance of Africa in Pyongyang's anti-Seoul campaign.

After the end of the Cold War and Korea's entrance into the UN, the driving force behind ODA was to promote greater trade and investment with developing nations. In a November 2000 editorial in the *Korea Times*, Park Kang-ho, then director of the Development Cooperation Division of the Ministry of Foreign Affairs and Trade (MOFAT), appealed for public support of ODA on the basis of promoting economic growth, saying that "providing ODA is not a charity or a gift out of sympathy. Rather we should consider it a strategic partnership." Korea Export-Import Bank President Moon also argued that "Korean enterprises must … survive in unbounded global competition and the [Economic Development Cooperation Fund] will pave the way." During this time, Korea's ODA was channeled to Korea's trading partners and major recipients of foreign direct investment (FDI) instead of to least developed countries (LDCs), and aid was allocated by bankers in Korea Export-Import Bank's credit department instead of aid specialists as was the norm in other OECD countries. In 1998, the neediest LDCs in Africa received only 11.1 percent of Korean aid, and Korea, an OECD member since 1996, had the lowest ODA to GDP ratio of any OECD country. Scholars David Lumsdaine and James C. Schopf argue in the *Pacific Review* that the strategic nature of Korean aid in the 1990s and its low compliance with DAC norms are part of a common pattern in that "they reflected the absence of strong elements in Korean society able to advocate aid on humanitarian and principled grounds." The nature of Korea's ODA was reflected in the underdeveloped nature of civil society in the 1990s. The dearth of NGOs and a lack of volunteerism were evidence of an underdeveloped civil society that may be seen as a legacy of the authoritarian state era of Korea; as late as 2000, 57 percent of Koreans polled agreed that the government's primary concern with ODA should be strategic, with 24 percent actually preferring a reduction in humanitarian-based ODA.

This was all set to change however, as Korea prepared and successfully entered the OECD Development Assistance Committee in November 2009.

III. KOREA'S TWO-PILLAR APPROACH TO ODA

Korea's successful transformation from an aid recipient to a full-fledged member of the OECD's aid committee places it in a unique position to contribute to Africa's development. However, until very recently there was no formal framework in existence between Korea and Africa to facilitate the coordination of ODA. During a state visit to Nigeria in 2006, President Roh Moo-hyun announced Korea's Initiative for African Development (KIAD), which pledged to target all 47 countries in the African Union, plus Morocco, and would focus on five areas: investment in human capital, development of health infrastructure, expertise in administrative governance, information and communication systems, and agricultural communities. KIAD was a watershed for Korea-Africa relations as it was the first time in 25 years a Korean president had visited the continent. It symbolized Korea's growing commitment to use ODA to alleviate poverty and promote sustainable development rather than solely to promote national interests. Four years later, Korea is now a full-fledged member of the OECD DAC and continues to commit to an enhanced role in Africa, with increased ODA to Africa making up a significant part of its goal to increase ODA to 0.25 percent of GDP by 2015.



Source: Korea International Cooperation Agency

Korea's current ODA system is divided into concessional loans and grants, with loans disbursed through the Economic Development Cooperation Fund (EDCF) by Korea Export-Import Bank, and grants handled by the Korea International Cooperation Agency (KOICA), under the supervision of MOFAT. According to a report by the United Nations Conference on Trade and Development (UNCTAD), this two-pillar system has been criticized as fragmented and is in need of consolidation. The International Development Cooperation Committee (IDCC), a supervisory body under the prime minister's office that is working to establish a comprehensive national ODA plan "aimed at streamlining its assistance," is tasked with heading this reform. The latest sign of reform is a comprehensive ODA bill passed in late 2009, which established a legal and institutional framework to guide and coordinate all ODA activities.

Currently, Korea uses three channels to facilitate ODA and promote trade and investment with African countries. The main platform for dialogue is the Republic of Korea-Africa Forum, organized by President Roh to promote the implementation of KIAD. In addition to the forum, Korea established complementary frameworks to promote trade and investment. First initiated in 2006, the KOAFEC is held every two years. The second parallel framework, the annual Republic of Korea-Africa Industry Cooperation Forum was initiated in 2008. These aim to promote stronger investment and ties between the private sectors of Korea and Africa.

In 2009, Korean ODA to Africa totaled $53 million, accounting for nearly 20 percent of total bilateral grant assistance. According to KOICA, Egypt was the primary partner for grant aid, followed by Kenya, Senegal, Ethiopia, and Tunisia. The main sectors for grant ODA were education, health, governance, and rural development.

IV. KOREA'S ROLE IN SOUTH-SOUTH COOPERATION

At the most recent KOAFEC in September 2010, Minister Yoon Jeung-hyun promoted the theme of "RISING Africa, Together with Korea" (Responsiveness to needs, Inclusive policy, Sustainable growth, Integrated economy, and Global efforts), seeking to distinguish Korea's aid policy. Yoon emphasized Korea's unique ability as a recently developed country to be able to meet Africa's development needs, stating:

> From a nation torn apart by harsh colonial rule and devastating war, we struggled as one of the poorest countries in Asia. But through ceaseless efforts, we accumulated extensive knowhow in navigating our way to economic success. We hope to put our experience to good use to help African countries find their way
> to prosperity.

By emphasizing Africa and Korea's shared colonial history and Korea's own recent struggle with poverty, Yoon highlights Korea's ability to provide technical expertise and training in the Korean development model as its comparative advantage in ODA. In this respect, it parallels Japan's notion of aid as support for "self-help," where the recipient country receives aid to fill investment, foreign exchange, and technology gaps to foster sustainable growth.

The IDCC targets project-type assistance and technical cooperation in agriculture as the cornerstone of Korea's development policy for Africa, and 33 percent of gross aid disbursement went to technical cooperation in 2008. The main aid modalities for technical cooperation are the Knowledge Sharing

Program (KSP), which develops technical assistance in diverse sectors including agriculture, human resources, e-government, and export promotion, and the Korean Overseas Volunteers (KOVs) program, which dispatched 938 KOVs to Africa between 1990 and 2008, 16 percent of the total. As part of its Midterm Strategy for ODA, Korea is working to design “tailor-made” development strategies for each country it operates in. In the agricultural sector, the Korean government has actively promoted the New Community Movement (*Saemaul Undong*), an agricultural policy that is credited with the huge increase in South Korea’s rural incomes in the 1970s. In 2004, a pilot *Saemaul Undong* Center was built in Kinshasa, DR Congo, and KOICA, under orders from the IDCC, has plans to expand the initiative throughout Africa.

Not everyone is as optimistic as KOICA that the *Saemaul* Movement and Korean agricultural model will work for Africa. Elijah Munyi, a researcher for African economies at the Korea Institute for Development Strategy (KDS) in Seoul, criticized the movement “as a long shot policy” ill-suited for Africa’s realities, as it requires a level of government institutional capacity lacking in Africa and heavy agricultural subsidization, which today is constrained by the WTO. But the government continues to pursue *Saemaul Undong* as a model that can be adapted to suit Africa’s specific needs. Work moves forward to increase the share of ODA devoted to rural development from its 2008 level of 15.6 percent. Evidence of this commitment is clear in the region, with the Korea Rural Community Corporation (under the Ministry of Agriculture) announcing plans to build a 100,000-hectare agricultural complex in Tanzania, and in July a memorandum with 16 African countries was signed to establish the Korea-Africa Food and Agriculture Cooperation Initiative (KAFACI). As it highlights agricultural development, Korea also has a strategic interest in Africa’s rich endowment of oil, minerals, and land.

V. THE PULL OF RESOURCE DIPLOMACY

The humanitarian goals of Korea’s ODA and the efforts of KOICA to expand into Africa coincide with Korea’s quest to secure energy and other raw materials it needs to fuel and sustain the growth of its economy. President Lee Myung-bak has made energy diplomacy a central part of his foreign policy, and soon after his inauguration in 2008, targeted Russia, Central Asia, Africa, and South America as priority regions for summit-level meetings. Rising energy prices in 2008 provided a sense of urgency to Korea’s ongoing quest to reduce reliance on foreign energy imports, which in 2008, stood at 84 percent of total supply.

Korea relies on oil for 50 percent of its energy needs (much higher than the global average of 38%), and stands as the world's fifth-largest importer. Adding to its vulnerability, around three-quarters of Korea's oil imports come from the Middle East, ensuring its economy would be very affected by an event akin to the oil shocks of 1973 and 1979.

With energy security an imperative of the Lee administration, an editorial in the *Korea Times* during the September KOAFEC meeting highlights how ODA flows would be used to secure natural resources, namely oil:

> The Seoul government seeks to transfer its growth experience to African countries by drawing up a development roadmap that is tailored to the needs of each country. It is ready to finance the projects it suggests with the doubled official development aid. *This in turn will facilitate the advance of Korean companies into African nations.* It is truly a win-win approach. It is hoped that Korea can further expand its support for African nations and solidify its ties with them. The continent's *strategic importance* is growing due to its *rich natural resources* and vast growth potential. (Emphasis added.)

The explicit pairing of aid with strategic goals of expanding Korean trade and investment and securing natural resources is seen as mutually beneficial for Africa and Korea. To facilitate this, Korea has reopened a mission in Cameroon, which it was forced to close in 1998 in the wake of the Asian Financial Crisis, and is actively expanding into oil-rich countries such as Nigeria, Congo, Sudan, and Libya. In May, the Ministry of Strategy and Finance identified Algeria, Ethiopia, DR Congo, South Africa, and Tanzania as "strategically important" countries in its economic cooperation with the continent and plans to fund infrastructure projects in northern and southern Africa, and mining and agricultural investments in eastern and central Africa.

VI. OIL

Securing oil reserves is seen as critical to Korea's continued economic growth. Korea National Oil Corporation (KNOC) has taken its mandate and actively pursued investment in African oil-rich countries. Nigeria, as the world's eighth largest exporter of oil, stands as one of KNOC's most important forays into the continent. Responding to Nigerian President Olusegun Obasanjo's recruitment of Asian national oil firms in 2005, KNOC acquired the rights to two offshore oil blocks purported to contain as much as one billion barrels of crude. In the oil-for-infrastructure deal, Korea would build a gas pipeline with two integrated gas power stations en route, and rebuild the Port Harcourt-Maiduguri railway line. In total, KNOC promised an investment of nearly $6 billion in exchange for the two oil blocks, and according to a Chatham House report, the South Korean government called it "a win-win project where South Korea's technology and Nigeria's resources are swapped." The project did not live up to the high hopes placed on it, however. The Nigerian government revoked KNOC's rights to the oil blocks, citing failure to pay part of the signature bonus, and promptly gave the rights to India's Oil and Natural Gas Corporation (ONGC).

VII. AGRICULTURE

Oil is not the only resource South Korea lacks. As a major importer of grains, food security is a major issue of concern for Korea, and it has been involved in high-profile land investments in Sudan, Madagascar, and Tanzania. With a still highly protected farm sector, in 2008, South Korea was 99 percent self-sufficient in rice and 53 percent in barley, but imported 86 percent of its soybeans and nearly all (99%) of its wheat and maize. The UN Food and Agriculture Organization recommends that each country secure 18-19 percent of its annual grain consumption for its year-end stock to ensure food security. Due to the global shortage and surge in grain prices in 2007-8, Korea was unable to meet this goal, and it set up a government taskforce as well as the Overseas Agricultural Development Forum in 2008 in an effort to cultivate agricultural cropland overseas.

Korea's recent investment in land has received criticism from the media, drawing calls of neocolonialism and sinister portrayals of Korea's competition with other Southern neighbors in a desperate "land grab" on the continent. Korean officials have countered, highlighting the benefit of the agricultural projects for the host countries. In Sudan, Korean firms plan to take advantage of the country's access to the Nile River to grow wheat on 700,000 hectares of land. In Madagascar, the 2008 announcement of a 99-year contract to lease 1.3 million hectares to Daewoo Corporation to grow five million tons of maize and produce palm oil helped to spark a revolution that toppled the government. The new leader, Andry Rajoelina, promptly canceled the contract and is quoted in the *New Zealand Herald* saying, "Madagascar's land is neither for sale nor for rent."

Is ODA following the agricultural investments? It appears the quest for food security is at least in part driving allocation of ODA to the continent. The investment by Daewoo Corporation was solely a private venture, but the Tanzania project that followed it in 2009 was an example of food security tied to aid. The project plan ceded half the land to produce processed goods such as cooking oil, wine, and starch for export to Korea, with the other half going to create a Korean Rural Community Corporation (KRCC)-built “agricultural complex” featuring an agricultural technology center and agricultural export center; upon completion it will rank as the largest single piece of agricultural infrastructure Korea has ever built overseas.

VIII. IS AID TIED TO STRATEGY?

In 2009, the EDCF had concessional loan arrangements in Angola on seven projects worth $222 million. Those represented 4 percent of the total EDCF budget; the next-highest African countries were Tanzania at 3 percent, Mozambique at 2 percent, and Mali and Ghana with 1 percent each. As one of Africa’s oil-rich countries, Angola is a key theater for resource competition among China, India, and other developing countries engaged in energy expansion in the region. That Angola receives such a large amount of ODA is an important sign of how much national strategic interests still factor into Korea’s ODA policy. Angola, a country with a per capita GDP of $8,400 in 2009, is arguably much wealthier than other nations ranked by the United Nations as LDCs. But as Korea looks to *quid pro quo* deals such as the failed oil-for-infrastructure deal in Nigeria, it sends aid to relatively richer resource-endowed countries like Angola. The fact that China has cornered the market in Angola increases the urgency for Korea to find a foothold, and ODA is a powerful tool.

The rise of China in Africa and Central Asia is an important factor in reinforcing the use of aid for commercial interests in Korea. Within the two pillars of Korea’s ODA framework, the *Korea Times* quoted KOICA’s president saying that his agency and the Korea Export-Import Bank are often “at each other’s throats” over allocation of the development assistance budget. KOICA, responsible for grant aid, and the Export-Import Bank, which oversees the EDCF’s disbursal of concessional loans, don’t always have the same philosophy about what the goal of ODA should be. The relatively new emphasis on humanitarian aid in support of the Millennium Development Goals conflicts with a long history in the 1980s and 1990s of using aid solely to promote commercial and strategic interests. In this regard, Korea’s ODA implementation structure resembles Japan’s in the 1990s, during which time the Ministry of International

Trade and Industry focused on ODA as a tool for promoting Japan's economic growth, while the Ministry of Foreign Affairs associated Japanese aid with more traditional social and political factors highlighted by international aid agencies. This internal debate is further compounded by the exponential growth of China's presence on the African continent, which has led to fearful statements such as the one issued by a state auditor of MOFAT and quoted last summer in *JoongAng Daily*. The statement criticized Korea's small number of African embassies (13 compared to China's 42 and Japan's 25) and warned of the "gap in the government's efforts to engage the continent for business opportunities and energy and mineral sources." As China's aid to Africa grows rapidly, its East Asian neighbors feel pressured to counter China's growing influence with their own increases in aid.

IX. CHINA PROMOTES ITS SOFT POWER

China has played an active role on the African continent since 1949, with aid to the region as high as 6 percent in 1971 as China engaged in geopolitical rivalry with the United States and vied for Taiwan's seat in the United Nations. With the first China-Africa Forum in 2000, China switched tacks, using aid as a tool for soft power and to meet increasing demand for natural resources, new markets, and investment possibilities. According to UNCTAD, with $2.3 billion in estimated aid flows to Africa in 2006, China accounts for 83 percent of aid from developing or recently developed countries, dwarfing second-place Brazil, with $96 million, by a factor of 20. China's major focus for ODA in Africa is infrastructure development, with 70 percent of infrastructure aid aimed at Nigeria, Angola, Ethiopia, and Sudan. According to an article in *Development Policy Review* by Peter Kragelund, China bases its aid on principles of mutual benefit, noninterference in other countries' internal affairs, and the equal standard of living of Chinese experts in the recipient country, with the goal of differentiating its aid from other Western donors. It prefers to work on the bilateral level, eschewing multilateral cooperation with other donor countries or agencies, and ties its aid to non-policy conditions (e.g., access to natural resources or the purchase of goods and services by firms in the recipient country). China's ODA policies elicit a broad spectrum of reactions from other donor countries, from fear to praise to condemnation. Its unique status as both a donor and a recipient of ODA frustrates those who call for compliance with DAC standards, and as it is unlikely to renounce its developing status for political and economic reasons, it seems unlikely to reform its ODA policy in the near future.

There are key similarities between Korea's and China's model for aid. Both utilize regular high-level summit meetings as a mechanism to make pledges and commitments, increasing the predictability of aid and providing a built-in monitoring mechanism to ensure commitments are fulfilled. Both also continue to rely on project-based aid as the primary aid modality, and both countries have emphasized the positive hope for technical cooperation on agriculture and climate change as avenues for further development in South-South cooperation.

But China's model for Africa is not realistic for Korea, now a member of the OECD DAC. China is in a unique position, as it is able to use aid to support its commercial interests and natural resource procurement, and its presence in Africa is many times greater than Korea's because it sees Africa as an important market for exports and a source of support on global issues. Its FDI stock in Africa reached $7.8 billion in 2008, compared to Korea's $516 million, which ranks lower than FDI from Singapore, Hong Kong, Malaysia, and India. In 2009, China secured one-third of its oil supply from the African region. By linking official flows with FDI, China uses its export-import bank as a channel for providing financing and promoting trade and investment in ways that Korea as a liberal democracy cannot.

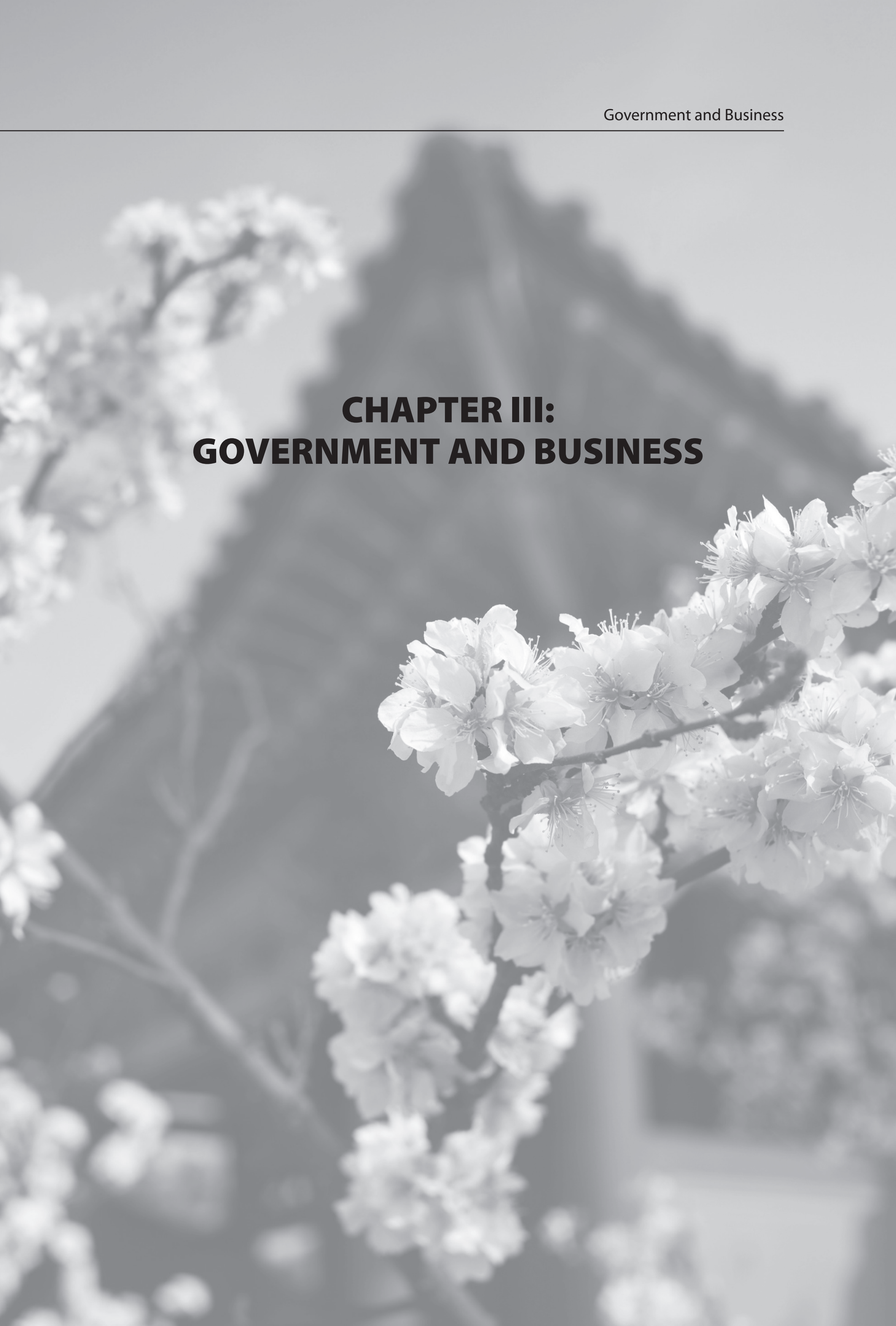
X. FUTURE PROSPECTS FOR ODA: TOWARD A MIDDLE GROUND

In order to examine Korea's role in Africa, it is necessary to understand the debate over reforms in ODA that are currently being carried out in Korea. In 2008, leading up to its formal application to the DAC, Korea commissioned a special review of its ODA policy and institutional framework. The study identified major areas in need of reform, including a low ODA/GNI ratio, a high percentage of concessional loans compared to grants, a high portion of tied aid, regional bias, and a relatively large number of recipients. Korea has taken steps to address these weaknesses and come into line with DAC policies, but these deficiencies are still a problem in its ODA to Africa. With an ODA/GNI ratio of 0.1 in 2009, Korea falls below the OECD/DAC average of 0.48 and the UN target of 0.7. It is important to understand, however, that the large amount of aid provided to North Korea isn't included in official ODA amounts because South Korea's constitution identifies the North as part of state territory, and therefore aid to the North is classified as an internal matter in ODA accounting.

The tension between Korean strategic interests in energy, minerals, and grain must be better balanced with Africa's development needs. Several scholars, including Elijah Munyi of the Korean Institute for Development Strategy, have criticized President Roh's Korean Initiative for African Development (KIAD) as doing little more than paying lip service to Africa's development needs while providing the majority of funding to relatively rich, resource-abundant countries such as Egypt, Nigeria, Algeria, and Morocco. As Munyi recommends, Korea must separate its funding for energy diplomacy from any future development initiatives. In 2009, Ethiopia and Senegal were the only two of the top five recipients of KOICA project grant assistance that were LDCs. Korea must direct a higher percentage of its ODA to LDCs, and aim for a better balance between strategic needs and African development needs. Further, Korea should continue to develop its core strength of technical cooperation as its development "niche." As it does this, however, Korea must ensure its Knowledge Sharing Programs in agriculture are tailored to African needs instead of focusing on dogmatically promoting the Korean development model through *Saemaul Undong* or other initiatives. Finally, Korea should address the transaction costs caused by the three-channel framework it now employs for interaction with the African region—namely the Korea-Africa Forum, KOAFEC, and the Korea-Africa Industry Cooperation Forum—as it places a heavy burden on the already weak human and financial capacity of African countries. One option identified by UNCTAD is to use the New Asia-Africa Strategic Partnership as a joint forum for engagement with region. As Korea streamlines its own channels for aid distribution it should also strengthen support for regional integration within the African region. Targeting aid to regional projects such as regional infrastructure development will reap dividends by reducing transaction costs, boosting trade, and encouraging growth.

As Korea prepares to host the Fourth High Level Forum on Aid Effectiveness (HLF-4) in October 2011, it must work to consolidate its Africa ODA policy and continue to take the lead on implementation of the Seoul Development Consensus at future G-20 meetings. Ongoing reform of its ODA implementation framework will continue to be met with pressure domestically from those who support ODA as a strategic rather than humanitarian tool and may face criticism from those who see a rising China's presence in Africa as a call to ratchet up resource diplomacy. If a middle ground can be reached, Korea can offer its unique technical expertise as a recently developed country to African partners while maintaining a balance with a pressing and real need to secure access to natural resources.

CHAPTER III: GOVERNMENT AND BUSINESS



Korea and the Great Recession: The Effects of *Chaebol* Reform on South Korea's Recovery from the 2008 Financial Crisis

By Kate Chekan

I. INTRODUCTION

While the 2008 financial crisis originated in the United States and Western Europe, it deeply affected East Asia as well due to global economic interdependence. Because of South Korea's reliance on exports and high level of integration with the global economy, the country as a whole suffered from the events of 2008. A number of indicators declined rapidly in what was an abysmal year for the nation's economy. Toward the end of 2008 and at the beginning of 2009, nominal GDP decreased from $928 billion to $821 billion, exports decreased from $433 billion to $374 billion, and the *won* depreciated from 1050 to 1570 against the U.S. dollar. Interest rates were reduced to an all-time low, with the policy rate decreasing from 5.25 percent to 2 percent to keep liquidity in the system.

While South Korea certainly suffered economically from the crisis and in certain ways is still feeling its effects, they also joined China as one of the fortunate nations that was very quick to turn its economy around. GDP growth improved very quickly from -4.5 percent in Q4 of 2008 to 3.2 percent in Q1 of 2009. Other trends also reversed; from December 2008 to January 2010, the KOSPI grew 42.5 percent, the country went from a deficit of $5.8 billion in 2008 to a surplus of $42.7 billion, and exports increased towards their pre-crisis levels.

Scholars cite a number of factors that account for the fact that South Korea rebounded faster than most advanced economies, especially its Western counterparts. This paper focuses on one of the factors that have received less attention: South Korea's *chaebol* reform that took place during the Asian Financial Crisis. Is it possible that the *chaebol* reforms after the 1997 crisis helped Korea's economy rebound faster from the global financial crisis a decade later? If so, what are the most salient features of the reform that helped Korea respond in an effective way? How did they help Korea minimize the adverse effects of the financial crisis and the time needed to turn around the economy? This paper seeks to answer these questions in the context of the reforms that were implemented as a result of the 1997 Asian Financial Crisis. First, it provides brief background information on the pre-1997 activities of *chaebol* and the reforms that followed the Asian Financial Crisis. Then, it analyzes the main features of reforms with a view to assessing whether, and how, they helped put South Korea in a position to thrive after the events of 2008. Finally, the paper identifies some of the gaps in the current *chaebol* system that can potentially impede Korea's ability to sustain the current rate of growth, and concludes with suggestions of measures that can be taken to fill those gaps.

II. *CHAEBOL* ACTIVITIES LEADING UP TO THE 1997 CRISIS

The 1990s: Expansion and Leverage

As early as the 1960s, the *chaebol* played a significant part in the growth of South Korea's economy, with help from the government's favorable regulations that created a "*chaebol*-state symbiotic relationship" that persisted into future decades. During the 1990s, the *chaebol* continued to have a large influence in shaping Korea's financial liberalization, but also contributed to the problems that Korea faced during the Asian Financial Crisis. On the macroeconomic level, South Korea saw an increasingly large current account deficit as well as a loss of price competitiveness in its export market due to the devaluation of the *won*. This led to a need for Korea to gain a competitive edge through aggressive regional and global expansion. Rather than raising more equity to have sufficient capital for these expansion ventures, the *chaebol* chose to accumulate more debt. Taking out loans was easier for the conglomerates than raising equity, because of the decreasing amount of government supervision. They now could take loans out not only from Korean banks, but also from international investors in larger amounts. This increased access to foreign capital markets enabled the *chaebol* to expand further. The *chaebol* always had a history of taking out a large number of loans; but a large problem was also the structure of this debt. By 1997, short-term loans and foreign portfolio investment together accounted for about 68 percent of the country's debt. By that same year, the top five *chaebol* had an average of a 473 percent debt-to-equity ratio. Such large amounts of debt were acceptable when there was an economic boom and the country's businesses were growing, but could cause serious damage to the country's reputation if the *chaebol* were in financial chaos and unable to pay off their loans.

The Hanbo Bankruptcy and Those That Followed: A Warning Sign for the Chaebol

Hanbo Iron and Steel was one of the first *chaebol* to collapse in the 1990s as a result of these risky business practices. The company went bankrupt in January of 1997, just months before the Asian Financial Crisis. Prior to bankruptcy, Hanbo was building one of the world's largest steel mills. The cost of the mill was greatly underestimated, and to add to management's imprudent financial choices, a lack of due diligence on the part of the lenders led to a massive amount of debt that Hanbo was not able to pay when its steel mill was not completed as planned. By the time the company collapsed, Hanbo was $6 billion in debt. The company would not have been able to even turn a profit at that point, even if sales had been at a high point, because their interest payments alone were $580 million a year and their debt was 22 times equity at the time. Even the most highly leveraged companies in Korea at that time did not accumulate debt more than 3.5 times their equity. Hanbo managed to accumulate this massive amount of debt because the bank managers working with Hanbo circumvented the normal loan review process, and the chairman had also added extra incentives to continue providing these bad loans by bribing the company's main creditor banks.

Hanbo was an extreme case of excessive debt and corruption but by no means was an exception among Korean *chaebol* of the time. Many *chaebol* had accumulated an unsustainable sum of debt after years of easy loans and imprudent expansions, and stayed barely afloat so long as they could manage to receive more loans to pay back their debt. After the real estate market collapsed in Thailand, banks were no longer willing or able to extend fresh loans and roll over new ones. Twelve more *chaebol* quickly went bankrupt in 1997, including Sammi, Jinro, Dainong, and Kia.

The Asian Financial Crisis

Economic circumstances worsened for South Korea during the 1997 Asian Financial Crisis; once incredibly optimistic towards Korea's growth prospects, foreign investors began to shy away from Korean ventures, and refused to roll over Korea's short-term loans when asked. Agencies such as Moody's and Standard & Poor's downgraded Korean financial institutions' credit ratings in November 1997. An overall lack of confidence in the Korean government and businesses to pay back what they owed began to surface among the investment community. To make problems worse, South Korea was coming to the close of the investment boom in manufacturing in the heavy and chemical industries that it had enjoyed in the previous decades, making it harder to generate the cash flow needed to pay back these loans. Because the debt problem in South Korea was so severe, the government had no choice but to turn to outside parties for assistance.

III. POST-CRISIS POLICIES

The IMF Bailout

South Korea eventually turned to the IMF, who granted a bailout loan totaling approximately $60 billion. This loan, however, came with a number of conditions, many of which were set forth in the IMF Stand-by Agreement drafted in December of 1997. While the agreement covered a number of aspects of the crisis, such as the forthcoming fiscal, monetary, and exchange rate policies, labor market reform, and trade liberalization changes, the most important provisions for the *chaebol* were those pertaining to their corporate structure, transparency in financial reporting and corporate governance, and massive debt levels.

Regarding the many highly leveraged and fundamentally unstable banks in South Korea at the time, the IMF resolved that for this loan to be given to South Korea, "troubled financial institutions will be closed or if they are deemed viable, restructured and/or recapitalized." During this same month, nine merchant banks were suspended for not meeting certain capital and solvency standards. This was important to the *chaebol* because it restricted much of the reckless funding that led to excessive leverage. Another important provision was that "accounting standards and disclosure rules will be strengthened to meet international practice" so that Korean companies could become more transparent. Even the publicly listed conglomerates in Korea had erratic, if any, disclosure on their financials. Under this agreement, Korean corporations would be subject to independent auditors and would be obligated to provide consolidated financial statements on a regular basis. There is also the issue of corporate governance, which was in dire need of a change among the *chaebol*. There are scholars who believe that East Asian countries, South Korea in particular, suffered more from the crisis than other emerging markets in South America and Eastern Europe because of their unique corporate governance structure. Paul Krugman adds to this by stating that while the crisis in Korea is a result of "private corporate sector profligacy," it was enhanced by the fact that the government gave implicit guarantees of assistance in times of distress that led to the conglomerates' reckless investing. In addition, there were a number of transparency problems when it came to corporate governance. These companies were seen as highly paternalistic, giving personal relationships a priority in business. In addition, *chaebol* generally lacked a sense of fiduciary responsibility; while their sales and overseas expansion were increasing rapidly, they had actually shown very little progress in terms of profit margins, and had very low profitability on average throughout the 1990s, indicating that shareholders' interests were not their primary concern.

The Administration's Response: Further Chaebol *Reforms*

The South Korean government had a generally positive response to the IMF package. When Kim Dae-jung took office in 1998, he met with the legislature to resolve anything that had not been discussed beforehand. The resulting statement was the Five Principles of Corporate Governance. The principles included "enhancement of management transparency, strengthening owner-manager's accountability, elimination of cross-debt guarantees among chaebol affiliates, improving financial structure, [and] consolidation of core business areas." To complement the IMF's reforms concerning reckless lending, Kim addressed the problem of the *chaebol*'s disproportionate leverage. The governing principles stated that the *chaebol* had to reduce their debt to equity ratio to under 200 percent. By 2001, the South Korean banks had 116 companies on a list created by the government of firms that were "recommended for liquidation, sale, or merger" due to their ailing health and overwhelming debt. Part of Kim Dae-jung's reforms also required the *chaebol* to consolidate their "oligopolistic corporate structure," meaning that they had to break their originally large company headquarters into smaller entities so that management could better oversee the firm's activities. By 1999, the *chaebol* completed 80 percent of their restructuring requirements, but the government pushed for quicker action; Kim threatened to "toughen sanctions against its five top conglomerates if they fail[ed] to restructure" by their allotted deadlines. Companies such as Samsung, Hyundai, and LG as a result were split up into smaller, more manageable entities based on their businesses. Combined with the aforementioned IMF guidelines, this wave of legislation began to bring important changes to the South Korean business landscape.

IV. DID THE IMF REFORM AND OTHER POST-CRISIS LEGISLATION HELP?

In the years after the reforms, despite worries that this regulation would cripple the growth and profitability of the *chaebol*, the conglomerates recovered from the Asian Financial Crisis. Even as early as the first quarter of 2002, Hyundai earned a record profit of $300 million, which was up nearly 20 percent from their profits in Q1 of 2001. In the same quarter, Samsung obtained a then-record first-quarter profit of 1.9 trillion *won*. However, as stated earlier, the central question of this paper is to determine, given the IMF's and South Korean government's *chaebol* reform, whether or not this legislation played a role in helping South Korea promptly recover from the 2008 crisis. When looking at the major fundamental reforms that took place after 1997, it is clear that reforms played a significant role in keeping South Korea from being damaged for the long term. It is important to look at each of the main reforms stated above and analyze each one in the context of post-crisis business activity to properly determine the way in which these reforms made an impact on the South Korean economy.

Corporate Structure: Breaking Up the Larger Conglomerates

Prior to 1997, management of the *chaebol* was much more concentrated at the center, and the companies themselves were large entities with leadership that was less connected to the ever-growing firms' operations. This brought with it a number of difficulties that come with overextended businesses, including that of moral hazard; many *chaebol* leaders were convinced by the time of the crisis that their companies were too big to fail. In many instances, this was the case; while the top 30 *chaebol* had an average of 4.2 subsidiaries in 1970, this number ballooned up to 26.8 by the end of 1997, and they were much more likely to move into sectors unrelated to their core business than were their conglomerate counterparts in Japan. These firms were simply too large, and Kim's reforms were meant to take care of this problem by breaking them up into smaller entities. Breaking these *chaebol* into smaller groups improved the quality of their business. According to scholars Lee and MacMillan, empirical evidence has shown that as multinational corporations expand, there is a "positive association between knowledge transfer by parents with foreign subsidiaries and the performance of those subsidiaries," so long as both coordinative and procedural knowledge are transferred from headquarters effectively. The fact that *chaebol* reform required these overextended conglomerates to consolidate a number of their business operations was a benefit as the *chaebol* continued to diversify their geographic reach. As each company established more foreign branches and increased the number of employees overseas, it was important to transfer managerial, operational, and cultural knowledge quickly and effectively; this would be much harder if their product lines were overly diversified and there were far too many different subsidiaries with dissimilar business practices. Better communication comes from a simpler and more coherent business structure, which was one of the major reforms that has benefited the *chaebol* since the 1997 Asian Financial Crisis.

The measures that South Korea took to break down their large and complicated structures have indeed put them in a more favorable position than the United States and Western European nations during the 2008 crisis. Banks and automobile companies in the United States (such as Citigroup and General Motors) were a contentious issue among politicians, economists, and taxpayers because these companies were seen as "too big to fail." As a result, it made more sense for the U.S. government to bail them out (which further angered taxpayers) than allow them to collapse. An analyst at the Korean Institute for International Economic Policy stated that because South Korea had seen the "too big to fail" problem and had taken post-Asian Financial Crisis measures to ensure that these large companies were broken down, large businesses in South Korea did not face the same troubles as those of the United States in 2008.

Decreasing the Amount of Leverage

As an analyst at the U.S.-Korea Institute at Johns Hopkins University School of Advanced International Studies (SAIS) states, the lower levels of debt the *chaebol* had was another factor that stood them apart from their Western counterparts when the 2008 financial crisis took place. As opposed to Korean *chaebol*, which made a point of reducing their debt levels below the 200 percent threshold set by Kim Dae-jung in his Five Principles, U.S. firms had been moving in an opposite direction leading up to the 2008 crisis and thus were in a less fortunate position. For example, in 2004, the SEC allowed the five largest investment banks to reduce their capital reserves; just a few years later, these five banks alone controlled $4 trillion in financial assets, but with very little net equity. Because of this capital structure, when credit sources were diminished in 2008, these highly leveraged firms were not able to refinance their debts, take out short term loans to cope with temporary cash flow problems, or purchase new capital equipment. Korean firms had a significant amount of capital on hand, and thus their firms were less concerned with interest payments and continuing general business operations. According to analysts, many of the *chaebol* had even reduced their debt-to-equity ratios much further than they were supposed to, with many ratios reaching as low as 115 percent.

While most companies, particularly in the West, were on the verge of bankruptcy and facing the possibility of liquidating, Korean *chaebol* continued their expansion plans in the wake of the crisis, and filled the production gaps that U.S. companies had left. Samsung, Hyundai, and LG, for example, were all putting expansion plans into place. In September of 2009, Hyundai announced that it would build a new $600 million car factory in Brazil. In the same month, Samsung made a $5.85 billion cash offer to U.S. memory-card maker SanDisk. While automobile giants such as GM and Chrysler were collapsing, and Japan's Toyota was mired in scandal due to a recall of malfunctioning brakes, Hyundai and its subsidiary, Kia, became more successful. Even though Korean automakers were criticized in the 1980s and 1990s for "shoddy construction" and failure to follow the elements of the "lean production" as was practiced at Toyota, there was nonetheless a surge in post-crisis demand. Through its competitive advantage of low prices, the Hyundai-Kia group soon passed Ford and became the fourth largest auto producer in the world. Hyundai Asan, a subsidiary of Hyundai that had previously been in poor financial health after the 1997 crisis, has even expanded its plans into North Korea, investing hundreds of millions of dollars in projects such as the Kaesong Industrial Complex and the Mount Geumgang resort. Samsung had already shown significant improvement by year end 2009; their gross profits rose from $15.1 trillion in 2008 to $18.3 trillion in 2009.

These results are impressive, considering that the health of South Korea's economy is heavily reliant on exports. The *Korea Times* noted that at year end 2010, "as many as 20 *chaebol*-affiliated manufacturing firms are to post earnings of one trillion *won* this year on the back of strong exports." In addition, the World Bank recently ranked Korea as the sixteenth-best country in the world in which to do business, up from twenty-third in 2008 and nineteenth in 2009, and surpassing Japan to become the third-best country in Asia for business transactions.

Improving Transparency and Corporate Governance

The third reform, that of increasing transparency and improving corporate governance practices, was incredibly important to the success of the *chaebol* from 1998 to the present. Prior to 1997, the *chaebol* were under-regulated in terms of what they had to report, which led not only to corruption, but also to mismanagement. While measures to improve transparency were introduced during the Kim administration, it was Kim's successor, Roh Moo-hyun, who pushed these reforms even harder because he believed, as he stated in a meeting with the *chaebol* in 2003, that some conglomerates had yet to "part with unsound practices, such as fraudulent accounting, stock manipulation, and irregular wealth succession [among family members]." According to interviews with analysts from the U.S.-Korea Institute at SAIS, the *chaebol* also improved objectivity on their boards of directors since the 1997 crisis, and have made improvements in moving towards new global transparency standards. The number of independent board members (meaning those outside the group of family members and close friends of the *chaebol*) increased. Changing the opaque way in which the *chaebol* conducted their business greatly increased investor confidence, which led to a higher likelihood that these *chaebol* would raise capital through equity and other business ventures rather than simply accumulating more debt from Korean banks.

Having more credibility in the way that they conduct their organizational and financial matters enabled South Korea to establish better relations with international firms and investors, which most likely put them in a better position once the 2008 financial crisis hit. Investors abroad will likely have more confidence in companies that have a more objective board of directors that doesn't consist mainly of family members, and also will be more amenable to doing business with firms from which they can receive properly audited financial statements. Back in 1997, though the economy as a whole in South Korea was declining, international investors realized that they could not trust the *chaebol* to carry out further investment, because they knew too little about their relations with the South Korean government and their business practices, and thus the overall trends of where these firms were headed. However, after the 2008 crisis, this was not the case, and as can be seen from the evidence above regarding the geographic expansion of the *chaebol*, many firms are still willing to do business with South Korean conglomerates, most likely because they are now taken more seriously as a result of their structural and operational changes.

V. CONCLUSION AND POLICY RECOMMENDATIONS

As the Lee Myung-bak administration continues to work with the *chaebol* and other Korean businesses to continue improving the nation's economy, leaders should take a number of steps in order to ensure further success. Though the analysis above shows that *chaebol* reform has improved the system, there are still numerous aspects of South Korean business that can be improved.

Take Measures to Prevent Further Overextension

As stated earlier, the 2008 crisis was largely due to the rampant over-leverage and overextension that occurred in the West. Because South Korea was experienced with the crippling effects of accumulating a large amount of debt, the government took measures to ensure that this would not damage the country the way in which it had more than 10 years ago. While the problem of excessive debt is improving, another aspect of the *chaebol* that must be addressed going forward is that of further overextension. Previous reforms ordered the *chaebol* to consolidate their separate companies and shed non-core businesses, which resulted in better control over a smaller number of entities, and thus better coordination as they expanded geographically. However, this expansion will also require significant planning, and they will face the same risks of making unsound business decisions and having poor communications between management and subsidiaries should expansion happen too quickly or not in an organized manner. The South Korean government should take steps to work with foreign businesses to increase the time that it takes for *chaebol* to propose and execute business ventures abroad so that these decisions are not made too rapidly. This is more of an issue, however, for the medium-sized *chaebol*, as they do not have as many resources as the larger *chaebol* to effectively manage rapid expansion. Nonetheless, caution should be taken regardless of the firm's size.

Continue to Increase Transparency and Limit Conflicts of Interest

While the issue of transparency is in my opinion the most important problem to address of the *chaebol* reforms, it is also the most difficult; there are no quantitative benchmarks, as there are in the size of smaller entities or lower debt levels, but rather, according to scholars, most indicators involving transparency are qualitative. The *chaebol* have certainly made strides in improving their corporate governance and credibility in the past few years. These conglomerates have greatly expanded their board of directors membership and have for the most part refrained from appointing a board of directors that also consists of management and their families. However, problems still remain; there are instances in which board members are close friends of the *chaebol* families, and thus the conflict of interest is just as present as if the board member were a relative. Such board members should be removed so as not to influence business decisions. In addition, the South Korean government needs to continue supervising the auditing practices at these conglomerates to ensure that there are no connections between auditors and management so that financial information might be distorted for management's gain. The government must add more regulations that require reports from these companies and their business decisions; according to scholars Shim and Steer, the "principal reason for the [Asian] financial crisis was the failure of management to adjust to changing business circumstances…[and] unless there is a management revolution, Korean firms may face another crisis in the near future." If the government cannot see what these companies are doing, then it will be hard for them to determine whether or not they are on a corrupt, self-destructive path. Requiring more disclosure of company activities will enable the government to work with the *chaebol* and ensure that they are not straying from best practices.

More importantly, transparency needs to be improved because there are many foreign investors who believe that these firms have, in fact, not improved in terms of corruption, which can lead to trust issues in the future should reforms not become apparent. According to a recent survey conducted by Professor O. Yul Kwon at Griffith Business school in Australia, of the foreign businesspeople questioned, the mean score on the question of whether or not the "importance of personal relationships in daily business operations" was 2.3, which by this survey's standard means that they do not believe that there has been an improvement (though they do not think that it has gotten worse). They also ranked this importance of personal relationships as the most difficult challenge that the *chaebol* will have to face in the coming years, and they see this as a crippling disadvantage for Korean firms, as personal interests are often likely to be counter to the best interests of the firm. To first understand what specifically needs to be improved, scholars should conduct more studies on how (and if) corporate governance has improved in recent decades. Once we know more regarding the main problems, lawmakers will have a better idea of what they have to implement in order to fix transparency problems and conflicts of interest.

Increase the Role of Watchdog Organizations to Continue Fighting Corruption

These aforementioned policy recommendations, fortunately, will be much easier to achieve and enforce currently than they were in the aftermath of the 1997 crisis. This is mainly because one key difference between the environment during the 1997 Asian Financial Crisis and today is the Internet. The more the public is informed about issues within large conglomerates, the more likely the government will be pressured to take action against such scandals. In addition, watchdog organizations such as the Fair Trade Commission serve as a preventative mechanism, or a sort of a panopticon for the *chaebol*; they are not entirely sure who is monitoring them, but there is the constant risk of being caught; thus, there will be even more incentive to behave out of the simple fear of getting caught. One such instance in which increased communication through the Internet has resulted in exposing organizations is that of Samsung in 2007. The Lee family (notably Lee Kun-hee, chairman of Samsung, along with his son Lee Jae-yong) was accused of bribery and buying several controlling shares at discounted prices within the company (right before he was caught, he was about to buy 1.25 million shares in convertible bonds at 7,700 *won*, which was less than half of the market amount). The issue came to public attention through the efforts of one of the company's former top legal affairs officers, Kim Yong-chul, who released the scandal in a four-page official company document that was posted online for the public to see.

The South Korean government should come up with a better incentive structure (such as that of allowing more anonymity) so that whistleblowers will be more inclined to expose any corruption that they see within a company and not be concerned with consequences of exposing powerful businessmen. This situation can also be improved by further disintegrating the previously referenced "*chaebol*-state symbiotic relationship" that has been in place for decades. Though the government has less influence in business matters and is not as involved in *chaebol* activities, these conglomerates still get a number of privileges that can potentially lead to relapses in reckless corporate behavior. A Korean lawmaker stated that South Korea still needs to learn from the United States in terms of objectivity in business, and that the traditional government-*chaebol* relationship has not changed significantly. In addition, among those questioned in Kwon's survey, many foreign businesspeople saw "lack of transparency and consistency in regulations," "prevailing cronyism and corruption," and "excessive discretionary power of bureaucrats" as prevailing problems. Until the government has less of a relationship with these big businesses and pushes for harsher reforms, the transparency problem will not improve, and it could lead to repeating the rampant corrupt practices that ultimately put them in vulnerable positions during a time of crisis in 1997.

To recap what has been said so far, this paper shows that these *chaebol* reforms that took place after the 1997 crisis were crucial to bracing such a large part of South Korea's economy for the events of 2008. Because they were not as affected as their Western counterparts were, the *chaebol* could grow in the face of disaster and improve their international reputation. Nonetheless, problems still remain, ranging from risks of further overextension to lingering corruption and conflicts of interests. In particular, as Korean firms continue their current trend of increasing presence and influence on the international scene, it will become even more important for the government to supervise and regulate these companies so that they do not make the same mistakes they did during their first round of expansion in previous decades. The government will have to play a more objective role and ensure that government relationships with the *chaebol* do not impede the ability to create legislation. Once the South Korean government puts itself into this more objective position to pass and enforce additional legislation concerning *chaebol* supervision, then South Korea will be in an even better position to continue on the trajectory of success on the international business stage.

FDI in Korea: The Permanent Achilles' Heel?

By Andrew Noh

I. INTRODUCTION

The South Korean economy has proven markedly resilient in the face of the global financial crisis that began in 2008, posting positive GDP growth while most economies recorded steep drops. The Korean economy continues its remarkable growth in 2010 with GDP projected to grow 5.5 percent according to Bank of Korea projections. Yet despite the impressive growth and goodwill in Korea in 2010, the Korean economy's Achilles' heel remains foreign direct investment (FDI). In 2009, net FDI hit a 15-year low of $965 million, according to government figures. The Bank of Korea (BOK) announced that the country's net FDI—inflow minus outflow—stood at $965 million from January through November 2009, down 57.6 percent from the same period in 2008. This amount represented Korea's lowest level of FDI since 1994, when net FDI reached $767 million.

When taken at face value, South Korea's low level of FDI is likely because of investors' retreat from all markets during the financial crisis. After all, foreign investment in the global economy tends to rise and fall with the global economy. Imports, foreign firms, and foreign investment are acceptable during times of growth, but subject to xenophobic scapegoating during times of crisis. The period 2008–9 was obviously a time of crisis for the world economy. Global FDI dropped 39 percent in 2009, so it should follow that inbound FDI in Korea would also fall at a similar rate. Unfortunately, this was not the case; Korea's FDI inflows dropped a drastic 57.6 percent. In addition, the 2010 UNCTAD *World Investment Report* found that FDI flows to Asia dropped a modest 17 percent in 2009, making Korea's 57.6 percent drop even more astonishing. The *World Investment Report* also reported that the region now accounts for one-fifth of global FDI inflows. Of that, FDI inflows to Korea accounted for only two percent of the region's inflows. The drop in Korean FDI was so large that Korea fell out of the A.T. Kearney Foreign Direct Investment Confidence Index for 2010, the first time since the index's inception in 1998.

What explains the precipitous drop in foreign confidence in Korea? Why are FDI inflows for Korea so weak in the most economically dynamic region in the world? These questions become even more confounding as Korea continues to improve its institutional and cultural framework for FDI. According to Bernie Bishop's "Barriers to Foreign Direct Investment in Korea and Australia," since the 1997 crisis the Korean government has undertaken a paradigm shift in its economic policy and pursued relentless institutional and structural reforms in compliance with the IMF rescue package. The government has abandoned its policy of protecting domestic industries, pursued the task of restructuring *chaebol* (conglomerates), and liberalized the economy, while opening the Korean market widely to international competition through trade, FDI, and mergers and acquisitions (M&A). These reforms have taken place across Korea's contentious politics; liberal and conservative governments alike have recognized the need to attract further investment in Korea. In addition, many researchers have argued that even Korean society and its people have changed, becoming more amicable to foreign business operations in Korea.

Yet despite the improving institutional and cultural framework for FDI, FDI inflows in Korea continue to diverge against global and regional trends. Research by Arthur Alexander in "Mergers and Acquisitions in Korea: The Leading Edge of Foreign Direct Investment" has shown that while worldwide M&A—a primary indicator of the level of FDI—set new records in 2006 and 2007, Korea's fell in both years. This is most surprising as the world economy reached new levels of prosperity during the same time period. The BOK's announcement of Korea's historically low 2009 FDI numbers paints an even grimmer picture of foreign investor confidence in Korea, and suggests that there is something seriously wrong with Korea as an investment destination. Why have international investors fled one of the most vibrant economies in the world? Does the source of foreign investors' aversion to Korea come from the top level of policymakers or from the bottom level of bureaucrats and civil society? What more needs to be done to increase FDI inflows so that it is comparable on a regional level?

This paper attempts to answer these questions. First, it begins with a brief historical examination of FDI inflows in Korea in an effort to lay out the institutional improvements Korea has made to its FDI framework since the 1960s. The paper will then examine the current Lee Myung-bak administration's efforts to promote FDI; the Lee administration has been the most proactive administration to date, and an examination of current FDI initiatives is necessary to understand the current FDI environment in Korea. The paper will then delve into three case studies—covering a success, a semi-success, and an outright failure—that will provide a sampling of the issues foreign companies encounter when they choose to invest in Korea. The paper will conclude with an assessment of historical factors, case studies, and the current FDI framework to determine what exactly helped contribute a successful or unsuccessful case of FDI. Finally, the paper concludes that despite improvements, FDI in Korea is still at times subject to insufficient regulatory transparency; inconsistent, ad-hoc changes in the interpretation of regulations by lower-level bureaucrats; underdeveloped corporate governance; and the lingering remains of economic domination by the remaining national economic champions, the *chaebol.*

II. BRIEF HISTORY OF FDI IN SOUTH KOREA

The Korean government has long maintained tight control over allocation of financial resources to ensure that investment activity would take place according to its priorities and plans. This has been possible for three important reasons. First, the government had a firm control over domestic finance after nationalizing commercial banks in 1961. Second, the government controlled the use of foreign savings by requiring all foreign loans be authorized by it. Third, the government could control the direction of industrial development by maintaining tight regulations on FDI. Had foreign multinationals established a large presence in Korea, it would not have been easy for the government to maintain its industrial policy.

While Korea relied heavily on foreign borrowing, it largely stayed away from capital inflows in the form of FDI or portfolio investment. Simply put, the Korean government preferred loan-based development to investment-based development. It was not until the Kim Young-sam administration in 1993 that Korea finally placed foreign investment policy high on its economic agenda. The Kim administration entered into power at a time when international economic issues moved to forefront of global and domestic politics. The formation of the North American Free Trade Association, the conclusion of the Uruguay Round, the evolution of the General Agreement on Tariffs and Trade (GATT) into the World Trade Organization (WTO), and the creation of the Asia-Pacific Economic Cooperation (APEC) forum all loomed large, and Korea sought to find its place in the emerging global economic order. Korea's desire to be a part of APEC and the Organisation for Economic Co-operation and Development (OECD) would drive the Kim administration to reverse Korea's long aversion to FDI and move Korea towards more market-friendly, liberalization policies.

Despite these reforms by the Kim administration, inbound FDI in Korea during the 1990–97 period amounted to 0.96 percent of its gross fixed capital formation, while the average for other East Asian economies was 7.4 percent according to the 2002 UNCTAD *World Investment Report*. According to O. Yul Kwon, when it came to attracting foreign investment, the Korean government was passive and restrictive. The 1997 crisis would force Korea to change after it agreed to the IMF's conditions to open its economy to foreign investment.

As a result of the IMF's conditions, the government faithfully carried out the liberalization reforms, including making a full-fledged opening of the financial markets, selling off troubled financial institutions to foreign investors, lifting foreign exchange regulations, and radically liberalizing inward foreign investment, both portfolio and direct. The Foreign Investment Promotion Act (FIPA) codified Korea's commitment to FDI and sought to create a more open and transparent investment regime, and to abolish many of the regulatory restrictions that plagued the country prior to 1998. Structural reforms were launched in four areas: financial, corporate, labor, and public. Old industrial policy placed restrictions on inbound FDI, but the government began actively engaging FDI as a source of not only foreign capital inflows, but also advanced technologies and management practices. The government further established two FDI-promotional agencies, Invest Korea, an agency mandated to offer a "one-stop shop" for attracting FDI, and the Office of the Investment Ombudsman to provide investment aftercare services to foreign companies operating in Korea. For the first time, FDI definitions and requirements were put forward in an explicit and transparent manner for foreign investors.

As mentioned earlier, most of the traditional barriers to FDI were removed following the Asian Financial Crisis and subsequent liberalization of the Korea economy. The traditional barriers of local company promotion—limited foreign ownership, technology poaching, and *chaebol* favoritism—finally ended, primarily as a result of the Asian Financial Crisis. Foreign companies were finally allowed to invest in all but a few, mostly manufacturing, industries. All told, FIPA liberalized Korea's FDI framework to 99.8 percent of business sectors open to FDI, now in line with most OECD practices. The financial crisis would also force the Korean government to implement *chaebol* reforms, thereby dissolving some of the collusive government-*chaebol* relations, and ultimately resulting in improved corporate governance, management transparency, and accountability. The government would also lay the framework to later establish three free economic zones (FEZs), providing a range of investment incentives including tax breaks, tariff-free imports, relaxed labor rules, and improved living conditions for expatriates in areas such as housing, education, and medical services.

Despite the dramatic reorientation of the Korean economy towards foreign investment, old habits die hard, and FDI in Korea reverted to previous levels. Although FDI increased at a rapid rate after 1997 because of the IMF's conditions and foreign M&A of troubled Korean corporations, the flow of foreign capital quickly slowed when the IT bubble burst in 2001. Foreign investment would rise again from 2004 to 2007, but would quickly slow thereafter, bottoming out in 2009 as mentioned earlier. Table 1 shows the rapid rise and fall of FDI in Korea.

Table 1: FDI Levels in South Korea

(Unit: USD, millions)

Year	Notification	Arrival
2001	11,287	5,034
2002	9,095	3,806
2003	6,471	5,138
2004	12,796	9,289
2005	11,566	9,618
2006	11,247	9,123
2007	10,515	7,850
2008	11,711	8,371
2009	11,484	6,668

Source: Invest Korea

Although President Lee Myung-bak came to power as FDI in Korea was falling, the blame cannot be placed solely on his policies. In fact, during his fall 2007 presidential campaign, one of Lee's key promises was to take steps to attract more foreign direct investment in Korea in an attempt to revitalize Korea's economy.

Since taking office in February 2008, President Lee has recognized the forces of globalization and the need to move Korea away from a manufacturing-based economy and towards a knowledge and services-based economy. In a January 2009 speech before the American Chamber of Commerce in Korea and the European Union Chamber of Commerce in Korea, President Lee emphasized Korea's strong potential for overcoming the crisis and reassured foreign investors of his administration's business-friendly policies. In addition, President Lee established the Presidential Council on National Competitiveness to address FDI by inviting foreign business association leaders and foreign CEOs operating in Korea to be regular members on the panel.

President Lee also laid out explicit promises to further promote FDI through corporate tax reductions and a restructuring of Korea's cumbersome corporate tax code. Capital market reforms under the Lee administration have eliminated or raised ceilings on aggregate foreign equity ownership, individual foreign ownership, and foreign investment in the government, corporate, and bond markets. Taxes remain as one of the biggest barriers to FDI, and President Lee further proposed cutting the corporate tax rate and increasing the threshold between high and low tax brackets by the end of 2010, as shown in table 2 below.

Table 2: Corporate Tax Rates in South Korea

Current	Tax Rate	End of 2010	Tax Rate
<₩100 million	13%	<₩200 million	10%
>₩100 million	25%	>₩200 million	20%

Source: Ministry of Strategy and Finance, Republic of Korea

Korea has chosen to pursue a slow evolution of its FDI policy evolution, from openly hostile policies until the 1980s, to hesitant ones in the 1990s, and finally to actively seeking FDI as a critical component of its Korea-as-a-business-hub strategy. Despite the sudden rapacious FDI policy and active recruitment, FDI inflows remain precariously low. The reasoning for this may be deduced from an analysis of successful and failed cases of FDI. In the following section, the paper examines

MetLife, GM Daewoo, and Lone Star Funds in an attempt to identify the factors that are responsible for the lack of achievement despite Korea's activity.

III. CASE STUDY 1 (SUCCESS): METLIFE KOREA

The American insurance giant MetLife began its operations in Korea in 1989 through its subsidiary MetLife Korea, when the Korean insurance market opened to foreign investors. MetLife's operations began when it established a joint venture in Korea with the Kolon Group, a Korean textile manufacturer. The joint venture began as a small operation and captured very little of the Korean insurance market (insurance was sold on an informal basis at the time, usually person-to-person) and would continue that way until 1998, when MetLife was able to acquire Kolon Group's stake in the venture, rename the company, and begin restructuring MetLife Korea.

Once MetLife gained full control of its operations in Korea, it began offering variable insurance products—the first insurance operator to do so in the Korean market. In an effort to upgrade its workforce, MetLife launched the "professional agency force" to convert its informal, person-to-person sales force into the professional force seen today. Long-established domestic firms, whose sales force consisted mostly of women, historically dominated the Korean insurance market; shop-owners and homemakers sold insurance on a part-time basis to make ends meet. This sales channel was dubious at best, as these agents had little or no training, and as a result, the insurance industry was marred by complaints of unprofessionalism and low customer retention. Upon entry, MetLife immediately professionalized the workforce and established a precedent that all insurance companies operating in Korea now follow. This positive externality, both for foreign firms and for MetLife, almost certainly came about because of market needs rather than any government policy or company initiative.

Since then, MetLife has launched telemarketing, bancassurance, and pension products, and is now the fourth-largest variable universal life insurance writer in Korea, capturing approximately three percent of the market. Although small in percentage terms, MetLife's three percent market capitalization represents a large portion of the 18.9 percent market capitalization by foreign insurance firms.

Although MetLife successfully cultivated local talent and increased labor productivity through its professional agency force, the company's cultivation of foreign talent cannot be ignored either. Stuart Solomon, longtime CEO of MetLife Korea, speaks Korean fluently. This skill has no doubt helped his image with the local population and enhanced MetLife's image as the rare responsible foreign company in the eyes of the Korean public.

MetLife's success in Korea stands as a shining example of FDI's potential in Korea. Although the company started small and in a joint venture with a company unrelated to insurance or other financial services, it was able to take advantage of the Asian Financial Crisis and the Korean government's liberalization of financial services to shed the joint venture and strike out on its own. MetLife also successfully cultivated the local population through its "professional agency force" and actuary programs at Seoul National University when it initially arrived. MetLife's cultivation of local talent and its Korean-inclusive corporate governance structure allowed it to engage the Korean government and society at all levels. These actions exhibited its commitment to both the Korean market and the Korean people, as if to portray itself as a Korean company when it was not.

Another factor in MetLife's success is its strategies specifically customized for the Korean market. Korea is a rapidly aging society; 38 percent of the population is expected to be elderly by 2050, putting it in contention with Japan, Italy, and Spain for the oldest country in the world according to the Korea National Statistical Office. MetLife was the first foreign firm to have made inroads into the retirement markets in a systematic way. It hired Korea's top financial planners, while preparing the next generation of insurance actuaries through a dedicated education program on pensions and annuities at Seoul National University. The program is set to produce a total of 2,400 retirement-planning professionals by the end of this year. The firm plans to further improve the program in the near future.

MetLife's success is not a result of its actions alone. Luck has played a significant role in MetLife's success, having benefited from the Asian Financial Crisis and reform of the insurance industry. In 1999, the Korean government established the Financial Supervisory Service (FSS) to regulate the financial services industry, which includes insurance. The FSS is one of the most transparent and effective regulatory agencies in Korea, and provides a comprehensive one-stop shop for all insurance regulations. The FSS immediately joined the International Association of Insurance Supervisors (IAIS), thereby synching Korea's regulatory standards to international norms, which MetLife was already familiar with. MetLife International also never ran into debt issues in any of its operations around the world. Although some may contend that this is a product of proper corporate governance, luck plays an important factor as well.

MetLife's success is a combination of good corporate governance, a high-penetration market, and luck. Regulatory agencies are notoriously difficult in Korea, but the FSS was an internationally recognized agency held to international, not Korean, standards. As such, MetLife was able to avoid the usual pitfalls of FDI implementation and was left to fend for itself according to the market's, not the state's, machinations.

IV. CASE STUDY 2 (PARTIAL SUCCESS): GM DAEWOO

In 1984, the Korean government brokered a deal with Detroit's General Motors and Korea's Daewoo Motors to form a Korean-based 50-50 joint venture (JV). Each company would invest $100 million to form Daewoo Motor Company, and produce the Pontiac LeMans subcompact car. Using technology from Opel, GM's wholly owned German subsidiary, Daewoo Motors would produce the LeMans for the Korean and U.S. markets. The JV was thought to be a smart move for both firms as Daewoo lacked the engineering expertise to design and manufacture a car on par with Western standards, and GM privately doubted that a subcompact car could be profitably produced in the United States. GM took on the responsibility of marketing the LeMans, allowing Daewoo to concentrate solely on adapting the superior engineering skills of GM in its effort to gain market share from its main Korean competitors, including Hyundai.

Despite what looked great on paper, multiple problems began to develop just as production began. Daewoo's union began demanding higher wages and launched a series of strikes that repeatedly halted production. The higher wages demanded by Daewoo's union essentially made it cheaper to produce the automobile in its native Germany, thanks to Germany's higher productivity. The LeMans also suffered from several quality issues. The vehicle routinely experienced problems with its brakes and electrical system. Sales of the LeMans fell dramatically within three years of its initial production. Each partner began to blame the other: Daewoo blamed GM for failing to promote the vehicle in America, and GM blamed Daewoo for quality and structural problems. Daewoo wanted to invest aggressively outside the initial target markets, hoping to export cars to Eastern Europe, which Daewoo saw as an ideal market. However, GM saw Eastern Europe as Opel's territory and actively blocked Daewoo's efforts to expand. In addition, Daewoo wanted to invest in the booming Korean auto market, but GM was not interested in investing additional capital to take advantage of this market.

Relations soured to the point of dissolving the JV in 1991, with Daewoo agreeing to buy out GM's stake in the JV, paying $170 million for complete control of Daewoo Motor Company. Despite the brief breakup, GM and Daewoo would later join forces again. Although Daewoo managed to escape serious financial harm during the 1997 Asian Financial Crisis, Daewoo found itself in need of investors after its questionable acquisition of rival Korean automaker SsangYong in 1998. Daewoo strongly preferred a takeover from rival Hyundai or at least Ford, but those two would eventually chose not to invest, thereby reopening the door for GM and creating a new company, GM Daewoo Motors. The new JV between GM and Daewoo was established in 2001, with GM investing $400 million for a commanding 67 percent stake, allowing it tight control over the JV's operations. A group of Korean investors led by the state-owned Korea Development Bank (KDB) held the remaining 33 percent stake. The new JV would enjoy greater success than its previous incarnation, introducing eight new models to date, but would suffer from a variety of issues in its home market of Korea. Much of the new JV's success was tied to its production of vehicles for export to the American and European market, but Korean consumers shunned the brand in favor of Hyundai and Kia. Various public opinion polls revealed that the average Korean consumer viewed the GM Daewoo brand as a hostile foreign takeover of a Korean company. This public perception problem would continue on for many years even as GM Daewoo upgraded its design, production facilities and marketing that lead to the immensely popular Altheon sedan, and eight new models available for export to more than 150 markets.

Despite its efforts to grow the company, GM Daewoo, like its parent company in the United States, suffered heavy losses during the 2008 global financial crisis; sales dropped amid currency-related losses and a drop in global demand. The downturn left GM to seek loans from governments around the world, including KDB, in an effort to keep the company afloat both in Korea and around the world. Lending between mutual investors is traditionally kept secret from the public, but KDB routinely went public about its dealings with GM, often times leaking erroneous info about the financial health of the company in an effort to turn public opinion against the company. The bitter battle between the KDB and GM Daewoo would continue for many months until the two finally reached an agreement on December 1, 2010, after months of negotiations. According to the Associated Press and Agence France-Presse, the agreement will require GM to guarantee redemption of GM Daewoo's preferred shares held by local (Korean) creditors. GM is also required to share licenses with its South Korean unit for vehicles they jointly develop. Under the agreement, KDB will have a greater say in GM Daewoo's management with the appointment of three outside directors to GM Daewoo's board. KDB will also have veto rights over GM Daewoo's management decisions. As part of the new arrangements, the stake limit for this right was lowered to 15 percent from the previous 28 percent.

GM's dealings with Daewoo from 1984 to 1991 and again since 2001 demonstrate the best and worst of FDI in Korea. Although the new GM Daewoo proved to be far more successful than its predecessor, GM was not without its share of problems in Korea. Despite its success in designing, manufacturing, and selling automobiles, U.S.-based GM fell victim to a game of entrapment with government-owned KDB and hostile misrepresentations of its management. Furthermore, GM's relationship with KDB was always tenuous at best. KDB extended a $2 billion credit line to GM as part of the initial deal to create the new JV in 2001. The latest deal allowed government-owned KDB veto rights and three positions on the board of directors. Although GM was in need of a capital infusion that only the Korean government seemed to be able to provide, the onerous provisions of that capital seem to cripple GM's future corporate flexibility. Although the U.S. government took full corporate ownership of GM in 2009, the scope of its investment to save GM justified the provisions of the deal. With only a 17 percent stake in GM Daewoo, KDB's terms far exceed the scope of its investment, and the deal does not seem to have the corporation's best interests in mind, but those of the Korean government.

Although GM's foray into the Korean market has been fraught with difficulty, the fact that it has endured this long demonstrates what it truly takes to succeed as a foreign investor in Korea. For starters, it takes great patience; GM's negotiations with KDB dragged on for the better part of two years. It requires resolve to succeed despite past failures. And finally, it requires wedding a company to a single market, and staying in the game no matter the circumstances. The semi-success of GM Daewoo shares none of the characteristics of MetLife's successful foray into the Korean market. GM Daewoo could not tap into and improve its workers in any systematic way—the worker's union was just too entrenched, and powerful enough to resist any real professional development. The company also failed on the macro-level by failing to take full advantage of Korea's then-booming automobile industry and automobile export market because of Daewoo's own failing before the JV with GM. All told, the GM Daewoo JV could not, or chose not to, capitalize on the macro- and micro-level opportunities afforded to them

V. CASE STUDY 3 (FAILURE): LONE STAR FUNDS

The most famous failure of FDI in Korea is the case of Lone Star Funds' acquisition of Korea Exchange Bank (KEB) in 2003. Arthur Alexander has meticulously examined the chronology of Lone Star's troubles in Korea in his paper "Policy Implications of Korea's Low Level of Foreign Direct Investment," and I will merely summarize and update the Lone Star case to reflect the continued problems with private equity funds in Korea.

In 2003, Lone Star Funds, a mid-cap private equity firm based out of Dallas, purchased 70.9 percent of the distressed Korea Exchange Bank (KEB) for $1.2 billion. KEB was a product of Korea's push towards liberalization in the late 1980s and early 1990s, and like other South Korean banks that were privatized during that period, suffered when the loans it made to the *chaebol* were defaulted on during the buildup to the Asian Financial Crisis. Similar to other private equity firms doing business in Korea at the time, and along the lines of all private equity firms, Lone Star identified an undervalued company with sound economic fundamentals that had fallen on hard times. Lone Star would restructure the company, eliminate its nonperforming loans, and sell the company for a profit once the two-year moratorium expired in 2005.

Lone Star swiftly employed Western-style corporate restructuring practices, cutting four hundred jobs and overhead expenses, mostly by closing nonperforming branches, and updating technology. With the global economy booming and Korea's renewed exposure to international capital, Lone Star quickly turned KEB into a profitable company. By summer 2005, the *Wall Street Journal* reported that KEB's ratio of bad loans to total loans fell to 1.32 percent, easily making it a healthy and profitable asset for Lone Star to unload. The outlook looked bright as the two-year moratorium on divestment was set to expire in October 2005 and Lone Star was primed to gain a healthy return on its investment.

Lone Star's problems began to surface almost as soon as KEB recovered from its malaise and began earning profits. After many years of watching foreign firms earn profits from Korean companies, the Korean government slowly realized that it was not receiving taxes from foreign firms' purchase of Korean companies during the Asian Financial Crisis. The reason for the loss of tax revenue was that Korea had signed bilateral tax treaties banning dual taxation, which allowed foreign companies to be taxed only in their home country. Most foreign firms, including Lone Star, created subsidiaries in these countries to take advantage of the loophole. By April 2005, Korean tax authorities began questioning Lone Star's financials, and soon they began raiding Lone Star and other foreign private equity firms in Korea, eventually culminating in $200 million in tax penalties and indictments for personal tax evasion against Lone Star executives.

However, the nightmare for Lone Star would not end there. In February 2006, National Assembly members began pushing the "independent" Board of Audit and Inspection (BAI) for further investigations into Lone Star's original 2003 purchase of KEB. At the local level, the Seoul district prosecutor's office launched a probe into Korean government officials and KEB executives for allegedly accepting bribes and committing fraud in an effort to unload the then-failing company. Prosecutors further alleged that KEB and Lone Star executives conspired with government officials to undervalue the company so as to avoid regulations in the initial sale of the bank. Lone Star would also come under attack from its own workers when the KEB union organized several rallies to protest Lone Star's sale of the bank. Despite the investigations and negative publicity, Lone Star reached an agreement with Kookmin Bank to sell three-quarters of KEB's shares for $7.8 billion. The sale, if completed, would return a huge profit for Lone Star and would be the country's largest acquisition ever.

The good fortune would not last long, as Lone Star's legal troubles began hampering Kookmin's due diligence research of KEB and Lone Star, and the bank hinted that it might delay, or even cancel, the original agreement to take over KEB. In May 2006, the Seoul city government announced its plan to revise certain tax treaties in an attempt to tax the capital gains of all foreign companies owning local firms. In addition, the National Tax Service launched a nationwide audit of all foreign companies. Nearly 5,000 companies fell under the probe.

So by May 2006, current and former Lone Star executives were under indictment, the firm was under investigation for manipulating financial data, and the government was attempting to collect taxes that had been protected under tax treaties. Moreover, the government was attempting to rewrite bilateral tax treaties and was auditing the books of nearly 5,000 foreign companies. Lone Star's sale of KEB to Kookmin would eventually fall apart due to the legal investigations, but Lone Star's prosecution would continue for many more months to come.

Lone Star would eventually find a new suitor in the British giant HSBC and confirm a deal to sell KEB's remaining shares for $6.3 billion. However, Korea's regulatory agencies refused to approve the sale while Lone Star was under investigation. Lone Star's legal woes would continue into late 2008, by which time the financial crisis took full hold on the global economy and HSBC announced that it was abandoning its pursuit of KEB after failing to renegotiate a lower price to reflect the new economic climate.

It was not until late November 2008 that a Seoul court ruled the sale of KEB to Lone Star was legal and the firm was finally cleared of its legal and regulatory woes. Since the ruling in late 2008, Lone Star has been unable to divest its shares of KEB and has been searching for potential buyers. In March 2010, Lone Star renewed its discussions with Kookmin bank to purchase KEB for $3.9 billion, but the Korean government's attempt to sell its 57 percent share in Woori Finance Holdings (Korea's largest financial firm) overshadowed the sale and hampered Lone Star's ability to generate interest in the smaller KEB. Since then, the Australia and New Zealand Bank Group (ANZ) and Korea-based MBK Partners have expressed interest and are conducting due diligence.

The troubles of Lone Star's foray into Korea worried many foreign investors and no doubt played a role in the massive FDI exodus from 2006 to 2010, as chronicled by a December 2007 Heritage Foundation report and comments by then American Chamber of Commerce president Tami Overby. A 2008 *Los Angeles Times* survey on the Lone Star case reported that foreign investors worried about the way in which investigators from the Supreme Prosecutors' Office fed a steady stream of insinuations about corporate malfeasance to the Korean media, stoking nationalist resentment against foreign investors. Investors additionally accused the prosecutors of harboring a grudge against foreign private equity firms.

VI. CONCLUSION

President Lee's efforts to increase FDI in Korea demonstrate the serious commitment of Korean political leaders to build their country as an attractive investment destination and Northeast Asia hub. Yet despite their efforts, Korea is still not among the premier destinations for international investors. The desire of top political leaders and policymakers of all stripes to attract investment is chronicled here in this paper and in many others. As Alexander noted, the institutional framework to attract such investment has grown stronger every year since 1998; return on investment is comparable with other Asian countries, and Korean assets have become cheaper since the global crisis began. Yet, investors have consistently chosen other Asian countries over Korea.

The Economist Intelligence Unit's 2010 *Country Commerce* report on South Korea further states that "despite government attempts to create a more foreign-friendly investment environment, South Koreans regularly voice concern about foreign takeovers of domestic companies." This is in many ways similar to the claims made in the EIU's 2007 report that Korean government bureaucrats still hold an apparent de facto negative attitude toward foreign involvement in Korea's economy: "The government's attitude towards foreign trade emphasizes exports and slow liberalization of imports. This attitude remains deeply ingrained in the outlook of the government and the country despite continuing globalization and liberalization."

As seen earlier, it is not for a lack of effort that FDI in Korea remains at a historic low. Key Korean policymakers have taken major steps to address the concerns of foreign investors, including incentive structures for government bureaucrats who promote FDI. However, the government can do little to change the Korean public's suspicions of foreigners and foreign investment. It has essentially created its own worst enemy with its loan-based command economy favoring domestic industries and is now finding it difficult to reverse decades of aversion to foreign investment. FDI in Korea is still at times subject to insufficient regulatory transparency; inconsistent, ad-hoc changes in the interpretation of regulations by lower level bureaucrats; underdeveloped corporate governance; and the lingering remains of economic domination by the remaining national economic champions, the *chaebol.*

In private interviews, foreign business leaders operating in Korea acknowledged the disconnect between top-level policy and bottom-level implementation. Some business leaders explicitly referenced earnest high-level Korean officials who truly want to correct Korea's FDI imbalance. However, many were quick to point out lower-level bureaucrats' failure to understand the increased competition from other Asian economies, especially cheaper labor throughout the rest of Asia. These leaders also cited these factors as the main impediments to correcting South Korea's FDI problem: Korea's difficult labor relations; sudden regulatory changes without advance notice; constantly shifting safety standards; and the remnants of Korea's old command economy personified by a combination of national and local implementation and interpretation. Many were also quick to point out that news about Korea does not reach Western companies that often, and that when it does, it is usually a negative story about one of these issues. Western CEOs see the negative news of the few brave companies to enter Korea and choose to invest elsewhere, knowing that they will receive a higher return on investment without the headaches.

Many of these business leaders' complaints about the Korean market are personified in GM's and Lone Star's dealings in Korea. Indeed, GM and Lone Star serve as important warning signals for foreign firms planning to enter Korea. The failure of Lone Star, the partial success of GM Daewoo, and the success of MetLife demonstrate how imperative it is for foreign investors to build support through Korean society and government. It is important to cultivate relationships with the lower-level agencies, such as the FSS, KDB, and the district prosecutor's office, no matter what the national government puts forward. In the successful case of MetLife, the company was able to paint itself as a "Korean" company by launching its "professional agency force" and cultivating local talent, and creating a perception of MetLife as a responsible "Korean" stakeholder. This had the double effect of heading off any potential labor disputes and setting the market standard for labor, which other insurance companies soon adopted. MetLife also inadvertently benefited from the creation of the FSS and the overall regulation of the insurance market. The impact of the FSS's membership in IAIS cannot be overstated. The FSS could not impose inconsistent ad-hoc regulations at any level, provide insufficient transparency, or use poor corporate governance, because of the uniform international standards set by IAIS. GM and Lone Star were not as fortunate.

Despite great improvement in Korea's FDI framework, this paper has pointed out numerous areas where the Korean government should improve if it is to rehabilitate its image as an investment destination. The complaints of current business leaders and the cases listed above prove that foreign perceptions matter, and the Korean government must take radical steps to change these perceptions. Many of these problems, such as the militant labor unions, are a structural feature of the Korean economy itself, and policies to increase FDI will do little to solve them. It seems that the Korean economy as a whole must adjust to its new geopolitical reality as a "nutcracker" position between China and Japan in order to truly stimulate FDI and advance its economy to the next level. As this paper has demonstrated, the desire to attract investment is there, but the will is not.

Sustaining Medical Tourism in South Korea

By Kristen Handley

I. INTRODUCTION

South Korea's breakthrough in the medical tourism industry launched during 2007 with 16,000 foreign patients. In the year 2010, 60,000 foreign patients are expected to travel to South Korea (ROK) for medical services. Anticipating 100,000 foreign patients by the year 2012, this rapidly growing trend will solidify South Korea's prominent role in the medical tourism industry. Interest in medical tourism has been steadily progressing among patients, particularly with mounting health care costs in countries such as the United States. The global medical tourism industry is expected to gross $100 billion by 2012. Clearly, there is profit to be made by providing medical care to foreigners. South Korea is cultivating this lucrative business while competing among other Asian nations to further expand its comparative advantages. This paper will explore the origins, development, and current status of Korea's fledgling—but flourishing—medical tourism industry.

Below are some important questions facing South Korea:

- How does the ROK promote medical tourism?
- What government policies are in place that foster the medical tourism industry?
- Who are the medical tourism consumers that the ROK targets?
- What are the ROK's comparative advantages in medical tourism?
- What capabilities does the ROK possess to adequately supply the service of medical tourism?
- What is the impact of medical tourism on Korean society?
- How can the ROK competitively sustain this industry?

This paper will illustrate that although the ROK demonstrates exponential progress in fostering medical tourism, there are challenges that need to be effectively addressed if South Korea is to continue to be competitive in this specialized niche industry.

II. INTRODUCTION: MEDICAL TOURISM OVERVIEW

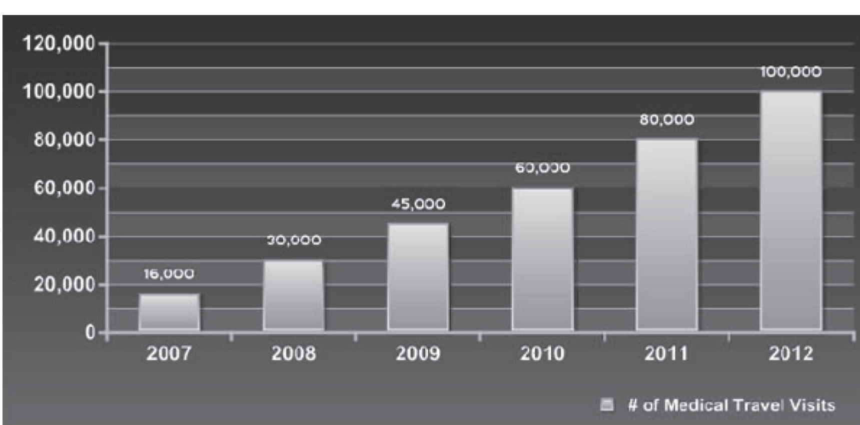
Medical tourism is loosely defined as travel to receive medical, dental, and surgical care, which also incorporates an extended holiday. The medical tourism industry is rapidly expanding due to high treatment costs and waiting times for procedures in countries with relative wealth, the increasing affordability of international air travel, favorable exchange rates, and aging affluent populations. Further propelling the growing medical tourism industry is the dissemination of information and marketing on the Internet, the incorporation of intermediary companies that broker transactions between international patients and hospitals, and calculated marketing strategies that link health care and tourism. Medical tourism advertisement campaigns tout the use of technology, quality care, and reliability.

Technology, care, and reliability may contribute to the success rates of medical procedures, but to gain even more traction, there must exist an economic incentive. Economic motives are the main drivers of medical tourism on the part of both patient and host country. The costs of medical care may be relatively high in a medical tourist's country of origin. Depending on the medical diagnosis and indicated procedure, patients will be directed to a specific medical center based on relative cost and expertise. Global differences in cost of medical services are widening, notably in Thailand, Singapore, India, and South Korea, as countries cultivate unique comparative advantages in medical tourism. Some argue that Thailand's health care system is relatively weak and its industry emphasizes standard tourism over medical care. The Korean consulting firm Horwath Choongjung reports that Singapore, in contrast to Thailand, has imported Western-style technology and medical institutions which specialize in medical tourism, which has succeeded in attracting hundreds of thousands of foreign patients every year. India's medical tourism industry is known for relatively low fees and short treatment waiting times. Its system also incorporates *ayurveda*, an alternative system of traditional medicine native to South Asia uniquely applied to treatment of coronary artery disease with respect to coronary artery bypasses grafting (CABG) and cosmetic surgery. India also touts advanced technology as well as competitive physician salaries which draw Indian medical providers to return from overseas and deliver care in this system, according to *Tourism Management*.

South Korea is developing its medical tourism industry by duplicating and expanding upon concepts formulated by its Asian neighbors. Before launching medical tourism, an ROK government-led investigation concluded that investing in the biotechnology industry would brighten Korea's economic prosperity. The Korean health care system would demand advancement of the biotechnology industry. Furthermore, the Korean university system is structured such that only the most competitive students compete for admission into medical school. A top pool of intellectual talent coupled with an emphasis on the biotechnology industry would ultimately combine to realize Korea's global health care potential, according to a physician at Konkuk University Hospital. From this point, government legislation to legally authorize measures that would further attract foreign patients was subsequently needed.

The number of foreigners traveling to South Korea for medical care remains a fraction compared to Thailand, Singapore, and India. Nevertheless, Korean clinics, hospitals, and entire towns exclusively dedicated to health care, known as "health towns," are dynamically implementing new policies and marketing strategies to attract more tourists, reports Choe Sang Hun in the *New York Times*. Medical tourists and their families generate much-needed revenue for hospitals and stimulate the economy by lengthening their stay to shop and sightsee after a medical procedure. The South Korean government continues to revise visitation and visa policies to permit patients and their families to extend their stay. As of 2009, Asia Pacific Biotech News cited policy changes that included extension of medical visas and permission granted to local hospitals to form joint business ventures with foreign hospitals.

The following chart from the Korea International Medical Association (KIMA) illustrates that the number of medical tourists expected to visit South Korea is significant.



The economic benefits to both the patients and South Korea are apparent, and the industry's trajectory is promising. This is chiefly a result of sustained ROK government involvement across a number of dimensions.

III. ROK NATIONAL GOVERNMENT PROMOTION OF MEDICAL TOURISM

Legislation

The medical tourism industry has been identified by President Lee Myung-bak as one of the ROK's growth engines over the next several years. South Korea aims to attract 100,000 foreign medical tourists by 2012. Although reliable data detailing the profit made in Korea's medical tourism industry was not found or not available, the Korea Health Industry Development Institute (KHIDI) reports that the medical tourism industry generated the equivalent of $33,570,000 in revenue in 2009. The industry will likely continue on a trajectory of growth and expansion in the coming years. The national government has adopted a national strategy to attract and multilaterally develop its medical tourism industry. The national strategy, according to the Gangwon Development Research Institute, will focus on increasing demand for foreign medical tourists, publicity, and implementation of advanced technology. The ROK has inaugurated a series of laws to implement the national strategy. These laws are generated from a variety of ministries and range from the establishment of free economic zones (FEZs) to modifications to existing visa requirements for foreigners. A synopsis of some recent legislation passed by the National Assembly includes:

- *Amendment to the Medical Services Act (passed January 8, 2009)* The original law prohibited hospitals from actively recruiting domestic and foreign patients. This law was seen as disadvantageous to Korea's national medical competitiveness. The amendment permits medical institutions that report to the Minister of Health, Welfare, and Family Affairs to actively seek out foreign patients living overseas to receive medical care in Korea. Limitations to this law are directed at insurance companies, which are restricted in permissible outreach to foreigners. Furthermore, general hospitals may allocate five percent of hospital beds of the 44 large-scale medical centers (of a total of 2,046 beds) for hospitalized foreign patients.

- *Amendment to the Tourism Promotion Act (passed March 2, 2009)* This amendment is designed to: 1) create legal grounds designed specifically to support a burgeoning medical tourism industry; 2) establish first-rate accommodation facilities; 3) institute a system to enforce travel contracts and ensure patient/tourist safety; and 4) promote travel agents' hire of licensed tour interpreters. Under this amendment, auxiliary organizations within the medical tourism industry will benefit from the formation of the tourism and development fund. Under the contract enforcement provision, travel agents are required to provide safety information corresponding to a traveler's/patient's destination. Travel agents are also required to receive traveler/patient approval if there is a change in a travel itinerary.

- *Amendment to the Special Act on the Establishment of Jeju Special Self-Governing Province and the Development of Free International Cities (passed March 3, 2009)* This amendment will: 1) establish a support system to cultivate the medical, tourism, and education industries of the Jeju self-governing province (most of the authority of the culture, sports, tourism, broadcasting, and communications minister allocated in the Tourism Promotion Act will be transferred to the provincial governor); 2) form a unique tourism promotion fund for Jeju; and 3) permit the government of Jeju to install an area within its administration as an English education city, including the organization of international elementary, middle, and high schools. Jeju's unique delegation of authority allows its legislature to distinctively tailor economic and commercial activities to its culture and geography.

Other Legislation

Visa waivers or relaxed visa requirements facilitate travel for patients. While patients originating from the United States do not require a visa or special permission for a stay up to three months, the ROK government has revised immigration laws to permit other foreign patients and their families to receive long-term medical visas. Chinese patients, for example, must substantiate the need for medical treatment with a document signed by a physician. Formerly the G-1 visa needed for foreigners to stay longer than thirty days was issued only under strict standards. A 2007 *Korea Times* article indicated this law has since been revised in Jeju to allow medical tourists and their families may stay up to four years to receive medical treatment.

Laws have also been amended to allow local hospitals to form joint ventures with foreign hospitals and clinics. Partnerships maintained by Korean health care providers in the United States include the Hollywood Presbyterian Medical Center (located in California), the Jaseng Center for Alternative Medicine (which has facilities in California, New York, New Jersey, and Illinois), and the G Laser and Aesthetic Institution (located in California). Korean hospitals may also maintain liaison offices abroad, such as the Seoul National University Hospital liaison office (located in California). Korean hospitals also cultivate relationships with health care providers beyond the United States. Konkuk University Hospital, for example, maintains a partnership with Jiangsu Province People's Hospital and Tianjin First Hospital in China.

Central government promotion of the medical tourism industry, though, is not limited to legislation. Other measures employed to cultivate this industry include:

- *Korea International Medical Association (KIMA)* The acting body designed to implement government policy is a joint public-private enterprise designed to promote Korean health care abroad and enforce a safe, reliable, and transparent health care system within Korea. Supported by the Ministry of Health, Welfare, and Family Affairs, KIMA was founded in 2007 to promote Korean health care through advertising and publications, as well as hosting and participating in international health conferences. KIMA works to minimize malpractice lawsuits and works toward ensuring facilities and human resources meet international standards. The KIMA website itself is specifically designed for prospective medical tourists seeking treatment and holiday in Korea. Users are instructed to select a medical specialization (e.g., cancer, cosmetic/plastic surgery, endocrinology, etc.) from a drop-down list and then select a corresponding hospital that focuses on the preferred specialization. The hospital's offerings (number of inpatient beds, operating rooms, and international patient beds; major medical equipment and facilities; quality certification information; and contact information) subsequently populate the user's web browser. The website also includes information specific to tourism such as visa and immigration procedures, a range of accommodation options, modes of transportation, and major tourist attractions.

- *The Korean Health Industry Development Institute (KHIDI)* Established by the Korean Health Industry Development Institute Act in 1999, KHIDI is a government-operated and funded organization that supports the Korean Ministry of Health. Its main functions are to guide health care policy, steer health care research and development (R&D), enhance the management and technology of hospitals, and support the competitiveness of the health industry. This act authorizes KHIDI to spearhead support programs intended to improve the delivery of the national health services and expand the global competitiveness of Korea's national health industry.

KHIDI's strategy to expand Korea's health services and serve foreign patients centers on four components: awareness, accessibility, affinity, and accountability. First, awareness focuses on launching Korea's national brand, promoting media activity, and hosting medical tourism conferences. KHIDI operates a branch from New York, for example, that promotes Korean health care on American television networks such as CNN and CBS. Both networks, among others, have featured segments highlighting Korea's medical tourism industry. KHIDI further disseminates a "Medical Korea" newsletter to further promote Korean health care in the United States and KIMA member hospitals. Second, accessibility is designed to facilitate medical travel and assist patients with obtaining medical travel insurance and medical visas if applicable. KHIDI contributes funds to hospitals for expansion of international patient centers and education for international medical coordinators and interpreters. Third, affinity refers to the expansion of international patient centers as well as education of medical coordinators and interpreters. And finally, the principle of accountability demands development of medical call centers, medical dispute legislation, and accessibility of malpractice insurance for international patients.

- *Nation-branding* A 2009 *Korea Times* article reported on the ROK government's launch of the "Medical Korea" nation-branding project designed to attract foreign patients to its best medical facilities. This campaign actively publicizes the Korean medical tourism industry at global medical conferences as well as through international television, radio, and newspapers. The Medical Korea campaign disseminates information about Korea's medical services, special treatments, hospitals, and foreign-language communication services (targeting English-, Chinese-, Russian-, Japanese-, and Arabic-speaking patients). The Korean Wave coincides with the government nation-branding campaign. This explosion of Korean pop culture, including television dramas performed by flawlessly fashioned actors and actresses, also collaterally contributes to the promotion of the plastic surgery component of Korea's medical tourism industry.

IV. PROVINCIAL GOVERNMENT PROMOTION OF MEDICAL TOURISM

Harnessing national government policies, several regions in particular are adopting policies to develop medical tourism.

- Under the National Assembly's Special Act on Establishment of the Jeju Special Autonomous Province and the Jeju Free International City Act passed in 2006, Jeju is a self-governing province. Jeju thus benefits from strengthened financial autonomy, personnel management, and regional self-governance, stemming from its unique geography and culture. Within this framework, the Jeju Free International City Development Center (JDC) is in the process of constructing a health care town in Seogwipo. The health care town will include a medical research and development, medical, and wellness area, targeting foreign patients seeking high-end medical and tourism facilities, according to the *Korea Times*. The 370-acre complex will also include upscale apartments surrounded by an eighteen-hole golf course and beaches. Travel to Jeju can be done with relative ease, as there are few visa restrictions for foreigners. Jeju continues to focus on forming an appropriate medical tourism infrastructure coupled with large-scale resorts. It will also emphasize infrastructure to accommodate foreign-language exchange.

- Busan's civilian-led "Busan Medical Industry Committee" is composed of university hospitals, the Busan Hospital Association, the Pharmaceutical Association, the Busan Tourism Association, and civic groups that facilitate the development of medical tourism projects. Busan focuses on education of medical personnel specializing in medical tourism. Busan's medical tourism website boasts foreign-language services and lists its registered medical centers with services specifically for foreign patients.

- To date, the Daegu metropolitan area features five medical universities, 29 general hospitals, 30 oriental-medicine clinics, and 18,000 medical personnel, including more than 6,000 doctors. The Gangwon Development Research Institute reports that Daegu has also built an international hospital modeled after the MD Anderson Cancer Prevention Center, which has branches throughout the United States. The Daegu Metropolitan City Medical Tourism Information System offers a variety of excursions, including package tours, Koreanthemed tours, and fashion tours. The Daegu province specializes in general checkups, hair transplants, dentistry, plastic surgery, skin care, obstetrics and gynecology, and oriental medicine. There is also an initiative to expand professional coordinators responsible for recruiting foreign patients from Jordan, China, and Japan.

V. HOSPITAL-LEVEL/PRIVATE SECTOR DEVELOPMENT OF THE MEDICAL TOURISM INDUSTRY

National and provincial policies are implemented at the hospital level. Relatively few restrictions about overseas advertising, coupled with allocations of hospital beds to foreign patients, allow hospitals throughout Korea to gain reputations across a variety of areas of expertise. Three such hospitals are the following:

- Wooridul Spine Hospital is one of the few hospitals at the vanguard of the Korean international medical tourism industry. In its aspirations to become the “spinal destination of choice,” Wooridul is distinguished for its specialized spinal treatment, with more than 1,130 neurospinal specialists and neurospinal, spinal thoracic, anterior spine surgery, spinal medicine, orthopedics, and rehabilitation services. One senior staff member of Wooridul’s International Patients Center indicated that patients are typically under the care of four to six physicians and nurses to deliver the most effective care possible. The hospital has facilities in Seoul, Busan, and Daegu and has also opened hospitals in Shanghai, China and Jakarta, Indonesia. Wooridul provides one-stop services for international patients, from airport transportation “until the patient is well-served and leaves back for home.” The International Patient Center provides multilingual medical services specifically to assist patients on a one-on-one basis. Since 2003, Wooridul has hosted foreign physicians for specialized spinal treatment training programs, testament to both Wooridul’s international reputation and the increasing forces of globalization.

- Konkuk University Hospital’s Office of International Services and International Clinic opened with the goal of becoming an internationally distinguished name in medicine. Konkuk University Hospital boasts innovative facilities and advanced technology that combine with skilled physicians, patient liaisons, and multilingual staff. Foreign patients contact the International Clinic to make an appointment for consultation. The International Clinic maintains direct billing agreements with international insurance companies to facilitate its services.

- Severance Hospital is at the centerpiece of the Yonsei University Health System. It is Korea's second-largest hospital, with more than 2,000 beds. Severance Hospital's International Health Care Center is staffed by medical personnel fluent in multiple languages to accommodate foreign patients. One particularly noteworthy component of Severance Hospital's website is its billing transparency. It honors most major credit cards and offers the option to arrange a contract between the hospital and foreign companies or embassies. Furthermore, Severance has established direct billing agreements with foreign insurance companies as the American Foreign Service Protective Association (AFSPA), AIG Atlas, and AIU (Japan), as detailed by the Yonsei University Health System website. Both billing and insurance relationships lend credibility to an institution and are testament to integrated components within an industry working together.

- Inha University Hospital's Health Promotion Center publicizes medical care tailored specifically to international patients, including the assistance of a specialized coordinator to manage patients' navigation of the medical system. According to its website, all physicians are fluent in both Korean and English, and coordinators who speak English, Chinese, Russian, and Japanese are available to work with patients. Like Severance Hospital, Inha University Hospital accepts payment via cash or international credit card; special contracts can be arranged between the hospital and foreign companies or embassies. The Incheon Medical Tourism Inducement Group, of which Inha University Hospital is a member, recently signed an agreement with a Russian medical tourism promotion agency, the Primorsky Club, to further expand medical tourism between the two countries, reported by *Business Wire* in 2009.

VI. KOREA'S GROWING COMPARATIVE ADVANTAGE

The annual Asian health care industry is estimated to be worth about $75 billion. Competition for the medical tourist dollar is fierce, and India, Thailand, and Singapore are Korea's biggest regional competitors. India's health care system has the benefit of low costs and short waiting times to receive medical services. Its highly successful information technology system advertises these services across the globe. Singapore's relative medical tourism success is drawn from importing Western-style technology and establishing institutions specifically targeting medical tourism. Thailand's long-time success in medical tourism, states Horwath Choongjung, focuses primarily on cosmetic surgery and tourist attractions. To break into this well-established niche, Korea is harnessing its cost, medical expertise, and technology to cultivate its competitive comparative advantage and adequately supply health care services to foreigners.

Cost

In recent interviews, two Korean physicians explained the cost structure of the Korean health care system. In Korea, medical care is publicly subsidized. Korean citizens subscribe to the national insurance system and contribute approximately 4.8 percent of their income to the national medical insurance program. In most cases, Koreans pay about 10 percent of a medical bill while the national insurance program funds the remainder of fees. Thus, medical care is inexpensive relative to many other countries, such as the United States. The cost to the patient of a computed tomography (CT) scan in Korea, for example, is about $70, compared to up to $1,000 in the United States. The Korea Health Industry Development Institute figures below, based on 2009 data and costs in USD, are testament to the dramatic medical cost differentials between South Korea and the United States.

Type of Procedure	Korea	United States
Heart Bypass	$24,000	$144,000
Heart Valve Replacement	$36,000	$170,000
Hip Replacement	$16,450	$43,000
Knee Replacement	$17,800	$50,000
Spinal Fusion	$17,350	$100,000

It is clear from the table above that the cost of medical care in Korea is substantially less than in the United States. The Korea International Medical Association touts the Korean cost advantage compared to the United States and mentions a cost advantage compared to some Chinese hospitals, with comparable prices relative to Singapore. A reliable comparison for the cost of medical procedures between Korea and some of its regional competitors is not available or could not be located.

Medical Procedures

Hospitals such as Wooridul Spine Hospital focus on specialized treatment, attracting patients with their exceptional treatment, facilities, and medical personnel. Korea is also renowned for its cosmetic surgery, particularly among Chinese, Japanese, and Russian patients. Cosmetic surgery in Korea is a lucrative business since it is not covered by national health insurance and fees are typically paid in full. Furthermore, domestic demand for cosmetic surgery is significant. Thus, top medical students tend to compete for entry into the cosmetic surgery field, where the profit margins are substantial. Drawing from extensive domestic demand and talented physicians, medical resources further fuel the cosmetic surgery niche. This makes for an established, competitive, and attractive environment for foreigners to receive cosmetic surgery. In addition to cosmetic surgery, Korea continues to develop specializations in stomach cancer surgery, Lasik eye surgery, and dentistry.

Technology

Given biotechnology was one of the original driving forces behind the Korean medical tourism impetus, it is not surprising that Korea's biotechnology is state of the art. KHIDI touts Korea's development and application of the most advanced technology. Many Korean hospitals use radio-therapeutic devices such as proton therapy, cyberknife, and tomotherapy, all specialized cancer treatments. KHIDI also reports that Korea is leading Asia in robotic surgery. KHIDI further cites Korea's utilization of a high number of diagnostic devices. Data from 2007 reveal that Korea employed 37.1 CT scanners per one million Korea citizens (relative to the UK, with 7.6 per one million citizens and the United States, with 34.3 per one million citizens). Furthermore, KHIDI indicates that paperless hospitals are becoming the norm.

VII. TARGETED CONSUMERS

The tables below are adapted from KHIDI 2009 figures and illustrate that the majority of foreign patients are female (about 57%) and come from the United States (about 33%). Japan follows closely behind the United States, representing about 30 percent of all foreign patients.

	Male	Female
Percentage of all foreign patients	43.4	56.6

Country	Percentage of total foreign patients
United States	**32.6**
Japan	**30.3**
China	**11.0**
Russia	**4.1**
Canada	**2.3**
Mongolia	**2.0**
Middle East	**1.4**

Country	Percentage of foreign inpatients
United States	40.0
China	17.9
Russia	9.6
Mongolia	5.3

Korea exploits rising health care costs and increased waiting times in the United States to its advantage. Compared to the United States, Korea's prices are inexpensive and waiting times are short. Furthermore, legislation encourages medical personnel exchanges, particularly with the United States. Collaboration, training, and contact with the U.S. health care system attracts additional American patients. According to Korean medical personnel, Japanese and Chinese patients are usually drawn by Korea's cost benefit. Japan, in particular, is experiencing a rise in its aging and wealthy population. It is reasonable for Korea to target these consumers with time to spend and disposable income to expend. Russian patients tend to be more severely ill and in search of services not adequately provided by their country's health care system. Their Mongolian neighbors tend to be very wealthy and will patronize Korean medical services for routine physical examinations. The minority of foreign patients coming from the Middle East is growing slowly. In sum, patients traveling to Korea for medical services are largely from the United States and countries in Northeast Asia. The numbers and varied demographics of foreign patients are testament to Korea's success in breaking into the medical tourism industry on a global scale. Despite this progress, however, there remain potential challenges to Korea's long-term competitive capability of delivering health care services to foreigners.

VIII. CHALLENGES TO ROK'S MEDICAL TOURISM INDUSTRY

Given the rapid growth of Korea's medical tourism and its steep trajectory, the industry's comparative advantages have thus far overcome potential challenges to growth. There are a number of potential difficulties, however, which may surface in the future.

- Korea's national insurance program provides coverage to local Koreans and foreign expatriates legally residing in Korea, but not to foreigners. This has resulted in a two-tiered pricing scheme. Hospitals charge foreigners, especially medical tourists, two and a half to three times more than locals. Hospitals claim pricing is globally competitive because of the nation's high-quality medical services. Discriminatory pricing, though, has serious potential consequences. Discriminatory pricing may alarm foreign patients and jeopardize Korea's plan to transform the medical tourism industry into a major growth engine. Under Korean medical law, hospitals may face temporary closure if they fail to report a fee list for medical services not covered by Korea's national health insurance. The majority of hospitals claim that foreigners are not subject to Korean medical law. If this is upheld within the legal system, foreigners may not be protected from malpractice or other legal risks. The two-tiered pricing scheme may also violate the Fair Trade Law, which punishes discriminatory pricing systems.

  There have been reports of advertised prices that conflict with reality. A *Korea Times* news article recently revealed testimony from American patients in Korea who allegedly paid what they claimed to be 80 percent of the cost of equivalent treatment in the United States. This conflicts with the KTO's quoted prices that are advertised as one-tenth those of the United States, one-fifth of prices in Japan, and half of the prices in Singapore. Because of the two-tiered pricing scheme, the KTO advertises the prices that Korean nationals pay, not the prices for foreigners. This could call into question the price differential, which may not actually be sufficient to motivate Americans to travel to Korea to receive medical treatment. The pricing discrepancy could also undermine the integrity of Korea's medical tourism industry, especially if government-sponsored agencies lack transparency or are perceived as dishonest and unfair.

It is reported that while Korea has adopted a discriminatory pricing system, its competitors have been more cautious about adopting two-tiered pricing schemes for foreigners. Hospitals in Thailand, for example, which attract over one million medical tourists each year, charge the same rate to foreigners as to Thai nationals. In Singapore, hospitals are legally obligated to display a list of medical procedures and medical fees for foreign patients. As mentioned previously, Korean hospitals are required by law to report medical service fees for foreigners, but are reluctant to do so because foreigners are not subject to Korean law. Particularly in the wake of hosting the most recent G-20 meeting in Seoul, it will be crucial for South Korea to assume leadership on equitable treatment of all patients, foreigners and Korean citizens alike.

- South Korea’s two-tiered pricing scheme has further consequences. The two-tiered pricing scheme generates fears that social inequality will grow if medical resources and skilled workers migrate from public health care to better-paying jobs that cater to foreigners. Hospitals that are able to charge more for medical services to foreigners will have a competing economic incentive to serve foreign over local patients. Some hospitals reportedly serve foreigners preferentially to Korean citizens.

  According to the World Health Organization (WHO), the distribution of health care personnel and facilities across Korea is not equitable. Most specialized centers and personnel are disproportionately concentrated in Seoul and other cities. This results in delivery of health care services that is, in part, related to income level or socioeconomic status instead of need. The WHO cites barriers to accessing health care services, such as high user charges and regional disparities in location of facilities that disadvantage the poor. In a 2009 article in *Health Systems in Transition*, the authors argue that compared to rural citizens, urban residents are able to visit specialized physicians in tertiary hospitals with relative ease.

  Given a health care system susceptible to socioeconomic inequality, the challenge for Korea will be to harness the medical tourism industry to improve and update all health care facilities, not just those that are the most profitable. Investing in less profitable facilities may pay health dividends by enhancing health care for the local population as well as attracting foreign patients to suburban locations.

- Medical tourism relies on a breadth of industries. Delivery of quality treatment to patients requires medical personnel working in cohesion with technological and pharmaceutical elements. In its current state, there are many moving parts to the industry, but little unity. There is a dissonance between government policy and hospital practice, as the pricing discrepancy highlights. The lack of transparency transmits an incongruous message to prospective foreign patients. Overcoming this challenge will entail more consistent government regulation and enforcement of laws. Medical personnel and others involved in the field of Korean medical tourism have also noted the need for human resources. Interpreters are especially needed to assist both foreign patients and physicians to communicate effectively. Government-led initiatives and incentives will close these gaps. Cohesive integration of all these constituent industries will be vital to the future success of medical tourism in Korea.

- Protection of international patients' rights is among the outstanding issues lacking clarity in Korea's medical tourism industry. KHIDI claims to be unique: it is among the few government-operated organizations assisting patients to resolve malpractice disputes. KHIDI cites minimal infrastructure in place to protect both patients and physicians, such as the National Commission on the Settlement of Medical Disputes to resolve medical malpractice issues. Patients receiving treatment in Korea who file for malpractice are subject to Korean jurisdiction. KHIDI also offers malpractice insurance for foreign patients as well as a multilingual around-the-clock medical call center to mediate conflict resolution. The interplay of foreigners' health insurance with the resolution of a medical malpractice disputes needs to be further developed.

  Further expansion of clearly delineated obligations for both patient and medical provider during and after treatment needs detailed elaboration. If a patient encounters complications from a procedure upon return to the home country, a comprehensive protocol should be in position to ensure both the patient's welfare and legal rights. As mentioned, some ROK hospitals maintain partnerships with hospitals in other countries, notably the United States. In some cases, patients who return home and experience a medical complication may receive follow-up treatment in a partnership hospital. These hospitals, however, may be geographically accessible to only some patients, further complicating or jeopardizing a patient's health. The government should legislate appropriate measures to ensure patient safety and the integrity of the Korean health care system.

- The expression "medical tourism" may be a mismatch of Korean marketing and reality. Korean "medical tourism" is heavily focused on the "medical" component of the industry, with the "tourism" component an apparent addendum. The global images of "Medical Korea" and "Dynamic Korea" suggest that Korea is technologically and medically innovative, but do not deliver in projecting a powerful tourism element. The term "medical tourism" could be changed to "global health care" if Korea chooses to asymmetrically focus on delivery of health care over tourism. Alternatively, Korea could exploit its tourism industry in conjunction with its health industry: a more accurate marketing campaign and more integration with the tourism industry may help Korea further propel its economy and enhance both sectors.

IX. CONCLUSION: TOWARD A HEALTHY GROWTH OF MEDICAL TOURISM

The South Korean medical tourism industry has made remarkable progress since its official, government-endorsed inception in 2007. Medical tourism is no longer a novelty; rather, it is transforming into an institution that promises to generate profit for the Korean economy. Given the challenges identified, however, there are some caveats regarding Korea's current medical tourism system that pose challenges to both suppliers and consumers of its medical services. Below are some considerations and conclusions that may be drawn with respect to the ROK's evolving medical tourism industry:

- The medical tourism industry is profitable, and Korea is in only the nascent stages of its cultivation.
- Korea is becoming a viable competitor in the medical tourism arena, but it remains to be seen if it will be able to further distinguish itself from the more established competing Asian nations.
- The adage "buyer beware" rings true: Korea's medical tourism is not a panacea. Its system comes with many caveats: there remain cultural hurdles to overcome; continuity of medical care may be interrupted; and assurance is needed for the delivery of evidence-based medicine that contributes to a high-quality and credible system. It takes a

medically sophisticated tourist to have truly informed consent in order to select the appropriate treatment and distinguish charlatans from legitimate sources of care.

- Enhanced technology is among Korea's potential comparative advantages, but does not guarantee that medical care will be improved. Care will be better only with the use of evolving application of evidence-based medicine.
- A consequence of the two-tiered pricing scheme is *discriminate* care. This may have both domestic and international ramifications for both patient and medical provider if not seriously addressed at the government and hospital levels.

There is value in considering a Korean health care delivery solution. The current challenges identified provide fertile opportunity to further harness and enhance Korea's medical tourism industry. Further government regulation is necessary to address these challenges and translate Korea's breakthrough in the medical tourism industry into a long-term sensation.

CHAPTER IV:
IDENTITY AND SOCIETY

Searchers and Planners: South Korea's Two Approaches to Nation Branding

By Regina Kim

I. INTRODUCTION

"Nation branding," a concept first developed over a decade ago by British government advisor Simon Anholt, is the practice of creating a positive image of a country, leading to a more favorable perception of that country by the outside world. The national brand of a country is largely a reflection of its soft power, and since exerting strong soft power can enhance a country's influence and competitiveness in the international community, countries are increasingly turning their attention to improving their national brands. Perhaps no other country in the world has tried so aggressively to improve its national brand in recent years as South Korea. In South Korea, there are currently two main forces of nation branding: the country's official nation branding campaign, which was launched by the South Korean government in 2009, and the Korean Wave (*Hallyu* in Korean), the Korean pop culture craze that began in the 1990s, led mainly by the private sector.

The two drivers of South Korea's nation branding—the Korean government and the Korean entertainment industry—may share a common interest in enhancing Korea's image abroad, but they fundamentally differ in their approaches to promoting Korean culture. The Korean government seeks to design and implement its nation branding projects using a top-down approach, in which plans are initiated and decisions are ultimately made by a council. Plans are subsequently brought to fruition by various Korean organizations. In contrast, the Korean entertainment industry's agenda seems to be largely fueled by market demand. That is, the industry responds to the demands of consumers of Korean pop culture. This difference in approach can be likened to William Easterly's comparison of planners and searchers in his book *The White Man's Burden: Why the West's Efforts to Aid the Rest Have Done So Much Ill and So Little Good*. In the first chapter of the book, titled "Planners versus Searchers," Easterly explains why the efforts of advanced countries and multilateral institutions have largely failed to help the world's poor by contrasting "planners" with "searchers." Unlike national governments and multilateral aid institutions (the "planners"), some NGOs and private companies have taken a "searchers" approach to development aid and have been relatively successful. That is, instead of setting unreasonably high goals and attempting to execute grandiose projects through layers of bureaucracy, they try to figure out where the demand is and what the reality is like on the ground, adapting their strategies accordingly to satisfy their targeted beneficiaries. Although Easterly used this theory in reference to international aid, we can apply his "planners versus searchers" dichotomy to Korea's nation branding activities.

This paper will compare the Korean Wave "searchers" approach and the Korean government "planners" approach to South Korea's nation branding efforts and will attempt to assess their respective strengths and weaknesses. It will assess which approach is more effective in upgrading Korea's national brand, or if some combination of the two should be used. Finally, it will conclude by suggesting some general policy recommendations for the future direction of Korea's nation branding efforts.

II. THE KOREAN GOVERNMENT'S NATION BRANDING CAMPAIGN

Formation of the Presidential Council on Nation Branding (PCNB)

When the Anholt-GfK Roper Nation Brands Index, the most widely accepted measurement system for national brands, ranked South Korea thirty-third out of 50 nations in its 2008 edition, President Lee Myung-bak vowed to improve South Korea's national brand to be on par with the OECD average—to raise it 18 spots to fifteenth place by 2013, to be precise. On January 22, 2009, in order to accomplish this objective, he established the Presidential Council on Nation Branding (PCNB) and appointed Euh Yoon-dae, a former president of Korea University, as its chair. Euh considered South Korea's low ranking in the brand index as "a shame for Koreans," noting that there existed a huge gap between the reality in South Korea and its perceived brand image that needed to be rectified.

Role and Structure of the PCNB

The mission of the PCNB (otherwise referred to as "the Council" in this paper) is to educate other countries about South Korea, with the ultimate goal of improving Korea's status and image in the world, correcting misperceptions about Korea, and increasing other people's respect for Korean individuals and businesses. The Council's hope is that raising Korea's recognition and standing in the world will result in Korean individuals being more respected by foreigners; more people wanting to visit or live in Korea; and Korean products and services being valued more highly. The main functions of the Council include: 1) overseeing and coordinating nation branding projects; 2) implementing nation branding–related policies and projects in an effective manner; and 3) cooperating with the private sector as well as the general public in formulating ideas and executing projects. The Council plans medium- to long-term strategies, sets medium- and long-term objectives, and reviews the outcomes of its projects every year to make any necessary adjustments. While ideas and suggestions for improving the nation branding campaign are welcomed from the public (both Korean and non-Korean), the campaign's strategies and policies are still initiated and ultimately decided on by the Council.

The Council is composed of 47 members (34 appointed members—most of whom are professors or CEOs of Korean companies—and 13 ex-officio members from the government) and 34 international advisors who sit on five different committees: planning, international cooperation, business and IT, culture and tourism, and global citizenship. The chair who heads the Council is appointed by the South Korean president. The current chair is Lee Bae-yong, who succeeded the Council's inaugural chairman, Euh Yoon-dae, in September 2010. The Council also has a Secretariat composed of government officials seconded from various Korean ministries. The Secretariat works with the chair and the committee members to plan and execute the Council's activities.

The Council's Strategy

The Council's main objectives for its nation branding campaign are: 1) to increase Korea's commitment and contribution to the international community; 2) to help Koreans become responsible, respectful global citizens; and 3) to promote Korean products and services. The Council's strategy to achieve these objectives consists of four parts. First, it seeks to cooperate closely with the private sector and the general public to carry out its branding efforts. Second, the Council has been attempting to manage Korea's brand power by establishing a "master plan" and by developing Korea's own nation-brand index. The third part of the Council's strategy consists of tailoring its policies to fit the needs of different regions around the world. Fourth, the Council aims to create and maintain a strong momentum behind its branding campaign by fostering a "common national response" with the participation of the private sector and the public.

The Ten-Point Action Plan

In March 2009 the Council devised the following 10-point action plan for carrying out its campaign:

1. "Shaping the Future with Korea." Help developing countries achieve rapid economic growth by providing them with technological support and by applying Korea's development model to their cases.
2. "Campus Asia." Provide funding for international students to study in Korea. Promote exchanges of university students and talented young professionals between Korea and other Asian countries to build a pan-Asian network of future leaders.
3. Dispatch 3,000 volunteers abroad every year as part of the World Friends Korea program, launched in May 2009 as the Korean counterpart of the United States Peace Corps. The volunteers teach people everything from math to sports to IT, as well as methods for improving medical treatment and agricultural productivity, and other skills the local people might need or request to learn. Emphasis is placed on personal interaction between the volunteers and the locals, in line with the Korean government's belief that developing such trust and cooperation on an individual level can be more effective and sustainable than simply donating money to these countries.
4. "Global Korean Network." Establish a single network that connects all Koreans living overseas and use them as a resource for promoting Korea abroad.
5. Promote certain aspects of Korean culture such as Korean cuisine, language, and *taekwondo*, and develop Korea's tourism industry.
6. "Global Citizenship." Help Koreans become global citizens by conducting a TV campaign to encourage Koreans to treat foreigners better and improve their etiquette (whether in Korea, abroad, or on the Internet).
7. Promote Korea's technological achievements and high quality products abroad and more closely associate Korea's successful corporate brands such as Samsung, Hyundai, and LG with Korea's national brand. However, this project has run into some difficulties, since many of these famous Korean conglomerates are reluctant to acknowledge their brands as being Korean because of the "Korea discount"—that is, the cheaper value that is often given to Korean

products because of the lower prestige that they are perceived to have. The government's purpose here is to help turn the "Korea discount" into a "Korea premium."

8. Help the increasing number of foreigners and multicultural families better assimilate themselves into Korean society by providing them with economic and other types of assistance, including better health care and education.
9. Promote online communication and information sharing between Koreans and foreigners to improve cross-cultural awareness and understanding.
10. Periodically assess the campaign's progress and evaluate Korea's national brand power.

Of course, many of the components of the action plan are interrelated and reinforce each other. For instance, the Korean government hopes that by fostering global etiquette among Koreans and by encouraging them to embrace multiculturalism, it will make Korea a more attractive tourist destination.

Results of the Nation Branding Campaign

The PCNB's planners approach to nation branding is most evidently exemplified by this ambitious 10-point action plan. Whether this approach has been successful is yet to be determined; considering the fact that the Korean government's nation branding campaign was not launched until 2009, it may still be too early to thoroughly assess the impact it has had on improving Korea's brand image in Asia and elsewhere. We may still have to wait for at least another year or two before we can confidently determine to what extent the campaign has enhanced Korea's national brand. Nevertheless, there are some signs that the campaign might be beginning to have some sort of impact on raising Korea's brand power. For instance, while Korea was ranked thirty-third in the Anholt-GfK Roper Nation Brands Index in 2008, it moved up two spots to thirty-first in 2010.

Moving beyond mere numbers, however, the Council seems to have the right idea in devoting much of its campaign efforts to assisting developing countries. In the recent past, numerous government officials from developing African countries had approached the Korean government and expressed their desire to learn from the Korean development model. As a result, the Korean government began its World Friends Korea program, sending Korean volunteers to Africa and other developing regions. Volunteers are placed in these countries for about two years, during which time they befriend the local people and teach them valuable skills in technology, medicine, farming, and more. In Burma, Korean volunteers from this program have been teaching the local population effective farming techniques; in Africa, they have been helping African villagers maintain cleaner and safer communities in order to reduce the incidence of malaria and other diseases. Since the start of the program, small yet noticeable improvements are beginning to occur in some villages in Africa.

III. THE KOREAN WAVE

*The Origins and Development of the Korean Wave (*Hallyu*)*

The second major force of Korean nation branding has been the Korean Wave, or *Hallyu*, as it is called in Korean. The term *Hallyu* itself (which literally means "Korean Wave") was coined by the Beijing media around 1999–2000 to describe the surge in popularity of Korean pop culture in China. Today, the term is used to describe the spread of Korean pop culture throughout Asia, as well as to other parts of the world. The Korean Wave phenomenon can be arguably divided into four stages: 1) the beginning stage (1993–97), when Korean pop music and dramas first started becoming popular in mainland China; 2) the growth stage (1998–99), during which Korean pop culture spread to other Asian countries, including Taiwan, Hong Kong, and Vietnam; 3) the peak (2000–2004), a period in which *Hallyu* became a notable cultural phenomenon that was sweeping across virtually all of Asia, especially Japan and Southeast Asia; and 4) expansion (2005–present), a period in which the Korean Wave has been spreading to other regions of the world, including the Middle East, Latin America, and Africa.

The Korean Wave, unlike Korea's nation branding campaign, has been largely the result of a searchers approach used by Korea's private sector. Instead of mapping out a grand strategy for exporting Korean culture, individual media and entertainment companies have simply responded to rising consumer demand (both at home and abroad) for Korean dramas, films, and later, pop music. Each stakeholder in the Korean Wave—be it Korean actors, musicians, directors, producers, CEOs of entertainment companies, or others—simply continues doing what s/he does best and contributes in his/her own way to the Korean Wave (and indirectly to Korea's national brand). The overall result is that Korea continues to produce high-quality cultural contents that appeal to consumers, thereby sustaining the Korean Wave. Thus, the Korean Wave was not "a planned current" designed by any entity, but "an international cultural response caused by enthusiastic reactions from consumers."

The Korean Wave has hit a total of about 70 countries in Asia, the Middle East, Africa, Eastern Europe, and Latin America. Korean dramas such as *Dae Jang Geum* and *Winter Sonata* have been particularly successful, boosting the popularity of the Korean actors and actresses who star in them and also raising Korea's image in the process. While a few years ago, Korean dramas were at the forefront of the Korean Wave, recently Korean pop music has taken the lead. "K-pop" concerts regularly sell out throughout Asia, and it is common to hear contemporary Korean music blaring in cafes and malls in various Asian countries. In addition, Korean films, though not as successful as Korean dramas or music, have gained international recognition at major film festivals such as the Cannes Film Festival, where Korean films such as *Old Boy*, *Thirst*, and *Poetry* have won awards.

Korean celebrities have become the faces of the Korean Wave and Korea's unofficial cultural ambassadors (although many of them have been appointed by the Korean government as official cultural ambassadors). They have brought enormous economic and intangible benefits to Korea directly through product advertisements in other Asian countries for various Korean companies. Much of the Korean celebrities' impact on the Korean Wave is indirect, however. For example, when foreign fans like a Korean singer, they might also become interested in the singer's clothes, hairstyle, and the products s/he uses. They may begin copying Korean fashion and buying Korean cosmetics and food. Their desire to emulate their Korean idol leads them to learn about and appreciate other aspects of Korea. In this way, the Korean Wave has had a multiplicative effect in encouraging many foreigners to embrace various elements of Korean culture.

A 2005 report published by the Samsung Economic Research Institute (SERI) shows the effect of the Korean Wave as a four-stage process. In the first stage, foreigners become avid consumers of Korean dramas, movies, and music; at the time of the report's publication, Mexico, Egypt, and Russia were identified as examples of countries falling into this category. The second stage involves these consumers buying products that are directly derived from Korean pop culture (such as accessories worn by a Korean actress in a Korean drama) and visiting Korea after watching Korean dramas and films and/or listening to Korean music. At the time, Japan, Taiwan, and Hong Kong were labeled as being in this second stage. In the third stage, foreign consumers buy Korean electronics and other everyday items made in Korea; China and Vietnam were cited as two countries who have reached the third stage. In the fourth and final stage, the foreign consumer admires Korean culture and prefers the Korean lifestyle; as of 2005 no countries were identified as having yet reached the final stage. However, more recent years suggest that it is possible that Thailand could be placed in this fourth category, as many urban youth in Thailand have been eagerly copying Korean fashion trends (sometimes even to the detriment of their own health!) and attempting to look and act Korean, to the point that a former Thai minister of culture expressed his concern that the Thai youth had forgotten their own culture.

East versus West: Measuring the Impact of the Korean Wave

The Korean Wave has had a markedly positive impact on Korea's tourism industry and economy and seems to have been the driving force behind the growing foreign interest in Korean culture. At its height in 2004, the Korean Wave was shown to be responsible for an estimated increase of $1.87 billion—the equivalent of 0.2 percent of Korea's GDP at the time—in Korean exports and tourism, according to statistics published by the Korea International Trade Association (KITA). Furthermore, out of the 968,000 foreigners who visited Korea in 2004, 647,000 (67 %) of them cited the Korean Wave as their main reason for visiting Korea. The Korean Wave has also improved Korea's image in countries such as Japan, which has had a long history of enmity with its neighbor. After Korean dramas such as *Winter Sonata* became a hit in Japan, the percentage of Japanese who claimed to like Korea increased to 55 percent in 2004. Among younger Japanese in their 20s and 30s, the percentage was over 60 percent (in 2004).

Owing to the spread of Korean pop culture throughout Asia, Korea became the world's ninth-largest exporter of cultural content in 2008, and it still remains in the top 10 today. However, not all of the results of the Korean Wave phenomenon have been positive: its enormous success has also led to a backlash in certain Asian countries. A 2010 study of the major newspapers in five Asian countries—Japan, China, Thailand, Indonesia, and Singapore—found that while the Korean Wave did not spark intense negativity towards Korea or Korean culture per se, it did cause some journalists to express their concerns that the Korean Wave was spreading too fast and that Korean cultural products (not only films and dramas but also pop music and games) were taking over their domestic markets.

Although the Korean Wave has had resounding success in Asia and has even reached parts of the Middle East, Latin America, and Africa, it has yet to make an impression on the U.S. audience. For instance, K-pop artists such as Rain, BoA, and Seven—all of whom have enjoyed enormous popularity in Asia—have tried to break into the U.S. market but have largely failed. Korean movies have been screened in select theaters in major U.S. cities, but on the whole, they have not yet made any noticeable impact on the way ordinary Americans generally view Korea. And while Korean dramas are broadcast on certain cable channels in the United States, the overwhelming majority of viewers are of Korean descent.

There are many possible explanations for why the success of the Korean Wave has not carried over to the United States. First, the American public generally does not like to watch a movie or television series filmed entirely in a foreign language with a cast of foreign actors. Moreover, Asians and Asian Americans have been traditionally underrepresented in the U.S. media, which makes it all the more difficult for Korean dramas and films to find a receptive audience in the United States. Korean films are also produced with a much lower budget than many Hollywood movies, which can greatly affect their overall quality. Korean dramas explore themes and values that the Korean people share with many other cultures that are more traditional, collectivist, and hierarchical than the United States, which partly accounts for the success of Korean dramas in unlikely places such as the Middle East and Latin America. Such traditional values may not resonate as well with an American audience.

The Korean pop culture craze in Asia has led many Asians—especially the younger generation—to view Korea as the epitome of cool. If one lived in Asia, one would probably be inclined to think that Korea's brand power ranked within the world's top five (instead of in the 30s). The fact that Korea currently has a very strong brand image in Asia but not in the West perhaps shows that the Anholt-GfK Nation Brands Index (as well as some of the other nation-brand indexes) has a Western bias. In light of this, perhaps it is impossible to come up with an objective, global index that accurately assesses national brands, since the strength of a country's brand power will inevitably vary according to region. As if in acknowledgment of this inherent bias, Simon Anholt and GfK Roper recently published an online, interactive version of their nation brands index, in which users can select and customize search options to see how a country is perceived in different countries of the world.

IV. CHALLENGES AND POTENTIAL LIMITATIONS TO EACH APPROACH

Both the Korean Wave and the PCNB's nation branding campaign face their own set of challenges. In the PCNB's case, its creation of a grand strategy for all branding activities is a classic example of the planners approach (and, as Easterly indicates, it is also a main reason why so many development aid efforts have failed). Although some amount of coordination is needed, too much planning could be rather cumbersome and inefficient (the Council's 10-point action plan actually consists of 100 smaller action plans). A large degree of flexibility and adequate room for creativity are needed and expected, especially in the realm of branding and promotion. In addition, while the Korean Wave allows people to naturally come to like Korea by learning Korean songs and watching Korean dramas and movies, the Council's overall campaign is, in effect, using a supply-driven approach by actively promoting Korea (though a few of the campaign's particular projects are rather demand-driven—more about this later). However, no matter how passionate one may be about a certain cause, idea, or culture, one cannot *force* other people to appreciate it. If the Council is too aggressive in its approach, this could incite a backlash from other countries, as we have already seen with the Korean Wave. At the same time, however, the campaign could lose its momentum if those who are involved lack the drive to sustain it. Thus, the Council needs to keep a careful balance between maintaining the campaign's momentum and not appearing too aggressive in its promotion of Korea.

The Council also needs to welcome more input from foreigners. While outside input may not be as important for the private sector since market results are often an automatic and simple indicator of success, such input is crucial for a government campaign to succeed since it must be conducted with prior knowledge of what are the elements of Korean culture that would appeal to foreigners and how best to market those elements. Despite the Council's purpose of promoting Korea abroad, there are currently no foreigners who work as paid employees of the Council's Secretariat—the entire staff is composed of Korean government officials. Currently, there are no plans to recruit foreigners to work for the Secretariat. The international advisers on the Council are prominent foreigners working in Korea who have been invited by the Council to join as volunteer (unpaid) members. These advisers play a rather minor role in the campaign: they do not work with the Council regularly, and they are limited to giving advice—often via email.

There has been limited participation from the Korean public as well, a fact that the Council hopes will change in the future. Furthermore, despite the Council's effort to engage the private sector in its campaign, there has been minimal cooperation between the two so far. However, cooperation is starting to grow and will likely continue to do so in the future. Finally, there is also the risk, however unlikely, that the Council and/or its nation branding campaign will disappear altogether when the Korean administration changes in 2012.

The Korean Wave faces two major constraints on its sustainability. First, as Korean drama and movie productions become more expensive, funding becomes strained, so entertainment companies are forced to ask the government for financial support. In response to their demands, President Lee decided to create a special government fund for Korean movies; however, even this has proved to be inadequate, so entertainment companies are now turning to other countries for help with funding. Therefore, budget constraints can undermine the global competitiveness of Korean films and dramas.

Second, while Korean pop culture has been thriving in Asia and some other regions of the world, it has failed to make a noticeable impact on advanced Western countries (namely the United States and Western European countries). This may indicate a limited appeal of Korean pop culture to certain cultures. It may also imply that Korean pop culture does not have the multiplicative effect in these areas that it does in Asia. For instance, although numerous Korean movies have garnered awards at film festivals throughout Europe, they have generally not led their European viewers to become interested in other aspects of Korean culture (as Korean movies and dramas have done with Asian audiences). Thus, in order for the Korean Wave to continue to thrive and to spread to the West, it needs to broaden its scope by including other aspects of Korean culture, such as Korean food, traditional Korean music, and the Korean language.

V. IS A MORE INTEGRATED APPROACH NECESSARY?

General Cooperation between the Government and Private Sector

As we have seen, the PCNB's nation branding campaign (the planners approach) and the Korean Wave (the searchers approach) each has its own advantages and disadvantages. The planners approach used by the PCNB implies a great need for careful coordination—and the more numerous and more ambitious the projects are, the more difficult overall coordination becomes. At the same time, however, some coordination is desired to minimize overlap and reduce budget waste. And while the Korean Wave's searchers approach has proved remarkably successful so far in raising Korea's image in select regions of the world, the strong tendency of Korean companies to seek projects that will ensure economic profit implies that such an approach is risk-averse. In other words, many Korean entertainment companies desire to stick to established markets that have already been proven to be successful (e.g., Asia) rather than risking entering into new markets where the demand for Korean pop culture may be small or nonexistent (e.g., the United States).

Thus, it appears that a higher level of cooperation between the public and private sectors (and thus cooperation between the PCNB's nation branding campaign and the drivers of the Korean Wave) is optimal—as long as each party knows its roles and the government does not interfere too much with the private sector's activities. Careful coordination between the public and private sectors means that the Council should maintain the momentum of its branding campaign but also needs to be careful about not heavy-handedly promoting Korea. If the Korean government and the private sector were able to work synergistically together to upgrade the Korean brand and did a good job of complementarily blending their efforts, the result could be a surprisingly efficient and effective nationwide campaign.

Large private companies could cooperate more with the Council by agreeing to associate their products and services more with the Korean brand. Perhaps the Korean government could even make it mandatory for these companies to put "Made in Korea" labels on their products. At this point, brands such as Samsung and LG are already respected enough worldwide that alerting consumers that they are Korean companies will not cause their products to suffer from a Korea discount. Failing to acknowledge that these corporate brands are Korean will only perpetuate misperceptions about them. For example, in 2007, Anderson Analytics, a market research firm, conducted a survey of 1,000 American college students about their knowledge of global brands. Out of those surveyed, 58 percent thought that Samsung was a Japanese brand; 42 percent said that LG was an American brand; and 56 percent thought that Hyundai was a Japanese brand. Only 10 percent correctly answered that Samsung was a Korean brand; for LG, the number of correct responses was even smaller—9 percent. Hyundai fared a bit better, with 25 percent correctly recognizing it as a Korean brand. Simply letting consumers know that the products they love to purchase are Korean by adding the word "Korea" will only raise Korea's image in their minds.

Government Support of the Korean Wave

In some areas (for instance, the promotion of Korean entertainment—and hence, the Korean Wave), the Korean government should continue to play a minimal role and allow the private sector to take the lead, providing it with legal and financial support if necessary. Regarding legal issues, the government must carefully consider all of the potential ramifications of providing legal support to the entertainment industry. For instance, the 2005 SERI report on sustaining the Korean Wave states that the economic returns from the Wave have not been as large as they would have been otherwise due to the prevalence of piracy. The report suggests that hence, the Korean government should take more action to prevent piracy of Korean media. However, it is unclear to what extent the government should take measures to limit piracy. Such policies could potentially backfire, as they might prevent foreigners from having easy access to Korean media and thereby limit their consumption of Korean pop culture content, leading to a slowdown in the spread of the Korean Wave.

As for providing financial support, the Korean government could help Korean entertainment companies overcome their risk-averse tendencies in choosing their overseas markets by subsidizing some of their overseas projects. The government could also help fund innovative film projects and Korean indie artists, as they might find a more receptive Western audience. (Note, for instance, how films by directors Kim Ki-duk and Hong Sang-su are adored by many Western fans yet are not popular among Koreans. Many Westerners also probably would not like the manufactured sound of the Korean pop vocal groups that largely represent Korea's mainstream music today.)

In addition to providing legal and financial support, a third way in which the Korean government can support the Korean Wave without being overly involved is by continuing to play a crisis management role—that is, by stepping in to manage or prevent anti-Korea or anti-Korean Wave sentiment in other countries. To cite an example of how the Korean government has done this in the past, the release of the Korean drama *Winter Sonata* in Japan sparked a harsh outcry against the Korean Wave from the Japanese government, who claimed that Japanese wives were neglecting their husbands because of their obsession with the drama and its male protagonist (portrayed by actor Bae Yong-joon). The Korean government intervened by convincing the Japanese government to lessen its criticism and by urging Korean media companies to cool down their marketing efforts for a while. The government's efforts paid off, and the Japanese backlash against the Korean Wave subsided as a result. The Korean government should continue to intervene in such crises in the future.

The government should also continue supporting cultural exchanges between Korea and other countries, particularly in Asia, to reduce the likelihood that the Korean Wave will be seen as a unidirectional "cultural promotion scheme" for Korea. However, doing this may not be enough; if the Korean Wave becomes too successful, to the point where it is perceived as a threat to the domestic culture—as has already happened in certain Asian countries—anti-Korean sentiment can arise even if cultural exchanges are occurring between the two countries. Again, in such situations, the Korean government should respond by playing its role in crisis management.

A fifth and final way for the Korean government to support the Korean Wave is by investing more in maintaining historical and cultural sites, as well as other potential tourist attractions, so that visitors who are drawn to Korea by the images they see on screen will not be disappointed when they arrive in Korea. This disparity between the generally high expectations of tourists who come to Korea because of the Korean Wave, and their subsequent disappointment when they realize that the reality of Korea does not always quite match the Korea they have fantasized about, has often been pointed out as an important problem that needs to be addressed.

Sticking to the Tried and True and Responding to Feedback

Besides supporting the Korean Wave in such ways, the Korean government (particularly the Council) should also focus more on areas in which it has already proved to be successful, and in which there is already a high demand from foreigners that cannot be adequately met by the private sector alone. For instance, the government should continue to be actively involved in promoting volunteer programs such as World Friends Korea. In the case of World Friends Korea, the government has used the searchers approach, in a sense, as countries had approached the Korean government eager to learn from Korea's development model. The Korean government states that it is simply meeting the demands from these developing countries. Perhaps the government could employ the searchers approach more often in determining what foreigners would like to see from Korea (e.g., asking more foreigners which aspects of Korean culture—or culture in general—might appeal to them) and in pinpointing areas in which there is a demand for Korean help, or at least where Korea could possibly step in and make a difference. The government could then implement its projects by assigning different tasks to different agencies and adjusting its projects according to the feedback it receives from people on the ground (e.g., Korean volunteers working in other countries—this would be more in line with the searchers approach). In such a scenario, the government would be simultaneously using both the planners and searchers approaches in a mutually reinforcing manner.

VI. CONCLUSION AND RECOMMENDATIONS

Thus, in summary, a more integrated approach—a mix of both the planners and searchers approaches—would probably be the best way for the Korean government to move forward with its nation branding campaign. Similarly, the Korean Wave would probably be most effective when the private sector and the government work together, but with the government in a subordinate and supportive role (ideally, government support should be "invisible" whenever possible). In his book *Korea Brand Power*, Youn Jung-in illustrates a good example of the Korean private sector and the Korean government (or rather in this case, a government official who happens to be Korean) working together to help other people and improving Korea's image in the process. In June 2010, Hyundai, the Korean auto company, launched its project of donating a *million* soccer balls to kids in Africa who dreamed of playing professional soccer but could not practice the sport because they did not have enough soccer balls. The company asked Ban Ki-moon, the UN secretary general, to have the UN give the soccer balls on its behalf. When one of the African delegates to the UN found out about this, he was reported to have publicly said that none of the UN member countries, except for Korea, had ever done anything good for Africa.

Such an example shows how the Korean private and public sectors could work together to accomplish small miracles and raise Korea's image in the eyes of other countries. However, as mentioned earlier, the most effective approach to Korea's nation branding activities would not only be built on cooperation between the government and private sector, but would also incorporate more input from the Korean public and from foreigners in the planning and execution of nation branding projects. The PCNB needs to have more young, creative, internationally-minded, and multilingual people working for its campaign, and particularly as part of the PCNB's Secretariat, which is mainly responsible for implementing the Council's projects. Currently the Secretariat is composed of seconded government officials, many of whom may be working on the campaign only because they have been placed there by their respective ministries. Moreover, these government officials usually work on the campaign for only a couple of years or so before they are brought back to their own ministries or transferred elsewhere, often making it difficult to initiate, execute, and sustain large-scale projects. The layers of bureaucracy within the Council and the relatively high turnover within its Secretariat, if not addressed, could prove to be two major barriers to the campaign's future progress.

Instead, recent college graduates (both Korean and non-Korean) should be recruited into the Council to bring in fresh new ideas. Today's youth, especially those in Korea, are extremely internet-savvy and adept at using social media, which are essential tools for brand promotion in the current world. The older members of the Council may focus more of their efforts on problem-solving, ODA, crisis management, and the like, but the promotional aspect of the nation branding campaign should really be left up to these younger recruits who, in general, have a tendency to be more creative and are more in step with the times. Not only does the Council need such fresh, creative, young talent, but it should also hire foreigners who have an understanding of both Korean culture and their native cultures as paid employees, since such people are best able to see how messages can be conveyed effectively from Korea to their homelands. Currently, only a select group of prominent foreign professionals working in Korea have been hired as international advisors for the PCNB—but these are volunteer positions, and many of the advisors do not seem to have much influence in the campaign.

If Korea really wants to improve its national brand, it needs to not only do a better job of publicizing the PCNB's efforts, but to also consider ways to fundamentally change the structure of the PCNB and the operation of its campaign—otherwise, the campaign may be doomed to stagnate or fizzle in the future.

The North Korean Refugee Policy of the Lee Myung-bak Government: Nationalism and Multiculturalism

By Narae Choi

I. INTRODUCTION

There are nearly 20,000 North Korean refugees currently residing in South Korea, and that number is growing at an accelerating pace. According to a Korea Institute for National Unification (KINU) survey, however, in the midst of the Sunshine Policy between 2003 and 2005, the public perception of North Korean refugees by the South Korean population ranged from empathy to indifference. Anecdotal evidence suggests that increased tensions between the two Koreas—such as those following the *Cheonan* and Yeonpyeong Island incidents—instigate anti-North Korean sentiments that extend to North Korean refugees and are informed by Cold War-era anticommunist propaganda. On the other hand, the emphasis on Korean solidarity based on *minjok* continues to penetrate official and public discourse championing North Korean refugees and unification. Yet, how pervasive is the argument based on ethnic purity in the increasingly multiethnic cosmopolitan Korean society? How does the Korean government reconcile its unification and North Korean refugee policy based on the rhetoric of ethnic homogeneity with its campaign of embracing diversity, as Korean society struggles to adapt to the presence of *others*, North Korean refugees in particular?

This paper seeks to answer these questions. First, it will provide a short survey of differing views on North Korean refugee policy in light of increasing diversity in South Korean society. The following section will examine the ideological stance of the Lee presidency manifested in different government bodies. Based on this analysis, this paper will also make policy recommendations.

II. SHORT SURVEY OF CURRENT STATUS AND IDEOLOGICAL BACKGROUND ON ADMINISTRATIVE DESIGNATIONS OF NORTH KOREAN REFUGEES IN CONJUNCTION WITH MULTICULTURAL FAMILIES

According to the Ministry of Unification, the number of North Korean refugees entering South Korea each year has trended upward since 1998. By December 2009, cumulatively, 17,985 North Korean refugees had entered South Korea. Although North Korean refugees account for only approximately 0.037 percent of the South Korean population, their struggle to adjust to South Korean society is widely known. Jih-un Kim and Dong-jin Jang categorize such difficulties in their 2007 *Asian Perspective* article, "Aliens among Brothers? The Status and Perception of North Korean Refugees in South Korea": economic difficulties due to lack of professional skills, language barriers, discrimination, and poor health; educational maladjustment; emotional distance from South Koreans; and severe culture shock.

On the other hand, diversity has been another factor of change in contemporary South Korean society. As of 2009, South Korea has 580,000 migrant workers, 170,000 marriage immigrants, and 110,000 immigrant children, according to the Presidential Committee on Social Cohesion. In total, there are more than 1,100,000 immigrants and foreigners in South Korea, amounting to 2.25 percent of the South Korean population. This growing multiethnic population in a historically homogeneous society has sparked interest across mass media. The process through which South Korea has transformed from an ethnically homogeneous state to its current state is well documented in Kim Hyuk-rae's 2009 article in *Korea Observer*, "Contested Governance in Making of Multicultural Society." According to Kim, labor shortages in the late 1980s introduced migrant workers into Korean society and despite a brief hiatus during the Asian Financial Crisis of 1997, this trend has continued to date. Moreover, Korea's gender imbalance initiated another wave of immigration in the form of international marriages beginning in the 1980s. This trend also continues to grow, primarily between foreign women and rural farmers. Scholars, such as Yoonkyung Lee, argue that migrants and foreign brides brought changes to the South Korean identity of ethno-nationalism, as she highlights South Korea's struggle between nationalism that led to political and economic success and the present reality that calls for a multiethnic and diverse society.

Emerging Discourse: Shift in Administrative Definition of North Korean Refugees?

In many ways, the North Korean refugee population and multicultural families (다문화가정 is a term broadly used in official and public discourse to designate immigrants and immigrant families) are two of the most important minority issues that the South Korean government has been grappling with since the 1990s. In this context, there is an emerging discourse on how to provide care and services for North Korean refugees. This section will briefly discuss the two sides of the debate: the traditional and prevailing notion of North Korean refugees as a part of Korean nation in its own special category, and the more novel view of them as a part of a broader category of social minorities.

There are two different lines of reasoning behind the opinion that North Korean refugees should be supported as and separated into their own category. The emotional response stemming from the memories of civil war and division, as well as a nationalistic "Korean solidarity" based on one Korean ethnicity, are still acute. Furthermore, North Korean refugees strongly reject being grouped into other minority groups, emphasizing the view of North Korean refugees as "blood brothers."

On the practical side, many argue that most North Korean refugees acquire significant physical and psychological trauma as they escape North Korea, hide for years, and lose families and friends. Furthermore, they argue that unlike other social minorities and foreign-born South Korean nationals, North Korean refugees need fundamental training to cope with life in a capitalist society. Finally, they consider the North Korean refugee situation as a practice run for larger influxes of refugees and, eventually, unification.

On the other hand, those who prefer North Korean refugees to be treated as members of a broader category of minorities also have different viewpoints. Some argue that viewing North Korean refugees as brothers of one nation inevitably focuses on their inability to successfully adapt. Others point out that there's an existing channel of similar welfare distribution and care for both North Korean refugees and multicultural families, which means additional bureaucratic overhead and waste. Why not merge and cut costs?

Where Does the South Korean Government Stand?

North Korean refugees symbolize one of the last bastions of Cold War politics—a tangible tie to the arch-enemy-brother. But more than an artifact of the Cold War, the refugees represent a flash point in the political discourse, as their rate of entry grows and the public discourse is dominated by stories of unsuccessful resettlements. The political and social rhetoric of North Korean refugees as "blood brothers of one nation" nevertheless persists. Diversity in the South Korean society poses another layer of complication by pushing the society toward openness and diversity, and away from nationalistic rhetoric. With emerging discourse on how to treat North Korean refugees on an administrative level, how does the South Korean government form its North Korean refugee policies?

III. THE LEE MYUNG-BAK ADMINISTRATION'S STANCE AND ITS EFFECTS

The Lee Administration's Dilemma

The picture of North Korean refugee policy becomes even more complicated when it comes to the Lee Myung-bak government's framework. First, President Lee, just like any other South Korean president, faces an inherent constraint in setting the tone of North Korea-related policy: the South Korean Constitution. The Constitution's mandates are fundamentally nationalist; the preamble of the Constitution declares that "the people of Korea… [have] assumed the mission of… peaceful unification of our homeland and [have] determined to consolidate national unity with justice, humanitarianism and brotherly love." Article 4 specifies that unification is one of South Korea's national goals, which is reemphasized in article 66, paragraph 3, as the duty of the president. Promoting "national culture" is also mentioned twice, in articles 9 and 69. If the Lee administration considers North Korean refugee policy as a subcategory of North Korea and unification policy, then it is likely to employ the same line of rhetoric, traditional and nationalist. If, however, the administration considers North Korean refugee policy as a subcategory of broader social welfare policies, then its approach may differ, seeking the framework capable of maximizing the effect of limited resources.

Regardless of the constitutional mandate, however, North Korean policy has not been the center of Lee's presidency. After two consecutive progressive presidents who championed the Sunshine Policy toward North Korea, President Lee was elected on the platform of economic revitalization of South Korea. As a result, there were only a few North Korea experts on his Presidential Transition Committee. Furthermore, it is difficult to discern the Lee government's stance on the North Korean refugee issue from presidential speeches and briefings, for it is rarely mentioned. Therefore, the remaining method of analyzing the Lee administration's orientation is through examining the policy measures of various ministries.

In doing so, this paper has chosen to examine three (out of the 19) ministries involved in North Korean refugee support specified by article two of the Enforcement Ordinance on the Act on the Protection and Resettlement Support for the Residents Who Escaped from North Korea (대한 법률 시행령): the Presidential Committee on Social Cohesion, the Ministry of Unification, and the Ministry of Public Administration and Security. These ministries were chosen by their ideological orientations, which span from the nationalist platform to the Progressive pro-diversity platform.

Presidential Committee on Social Cohesion

The Presidential Committee on Social Cohesion (PCSC) is the youngest of the three government agencies dealing with North Korean refugee issues. It was inaugurated on December 23, 2010, following President Lee's August 15 Independence Day speech, which announced the advent of PCSC directly under the presidential purview. As noted in the *Transition Committee White Paper*, the issues of a multicultural society, migrant laborers, and North Korean refugees are grouped into the issue area of social cohesion (사회통합), which was part of President Lee's campaign pledge as well as a continuing theme.

Goh Kun, former prime minister under President Roh Moo-hyun, chairs the PCSC, which consists of four subcommittees (class, ideology, region, and generation), 48 committee members, and 120 personnel. The North Korean refugees settlement project is under the generation subcommittee, along with the generational workforce coexistence project, family-friendly workplace project, and marriage immigrant support project. According to the Republic of Korea National Budget Assembly office, the budget for PCSC increased from 2,043,000,000 *won* in 2009 to 2,734,000,000 *won* in 2010 (the sixth-largest among direct presidential committees). Although the PCSC does not have the power to enforce its decisions and findings, it facilitates dialogue between ministries and builds consensus. The PCSC's activities thus serve as an experimental venue for different ministries to voice their concerns on preexisting problems, although such concerns may never gain enough consensus to become binding legislation.

The PCSC's North Korean refugee support functions, according to its website, are the following: "discovering success stories, supporting, and correcting the negative view of North Korean refugees through public awareness campaign; coming up with unified responses from the 19 government agencies; involving regional governments' efforts." Of these functions, the supervisory role of 19 government agencies seem to be the most active, as meeting summaries show. During the first meeting of the North Korean Refugee Success Project Subcommittee on March 12, 2010, the PCSC asserted that there is a lack of cooperation among the 19 ministries as well as regional governments, implying that the PCSC's Subcommittee on North Korean refugees would serve as the place of cooperation in forthcoming months. Consequently, officials from the Ministry of Labor, Ministry of Unification, and Ministry of Gender Equality and Family, as well as other related ministries, attended most of the nine meetings held from March 12 to November 26, 2010.

The North Korean Refugee Success Project Subcommittee, however, is not the only place within the PCSC that North Korean issues are discussed. For example, Dasom alternative school is discussed both in the North Korean Refugee Success Project Subcommittee and the Foreigner and Marriage Migrant Subcommittee. Furthermore, the Foreigner and Marriage Migrant Subcommittee takes, at times, a more a proactive role in consensus building on North Korean refugee issues among ministries. In the fifth meeting of the Foreigner and Marriage Migrant Support Project Subcommittee on July 5, 2010, attended by the participants from the Ministry of Justice, Ministry of Gender Equality, Ministry of Culture, Sports, and Tourism, and Ministry of Education, Science, and Technology, Kim Seung-gwon, subcommittee chair, proposed the need for centralizing multicultural family and foreigner policy under the office of the prime minister. Furthermore, he argued that North Korean refugee policy should be under the same umbrella. His reasoning was that the integration of the service system for multicultural families, foreigners, and North Korean refugees, especially on the local government level, would lead to better service to all of the recipients. The meeting's minutes note that the Ministry of Unification is opposing the integration of a support system for North Korean refugees due to the difference in systems, and so do many North Korean refugees. Such record implies that there is an underlying ministerial disagreement surrounding the North Korean refugee policy resource allocation, based on differing perspectives of North Korean refugees—whether the issue is a minority group or unification preparation.

In short, the PCSC offers a vignette into the interaction among the Lee government's ministries and their differing views on North Korean refugees: grouping of North Korean refugees with multicultural families for practical reasons or North Korean refugee policy as a unification exercise. Furthermore, the meetings held at the PCSC as well as the virtual lack of nationalistic rhetoric or mention of unification on its website imply that although the PCSC endeavors to build consensus among ministries, it leans toward the former view, opposing the Ministry of Unification.

Ministry of Unification

The Ministry of Unification (MOU) evolved out of the 1968 National Unification Board, and officially became a ministry on February 28, 1998. Although its beginning was largely symbolic, the Ministry of Unification became more powerful as the North-South dialogue intermittently resumed in the 1960s and 70s. It reached its zenith under President Kim Dae-jung and President Roh Moo-hyun, with the construction of the Kaesong Industrial Zone and the establishment of the Mount Geumgang tour as well as the convening of historic North-South summits. The current head of the agency is Hyun In-taek, a former member of Lee's Presidential Transition Committee and the Presidential Council for Future and Vision. The MOU's 2009 budget was approximately 2 trillion *won*, of which, 83.5 billion *won* was allocated for North Korean refugee support; its 2010 overall budget is approximately 2.7 trillion *won* (see appendix).

The MOU underwent a near existential crisis under President Lee's Presidential Transition Committee, as the Transition Committee seriously considered plans to merge the Ministry of Foreign Affairs and the Ministry of Unification, as documented in the *White Paper*. However, in the end, due to strong opposition from minority parties, the Ministry of Unification remained as an independent ministry.

The MOU experienced another shock in the wake of the 2009 North Korean nuclear crisis. North-South relations soured, and most of its main functions and projects became defunct or were downsized. It was the turning point at which the MOU began to focus its resources on North Korean refugee support, which was becoming more visible and important in South Korean society. The shift is shown in the sharp increase in 2010 North Korean refugee project–related budget, which was 30 percent larger than its 2009 budget.

The MOU's North Korean refugee support is under the purview of the Humanitarian Cooperation Bureau, along with North-South cultural exchanges, humanitarian aid, and family reunions. According to the *2010 Practical Manual for North Korean Refugee Settlement Support* (2010북한이탈주민 정착지원 업무 실무편람) the North Korean refugee resettlement support policy is "the touchstone of [South Korea's] will and ability for unification"; therefore, the MOU compares North Korean refugee resettlement to "a mock-trial" for unification. In order to successfully support the refugees, the MOU emphasizes the Consultative Council to Deal with Dislocated North Koreans (북한이탈주민대책협의회) to bring together the 19 government ministries and connect them with local governments and the private sector.

Unlike the PCSC, the MOU employs nationalistic rhetoric throughout its projects, according to its namesake *raison d'être*, about the preparation and execution of successful unification. MOU vice-minister, Um Chong-sik, in his *Financial News* column on October 17, 2010, described unification as "the springboard for the Korean nation's big jump." According to the MOU website, one of the purposes of the South-North Cooperation Fund is to contribute to national community, closely mirroring the views of President Lee. The MOU also reinforces the Lee administration's vision of activating sociocultural exchange; harking back to the Constitution, it pledges that through exchange, we will heighten the national-community sentiment, and bring back the homogeneity of the two Koreas. Most recently, the MOU named its 3.8 million *won* project for unification planning and human capital management "South-North Community Foundation Project," and one of the subprojects is called "national community."

Moreover, the vice-minister's remark summarizes how the ministry channels unification into current focus: the North Korean refugee policy. In his speech for the Volunteerism for North Korean Refugee Pledge Rally on October 14, 2009, the vice-minister argued that "North Korean refugees who share our language, culture, and history are not even getting the same attention that multicultural families and migrants of different languages, culture, and history get."

In short, the MOU represents the traditional ethno-nationalistic values that most strongly adhere to the Constitution, and rejects the multiculturalism umbrella for North Korean refugee issues. The MOU is more closely tied to North Korean refugees and better acquainted with their concerns than any other ministry. Nevertheless, the MOU's desire to be the near one-stop solution for North Korean refugee support suggests the ministry's interest in maintaining the current scope and level of control over the issue is firm—fueled by the demise of yesteryear's main projects, such as the Geumgang tour and Kaesong Industrial Zone.

Ministry of Public Administration and Safety

In 2008, President Lee Myung-bak formed the Ministry of Public Administration and Security (MOPAS) from two separate ministries formed in 1948—the Ministry of Government Administration and the Ministry of Home Affairs—as well as the Civil Service Commission, the National Emergency Planning Commission, and the national informatization strategy functions of the Ministry of Information and Communication. The current minister is Maeng Hung-kyu, a former member and spokesperson of the Grand National Party and senior secretary to the president for political affairs. MOPAS is the biggest of the three government agencies, with a 45 trillion *won* budget (see appendix) and more than 607,628 civil servants.

Of the 45 trillion *won*, the budget for North Korean refugee support is a minuscule 343 million *won*, which means that MOPAS has little responsibility regarding North Korean refugees. MOPAS, however, is not planning on remaining in a minor role. In 2010, MOPAS commissioned a comprehensive report from the New Asia Research Institute on North Korean refugee resettlement, which sampled 10 percent of the North Korean population (1,800) and conducted one-on-one and group interviews. The report was subsequently reviewed by two MOPAS officials, who concluded the following: by utilizing the recommendation from the report, the MOPAS will be able to gradually cement its position as a de facto future ministry of unification. If this statement reflects the general consensus within the MOPAS ranks, the bureaucratic politics surrounding North Korean refugee policies becomes even more complicated, beyond the clash of nationalistic and multicultural views.

MOPAS currently plays a small role in providing services to the North Korean refugee population. It is marginally interested in the integration of support systems for multicultural families and North Korean refugees, but does not share the PCSC's and other ministries' goals to integrate different government agencies to create a cohesive policy. Nor does it emphasize the ethno-nationalistic rhetoric of the MOU. However, MOPAS recognizes the important role that the MOU is expected to play in case of the North-South reunification. MOPAS's goal, at least according to two commentators on the NARI report, is clear: to gradually replace the MOU in order to become a more powerful player in the aftermath of unification. In short, the bureaucratic politicking surrounding the North Korean refugee issue, and by extension, unification, has already begun.

The Lee Administration's Contradictory Rhetoric

Deciphering the Lee Myung-bak administration's overarching stance on North Korean refugees by analyzing the Blue House's official statements and speeches is difficult, because the issue is rarely discussed; when it is discussed, it is done so briefly. Thus, this paper turned to three different ministries and the manifestations of the overarching policy agenda: whether it considers the North Korean refugee issue as a subcategory of North Korea and unification policy, or as a subcategory of welfare policy for minorities.
The result is mixed. On one hand, the MOU's North Korean refugee support funding, as well as its push for "one-stop service" for North Korean refugees, is increasing; North Korean refugees should be treated with eventual unification in mind, the MOU argues, with its continuing nationalistic rhetoric. On the other hand, the PCSC is showing other ministries' growing interest in the administrative designation of North Korean refugees as a part of other minority groups. Finally, MOPAS subscribes to the view that North Korean refugees are an integral part of preparing for unification, but shows little interest in nationalistic rhetoric.

Thus, it seems as though the Lee Myung-bak administration is not seeking to eliminate the contradiction in championing both multiculturalism and national solidarity based on ethnic purity by choosing one of the two platforms: the unification preparation platform or the social welfare platform. This, perhaps, is a result of the administration's priority that categorizes the North Korean refugee issue as of second tier importance, unworthy of full articulation. The Lee administration has allowed different ministries to negotiate the overarching policy with each other and through forums such as the PCSC. The Lee administration's lack of clear direction, however, has allowed each ministry's agenda to shape the discourse. The result is a mixed bag—as efforts to build consensus between the two opposite views on North Korean refugees continue, the institutional rivalry between the MOU and MOPAS is developing.

IV. POLICY RECOMMENDATIONS AND CONCLUSIONS

Faced with a choice between the rhetoric of multiculturalism and that of ethno-nationalism, the Lee Myung-bak presidency chose neither. Such ambiguity has allowed ministries to pursue their own agendas and interests. The PCSC, with a multicultural bent, has tried to integrate the North Korean refugee support system into that of multicultural families, and has sought consensus among different ministries. The MOU continues its ethno-national rhetoric, guards its responsibilities, and refuses to consider the integration of the two support systems. MOPAS is mostly concerned with becoming in charge of unification management, the first step being North Korean refugee support. The Lee government needs to take action to ameliorate the situation, but how?

First, this paper recommends that the Lee administration adopt more coherent rhetoric toward North Korean refugees. The PCSC's current role is indecisive and advisory at its best; it often excludes representatives from the MOU and MOPAS. The Lee administration should also articulate a cohesive policy across different government agencies in order to maximize the benefit of limited resources and to eliminate contradicting policies and inefficiencies.

Second, there needs to be more active debate on the integration versus separation of the two issues—North Korean refugees and multiculturalism. Although combining both services would be beneficial in utilizing limited resources in the short term, the MOU's assumption that the current support for North Korean refugees as a practice run for unification is valid.

Third, in order to prevent and reduce competition between ministries for resources and control in the aftermath of unification, the Lee government should build post-unification scenarios, complete with roles for each ministry.

In the end, without a stronger drive for consensus building and steering from the Lee presidency, this trend of institutional competition may escalate further, along with the societal toll from the escalating flow of North Korean refugees. When the South Korean government cannot solve the institutional and ministerial differences surrounding fewer than 20,000 North Korean refugees, it is difficult to imagine unification. Either the rhetoric of unification or the way the North Korean refugees are dealt with needs to change if the administration wants its positions to appear based in reality.

V. APPENDIX

Table 1. Budget for North Korean Refugee–Related Projects

Ministry	Project Description	2009 Million KRW	2010 Million KRW	% Increase
Ministry of Unification(MOU)	North Korean Refugee Settlement Administrative Support	₩6,331	₩13,245	109%
	Digital Cataloguing of North Korean Refugee and Separated Family Support	₩109	₩142	30%
	Hanawon Operation	₩1,637	₩7,582	363%
	North Korean Refugee Education, Training, and Settlement Subsidy Support	₩55,510	₩62,539	13%
MOU total		₩63,587	₩83,508	31%
Ministry of Public Administration and Security(MOPAS)	[North Korean Refugees'] Reunion with Former Northern Province Residents, Unification School's normal and professional curriculum, North Korean Refugee Progress Direction Seminar, Former Northern Province Residents Event Participation Support	₩358	₩343	-4%
MOPAS Total		**₩358**	**₩343**	**-4%**

Table 2. Total Budget for MOU, MOPAS, MOL, and MOHW

Ministry	General Account		Special Account		Funds		Total	
	2009	2010	2009	2010	2009	2010	2009	2010
Ministry of Unification	₩4,715	₩5,042	_	_	₩15,086	₩22,279	₩19,801	₩27,321
Ministry of Public Administration and Security	₩319,550	₩311,932	₩4,919	₩5,268	₩129,465	₩133,548	₩453,934	₩450,748
Ministry of Labor	₩11,157	₩11,422	₩670	₩786	₩193,033	₩188,558	₩204,860	₩200,766
Ministry of Health and Welfare	₩181,766	₩196,083	₩4,293	₩3,202	₩843,983	₩845,664	₩1,030,042	₩1,044,949
Unit: 100,000,000 KRW								

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