

# Korea's Economy

# Korea's Economy 2009

Korea's Near-Term Economic Prospects and Challenges

Global Financial Crisis and the Korean Economy: Issues and Perspectives

The Impact of U.S. Financial and Economic Distress on South Korea

The Wall Street Panic and the Korean Economy

Economic Policy Reforms in the Lee Myung-bak Administration

Tax Reform in Korea

U.S.-Korea Economic Relations: View from Seoul

U.S.-Korea Economic Relations: A Washington Perspective

Engagement on the Margins: Capacity Building in North Korea

North Korea and International Financial Organizations: Political and Economic Barriers to Cooperation

a publication of  
**the Korea Economic  
Institute and the  
Korea Institute for  
International  
Economic Policy**

**Volume 25**

---

## CONTENTS

### Part I: Overview and Macroeconomic Issues

#### Korea's Near-Term Economic Prospects and Challenges

*Subir Lall and Leif Lybecker Eskesen* . . . . . 1

#### Global Financial Crisis and the Korean Economy: Issues and Perspectives

*Pyo Hak-kil* . . . . . 8

### Part II: Financial Institutions and Markets

#### The Impact of U.S. Financial and Economic Distress on South Korea

*Thomas Cargill* . . . . . 15

#### The Wall Street Panic and the Korean Economy

*Kim Dong-hwan* . . . . . 25

### Part III: Structural Reform

#### Economic Policy Reforms in the Lee Myung-bak Administration

*Tony Michell* . . . . . 33

#### Tax Reform in Korea

*Randall Jones* . . . . . 45

### Part IV: External Issues

#### U.S.-Korea Economic Relations:

##### View from Seoul

*Han Dongman* . . . . . 55

##### A Washington Perspective

*Jordan Heiber and*

*Jennifer Schuch-Page* . . . . . 64

### Part V: North Korea's Economic Development and External Relations

#### Engagement on the Margins: Capacity Building in North Korea

*Bernhard Seliger* . . . . . 67

#### North Korea and International Financial Organizations: Political and Economic Barriers to Cooperation

*Lee Sang-hyun* . . . . . 76

# U.S.-KOREA ECONOMIC RELATIONS: A WASHINGTON PERSPECTIVE

*By Jordan Heiber and Jennifer Schuch-Page*

“America is strongest when we act alongside strong partners,” the White House declared within days of President Barack Obama’s taking office in January 2008. The statement went on to stress a renewed commitment to achieving U.S. foreign policy goals by building U.S. alliances to meet the common challenges of the twenty-first century, noting that now is the time for a new era of international cooperation that strengthens old partnerships and builds new ones. Secretary of State Hillary Rodham Clinton placed specific emphasis on the role of Asia in this effort and echoed President Obama’s words when she made the region her first overseas visit as secretary of state. “I am going to Asia to reassert our commitment to our allies and partners in Asia, to work on a range of issues with Japan and South Korea, China, and Indonesia,” she said, shortly before departing for the Pacific.

For decades, the United States has maintained strong ties to Asia through bilateral alliances, multilateral forums, the presence and protection of the U.S. military, and sustained economic leadership in the region. Perhaps nowhere in Asia is continued U.S. engagement as crucial as in Korea. As the United States and others work to eliminate North Korea’s nuclear program, critical progress is being made on easing regional tensions, yet the dividing line between North and South Korea remains the most heavily militarized border in the world.

## **Deep Economic Ties Strengthen the U.S.-ROK Connection**

Much attention has rightly been given to U.S. cooperation with South Korea in the six-party talks. Forged during the Korean War, the U.S. security alliance with the Republic of Korea (ROK) has been a pillar of regional security for more than 50 years. Security cooperation will continue to be a key pillar of the U.S.-Korea alliance in the twenty-first century. However, it is no longer the only pillar.

The United States and South Korea today enjoy deep and strong economic ties, evidenced by the dramatic expansion of this economic relationship in recent years. South Korea has become both East Asia’s third-largest economy and the seventh-largest trading partner of the United States. In 2008, bilateral goods trade between the United States and the ROK surpassed \$80 billion for the second consecutive year, including nearly \$35 billion in U.S. goods exports to South Korea’s rapidly growing consumer economy. According to Department of Commerce statistics, U.S. business investments in South Korea totaled \$27.2 billion by the end of 2007, and ROK investments in the United States surpassed \$13 billion.

The U.S.-Korea Free Trade Agreement (KORUS FTA) has the potential to further anchor long-standing U.S. ties with this vital regional ally and to underscore the economic pillar of a future-oriented bilateral alliance. And, as the first U.S. FTA with a North Asian partner, the KORUS FTA highlights U.S. engagement in the Asia-Pacific.

## **Cooperation during Crisis**

The global economic crisis presents a very challenging environment. The United States and Korea can utilize our strategic partnership to work together to find ways to alleviate current economic pressures.

Like much of the world, South Korea has been hard hit by the ongoing global financial and economic crisis. The South Korean economy is one of the most trade intensive in the world, with two-way trade accounting for more than 75 percent of its GDP, making Korea especially vulnerable to the combination of a severe international financial crisis and the ensuing export demand-depressing economic slowdown.

Despite these challenges, the United States and South Korea have worked both bilaterally and

multilaterally to address stress in global financial markets. In October, the U.S. Federal Reserve and the Bank of Korea agreed to a \$30 billion currency swap arrangement to provide greater dollar liquidity during the current period of market stress. The swap was subsequently extended through October 2009. More recently, Korea has been admitted to the Financial Stability Forum, which promotes international financial stability through information exchange and international cooperation in financial supervision and surveillance.

The magnitude of the current global financial and economic crisis requires the government of every country to similarly examine its domestic policies and offer solutions that benefit its citizens. Regardless, no nation can risk overlooking the critical role that international partnerships can play in stabilizing the global economy and putting the world back on the path to economic prosperity. President Lee Myung-bak made this clear when he joined heads of state from the other Group of Twenty nations in Washington, D.C., in November 2008 to discuss solutions to the financial crisis. With the G-20 meeting in London in April 2009, it is clear that both the United States and Korea support open trade and investment regimes.

The ROK will play an even more important role in this process in 2010, when it takes over the chairmanship of the G-20. As we move forward, the U.S.-Korea global partnership can make an important contribution to international efforts to strengthen economic recovery.

### **People-to-People Ties: The WEST Program and Visa Waiver Program**

Speaking at the Korea America Friendship Society in Seoul on 4 December 2008, the U.S. ambassador to the ROK, Kathleen Stephens, noted that “people-to-people exchanges are at the heart of the modern U.S.-Korea relationship.” This has long been true, with tens of thousands of Korean students in U.S. schools, hundreds of thousands of Korean tourists visiting the United States each year, and numerous U.S. citizens living and working in Korea. These connections were dramatically strengthened in 2008, with the development of the Work, English Study, Travel (WEST) Program and with Korea’s inclusion

in the U.S. Visa Waiver Program (VWP). Both of these efforts will directly and indirectly impact the U.S. economic relationship with the ROK through increased personal connections and the exchange of ideas.

In September 2008, the United States and the Republic of Korea signed a memorandum of understanding on WEST in New York. This innovative exchange program will eventually allow up to 5,000 qualifying university students and recent university graduates from the ROK to study, participate in paid professional internships, and travel in the United States for up to 18 months. The first group of WEST participants will arrive in the United States in the spring of 2009. Although the program is still in its infancy, there are plans under way to expand WEST to send young Americans to Korea for a similar cultural and working experience. Mindful of the strain families are feeling during the current economic crisis, the WEST program has been developed to offer a unique opportunity with competitive costs.

Similarly, the recent expansion of the VWP to include South Korea will dramatically strengthen our burgeoning people-to-people ties. More than 800,000 Koreans visited the United States in 2006, a number that has grown significantly as Korean incomes have increased. With Korea’s inclusion in the VWP in 2008, visiting Koreans will find entry into the United States to be a simplified and convenient process. This newfound ease is encouraging to the people of South Korea as a sign of how strengthened bilateral cooperation can directly improve the lives of ordinary Koreans.

Originally introduced as a pilot program in 1986 for only a handful of countries, the VWP has grown to encompass 35 nations, promoting tourism and short-term business visits while allowing the Department of State to redirect consular resources to make its embassy operations more efficient. For Koreans, the benefits of membership are immediate, as VWP travel means shorter visa lines and no-fuss travel to the United States.

These two new programs are having an immediate and visible impact on U.S.-ROK relations. The WEST Program reflects the future-oriented nature of the alliance by providing students with a unique

opportunity to develop foreign language skills and gain professional experience in the international workplace. It will facilitate information sharing between Americans and Koreans, foster increased cross-cultural understanding, and create the foundation for future personal and professional interaction and cooperation. With Korea's inclusion in the VWP, the daily visa line that once stretched around the U.S. embassy in Seoul has all but vanished, and thousands of Korean nationals have arrived in the United States without first having to undergo an interview at the U.S. embassy in Seoul.

In the future the visa waiver program will continue to bring the United States and the ROK closer together by increasing both the quantity and frequency of Korean visits to the United States. Hawaii, for example, is looking at a doubling or tripling of Korean tourists by 2010. While the global economic slowdown and the weakened Korean *won* may slow this influx of Korean tourists in the short term, the broader implications of making it easier and cheaper for Koreans to visit the United States remain unchanged.

### **Stability and Opportunity in Transition**

Korea went through a year of substantial transition when it elected a new president, who took office in 2008. With last year's election of President Barack Obama, the United States is now completing its own political transition. Nonetheless, recent bilateral progress and committed assurances of cooperation by both administrations make the long-term significance of this relationship clear.

Secretary Clinton traveled to Seoul in February to deliver this message in person. The United States continues to look to Korea as both an economic and a military partner, as an ally in Asia with shared values. She represented a United States that is committed to working with leaders in Asia to resolve the economic crisis; ready to strengthen U.S. historic partnerships and alliances, while developing deeper bonds with all nations; and ready to expand combined efforts on twenty-first-century challenges.

*Mr. Heiber and Ms. Schuch-Page work in the Office of Korean Affairs, Bureau of East Asian and Pacific Affairs, U.S. Department of State. Views expressed here are those of the authors and do not necessarily represent positions of the U.S. Department of State or the U.S. government.*



Korea Economic Institute  
1800 K Street, N.W. Suite 1010  
Washington D.C., 20006

PRESORTED STANDARD  
U.S. POSTAGE  
PAID  
PERMIT #3777  
WASHINGTON, DC