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# Cho Tae-Hyon: "Foreign Direct Investment in Korea: Recent Trends and Changes to Improve the Investment Environment", Korea Exchange Bank Quarterly, First Quarter, 1995, Vol. xxx, No. 1

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# Cho Tae-Hyon, "Foreign Direct Investment In Korea: Recent Trends And Changes To Improve The Investment Environment", Exchange Bank Quarterly Review, First Quarter, 1995, Vol. xxx No. 1

## I. INTRODUCTION

Korea opened its doors to foreign investors in 1962 to raise capital for economic development. As at end-1994, the total accumulated volume of Korea's Foreign Direct Investment (FDI) on an approved basis amounted to US $12,525 million financing 4,709 projects. The conclusion of the Uruguay round and the establishment of the World Trade Organisation (WTO) which linked the global economy to free flows of trade and investment, are new challenges facing Korea in the search for ways to cope with the emerging era of unlimited competition. Tae-Hyon's paper attempts to review the trends in FDI and the recent incentives to promote a healthy environment in Korea which would provide the impetus for a much higher level of foreign capital inflow. The article is organised in four parts. Part I is the introduction, Part II presents Korea's recent trends in FDI, Part III focuses on recent changes to improve the investment environment, while Part IV concludes the paper.

## II. SUMMARY OF THE PAPER

2.1 In reviewing the trends in FDI for the 1970's through 1990's, the paper revealed that:-

(i) Foreign capital inflow grew tremendously by over 501.5 per cent in the 1970's because of the establishment of Free Export Zones and the government's support for investors in local heavy and chemical industries. Thus, at $266 million, the value of FDI in 1962 - 1971 grew to $1,600.1 million in the period 1972 - 1981. FDI in Korea stagnated in the 1980's due to world wide economic recession and political uncertainty on the Korea peninsular. Also in the early 1990's, the internal distortions characterized by rapid increases in wages and land prices, sustained high interest rates and inflationary pressures resulted in further reduction in FDI. In fact, FDI dropped from 358 projects valued $1,145.8 million in 1987 - 1989 to 236 investments valued $894.4 million in 1992. However, the trend reversed in 1993 and 1994 due to government's new incentives which included easy foreigners land acquisition, reduction in the excessive retained tax burden, establishment of foreign language institutes and courier service centers.

(ii) Investment was predominantly directed towards the manufacturing and services sectors. Manufacturing absorbed cumulatively $7,675 million in 3,004 investments or 61.3 per cent in value while services sector claimed $4,687 million in 1,425 investments or 37.4 per cent in value as at the end of 1994.

(iii) In terms of country of origin, the amount of FDI in Korea for the period 1962 - 1994 was dominated by Japan and United States, with Japan ranking first accounting for 39.1 per cent of all foreign investments followed by US recording 28.5 per cent.

2.2 The paper identified Korean Government's recent incentives to improve the investment environment to include among others:

(i) the announcement in 1993 of a Five-year Liberalization plan (1993 - 1997) for FDI, focussing on:-

(a) deregulation of interest rates,

(b) foreign exchange liberalization which would gradually allow for a free floating exchange rate system by 1997. Also by this date, mandatory documentation of all exchange transactions will be abolished.

(c) On stock market liberalization, the ceiling for foreign equity investment was eliminated for companies with 50 per cent or more foreign ownership. Also, the allowable ceiling of 15 per cent set for foreign investors participation in portfolio investments for firms listed on the stock market, will be further relaxed by 1997.

(d) The government is expanding opportunities for off-shore borrowing by foreign investment firms taking into consideration, the impact of such borrowing on the domestic monetary policies.

(e) Land acquisition by aliens has been made easy with approvals given within 15 days of application, provided they are used for legitimate business.

(f) Foreigners are now permitted to engage in trading business in Korea, simply by reporting their investment to the authorities instead of obtaining government's prior approval.

(g) Foreign investors in Korea will now be able to set up factories within 45 days of application compared with 200 days or more in the past.

(h) Labour management relations were strengthened and improved to check frequent industrial unrest. The Korean Government encourages the self-resolution of labour disputes since strict enforcement of labour laws may damage long-term labour management relations.

2.3 In the conclusion, the author observed that Korea has favourable investment climate that includes sizeable market, rapidly growing GNP, a well-developed and productive infrastructure and an efficient and disciplined labour force. The paper opined that the present international economic environment where both globalism and regionalism play prominence, globalization of Korean's industrial output including FDI will be useful for the economy.

## III. REMARKS

Countries in need of foreign capital inflow through direct investment must be prepared to package a comprehensive and competitive programme of incentives which could attract foreigners into investing in their economies. These incentives range from economic reforms which will also embrace consistent policies, to providing investment friendly environment. The Korean Five-year Liberalization plan for FDI is a case in point. Also in the West African sub-region, the Ghana Investment Promotion Act, 1994 completely deregulated the investment regime, simplified bureaucratic procedures and made incentives automatic across board to all foreign investment activities in all sectors. The analogy made from the foregoing reveals the need for a well articulated programme of action to attract more foreign investments into Nigeria, in the wake of the repealed decrees in the 1995 budget which hitherto had adversely affected FDI. There is the urgent need to formulate measures that would protect investors' lives and properties as well as guarantee their investments in the country. On the economic fundamentals, the Korean economy experienced a drop in FDI due to internal economic distortions in the 1990s and partly as a result of political uncertainty in the 1980s. Therefore, economic policy thrust that will in turn promote FDI shall be the one that will control the persistent inflationary pressure, stabilize the exchange rate and liberalize interest rates. Finally, it is important to democratize the political environment to give the needed confidence and political stability expected by the international community.

In general, the author has elucidated the trends in FDI and the package of recent incentives available to foreign investors in Korea. The exposition is concise and topical since FDI is suppose to be one of the engines for industrial development in developing economies.

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