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Development Stages and Legal Framework of Public Investment Policy of the Republic of Korea

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Abstract

The practice of foreign countries confirms that with the effective use of attracted foreign investment, there is a change in the nomenclature of production and exports from raw materials in favor of goods with high added value, an increase in the international competitiveness of the economy and the welfare of the population. Countries with well-designed policies to stimulate FDI inflows perform the most positively in terms of economic growth. One of these countries is the Republic of Korea.

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1 Introduction

Investment policy is a set of mechanisms and methods aimed at developing and supporting priority sectors of the economy, the transition from a centralized investment process to a decentralized investment process, and support for priority investment projects. We can say that investment policy is one of the most important means of goal-oriented activities for the socio-economic development of the country. This policy forms the basis of the country's political sphere or serves as the core of the country's political relations, whether it is developed or developing. Investment policy is a mechanism by which the state directs investment in the organization of the production of material goods. From the organizational and legal point of view, this area of public policy consists of the activities of the relevant authorities to identify the goals and objectives of investment policy and seek funding for their implementation.

2 Results and Discussions

Investment policy of the Republic of Korea: development stages and legal framework

One such country is the Republic of Korea. South Korea is one of the countries with the greatest economic success in the last 50 years. From a poor country after the Korean War, it has now become the richest economy in Asia. With decades of great economic success, post-1997 Asian financial crisis development stages, and prudent investment policy in the country's development, Korea is now considered as a development model for other Asian countries.

Numerous studies show that South Korea's economic success is linked to its political reforms aimed at opening up the country to foreign markets, as well as prudent investment policies. Indeed, one of the most important factors in South Korea's success has been its export-oriented policy and the country's strong focus on attracting investment by creating a favorable investment climate (Ahn, 2008; Chung, 2014).

In particular, the Republic of Korea has consistently implemented large-scale programs and efforts to attract investment, focusing on investment policy, opening the country's investment market to both foreign and domestic investors. In turn, the reforms in this process are significant because they are rapid and long-term.

The Korean government considers the intensification of its investment policy to be one of its priorities and identifies the following as specific areas of policy:

- Improving regulations and systems related to foreign investment.
- Reforming barriers for foreign investors.
- Investment support to increase the competitiveness of the industry.
- Improving the structure of industry, development of key industries.
- Development of high value-added services.
- Reform of expanded fiscal policy in winter.
- Expanding the implementation of fiscal and political financing expenditures.
- Reduction of economic uncertainties. Increasing flexibility in the labor market.
- Financial market development, etc.

Unlike other countries in the region, in the Republic of Korea, in the early stages of economic development, special emphasis was placed on import substitution, export promotion, and then heavy and chemical industry (HCI) incentives. Opportunities were created for both investors to improve the environment. In the early days, the main part of the policy was aimed at increasing the absolute amount of capital from abroad by providing benefits commensurate with the volume of investment. Investments that help export or transfer technology or alleviate balance of payments difficulties were also highly valued. But for a long time, technology licensing and international borrowing were preferred to achieve these goals (Crotty & Lee, 2001).

The process of investment liberalization in Korea began in the 1980s and accelerated in the 1990s. In general, the period of investment liberalization can be divided into three stages: the policy of restrictions until the 1980s; the process of gradual liberalization and rapid post-crisis liberalization, along with the attraction of some investment before the 1997 Asian financial crisis (Nini & Sufi, 2009; Harrison & Rodríguez, 2010). Stage 1. Restrictive policy until the 1980s. In particular, in the 1950s, direct investment was not legally allowed, and the Korean economy relied heavily on official support for U.S. development. In the 1960s, when the government switched to export development policy, funds were allocated according to the export potential of firms. There have been some breakthroughs for investors, but the government has opted to license foreign direct investment. Also in 1960, the Law on Attracting and Encouraging Foreign Investment (FCIPA) was passed, which allows the government to increase Korean exports, regardless of the amount or type of investment. Foreign investment is allowed (Karimov & Khojimatov, 2011).

At that time, along with some other Asian countries, free trade zones (FTZs) were established in Korea after 1970 to attract investment in labor-intensive, high value-added manufacturing activities and increase exports and employment, and technological transfer. Through which experience and knowledge were increased among local firms. In 1973, the Economic Planning Council created incentives for the following projects to direct investment in areas necessary for the Korean economy:

- Large complex projects that cannot be implemented by local firms due to limited capital, technology and management skills.
- Export-oriented projects, when it is difficult for local companies to develop or use foreign markets.
- Projects that promote the efficient use of internal resources.

In general, in the early period of industrialization, due to the low level of domestic savings, the Korean government pursued a specific foreign investment policy, giving preference to loans over direct investment. From 1962 to 1980, the total long-term foreign capital was $ 49 billion. Of this amount, commercial loans and borrowings from development agencies accounted for 65 and 32 percent, respectively, of which direct investment accounted for only 3.9 percent (zman-Saini & Law, 2010; Kim & Han, 2014).

Stage 2. The process of investment liberalization in Korea began in the 1980s. In particular, as the investment climate has improved, foreign investment has begun to flow into many business categories. At the same time, the minimum level of investment was significantly reduced from $ 500,000 to $ 100,000. In 1983, when the Law on Attraction and Control of Public Debt and the Law on Control of Foreign Capital were merged, the main direction of direct investment was significant changed significantly. The new law on attracting foreign investment reflects the government's control over foreign direct investment (Kye Woo Lee, 2014; Lutfullaevich, 2020). During the initial liberalization period, which lasted until the mid-1980s, the volume of direct investment in Korea was low. However, in the 1980s, the average annual volume of direct investment in Korea was $ 800 million. Increased to USD (Figure 1).

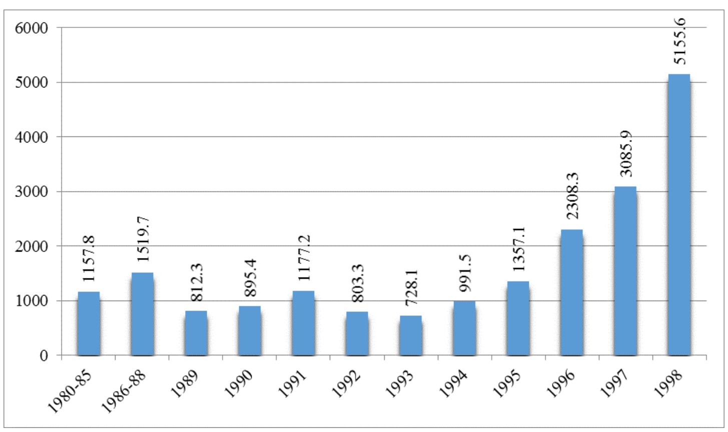


Figure 1. Periodic analysis of foreign investment in the Republic of Korea, 1980-1998 (million US dollars)
Source: Kong Tat Yan The Politics of Economic Reform in South Korea: A Fragile Miracle. - Routledge (UK), 2001. - p. 280. ISBN 0415145031

As can be seen from the picture above, after the contraction that lasted until 1993, direct investment rose to $ 3 billion in 1997 and $ 5.1 billion in 1998. This increase is partly explained by lower stock markets and real estate prices. It also reflects the Korean government's reform of new measures to introduce certain restrictions and incentives in shaping the investment climate and to build on its achievements in reforming the financial and corporate sectors (Nicolas et al., 2013). If we look at the inflow of foreign direct investment to Korea by industry, in the first liberalization period of 1962-86, the largest manufacturing sector accounted for 67.4% of investment. This trend continued until 1993, when the share of the manufacturing sector exceeded 65% of foreign direct investment. The share of production in total foreign investment has been about 55 percent since 1996 (Table 1).

Table 1
The share of foreign investment in industry, 1962-1998 (%)

Industries	1962-86	1987-90	1991	1992	1993	1994	1995	1996	1997	1998
Production	67.4	63.3	80.0	75.3	67.6	35.4	43.2	56. 2	59.4	54.9
Food	3.4	4.5	1.3	13.5	2.0	0.5	I.I	1.8	15.0	12.2
Chemistry	14.2	12.4	15.5	28.5	33.7	11.0	10.0	10.1	8.3	8.3
Medicine	2.8	3.6	4.8	3.8	1.8	3.2	2.9	1.1	1.3	2.3
Oil	3.3	1.5	33.5	0.2	2.8	0.5	3.3	9.3	0.1	0.0
Vehicles	4.2	7.7	9.5	5.9	3.3	7.0	6.5	5.9	3.1	10.4
Electrical Engineering	14.7	17.9	9.1	7.1	3.6	3.7	10.2	12.2	7.1	4.5
Transport equipment	11.2	10.1	2.0	4.2	11.5	3.1	3.4	10.8	11.6	3.0
Other industries	9.9	4.5	4.2	9.2	8.6	5.5	5.2	4.4	12.6	0.6

Source: June-Dong Kim, Sang-In Hwang "The Role of Foreign Direct Investment in Korea's Economic Development: Productivity Effects and Implications for the Currency Crisis", 2000. - p270

The table shows that the structure of domestic and foreign direct investment in the manufacturing sector has changed with more investment in the heavy and chemical industries. Since the mid-1980s, direct investment in labor-intensive and low-tech industries, such as textiles and apparel, has declined significantly due to rising labor costs. Instead, the electrical engineering, transportation, transportation equipment, and chemical industries have received large amounts of foreign investment. After 1997, the share of investment in this sector increased significantly, reaching 15 percent, through the acquisition of foreign food companies by local food companies and their distribution networks (Rodrik, 1991; Ghosh, 2016).

Since 1994, a reform plan to improve the investment climate has been implemented. In particular, the government has announced a five-year plan to attract investment in order to expand the areas of domestic and foreign investment. According to the plan, 132 out of 224 restricted sectors were liberalized. Corporate taxation of investment firms has been reduced, land tenure rules have been simplified and approval procedures have been simplified (Mielnik & Goldemberg 2002).

The concept of attracting foreign investment has been expanded to cover long-term (five years and more) loans, and foreign investors have been allowed to buy shares in local companies through friendly M&A. From 1994 to 1997, 129 service activities were liberalized. In 1997, foreign-run firms were assisted in purchasing land for legitimate business purposes. In 1997, the FCIA revised and promulgated the Law on Foreign Investment and Foreign Investment, which liberalized 47 of the 81 sectors closed to foreign investment caught in the act (Wüstenhagen & Menichetti, 2012; Dahiya & Chaudhary, 2016).

Stage 3. Open Door Policy after the Asian Financial Crisis (1997-98). President Kim Da Jung said, "What we need is, first and foremost, foreign investors. Market reforms and foreign investment are the only solution,"he said, describing the country's investment policy at this stage.

In the process of joining the OECD (2019), the Korean government undertook a number of measures in 1997 and 1998 to further liberalize the investment climate in the country as well as attract investment. One of the consistent steps in this direction was the adoption in 1998 of the Law on the Promotion of Foreign Investment (FIPA). Under the law, the country has worked to attract foreign investment and foreign investment, regulate investment, reduce restrictions, expand tax incentives, and define and regulate systems related to foreign investment, such as foreign investment zones. Under the law, investors can make any foreign investment in the Republic of Korea without any restrictions. Except in the following cases:

- If it threatens national security and public order.
- If it has a detrimental effect on public hygiene or the protection of the environment of the Republic of Korea, or is contrary to Korean morals and customs.
- If he violates the relevant laws of the Republic of Korea.

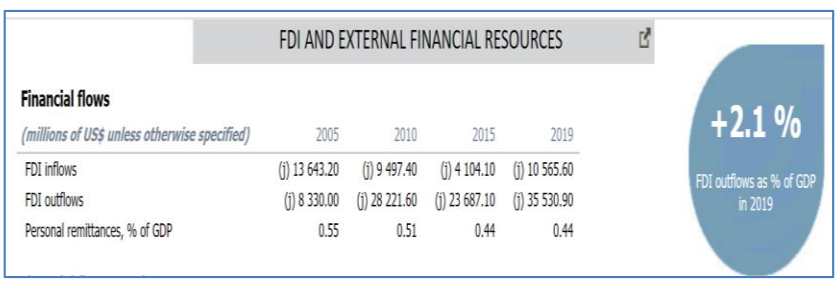
In April 1998, the government accelerated the liberalization of the sectors, including the rental and sale of real estate, securities management, golf course management, grain processing, and direct insurance. Opened ten business categories, including league business. In May 1998, twelve business categories, including gas stations, land production, stock exchanges, investment companies and trusts, electricity and water facilities, were fully or partially opened.

4 Conclusion

In this economic environment, the Korean government has carried out reforms to increase the inflow of direct investment, increase the potential for economic growth, and create a favorable investment climate, first of all, to achieve sustainable growth. . In this regard, President Kim Da Jung said, “Korea’s new policy of attracting direct investment is aimed at catching five birds with one stone, which will not only attract new capital, but also increase the transparency of business management. Increase, hand over advanced management techniques, expand markets and create new jobs, means further development of reforms to improve the investment climate. In particular, in the framework of reforms in Korea, the following work has been done:

- Expanding the definition of foreign direct investment.
- Changes that reflect the changing state of the market through the introduction of the FIZ system.
- Simplification of registration requirements.
- Introduction of an ombudsman for foreign investments.
- Strengthening the system of notification of restrictions on foreign investment.
- Further stabilization of the investment climate.
- Changes aimed at strengthening management functions.
- Opening additional networks for foreign investment.
- Expansion of investment benefits.
- Full-fledged liberalization of cross-border m&a.
- Abolition of the rules on foreign ownership of real estate.
- Simplification of investment processes.

As a result of the above-mentioned reforms, the investment climate in the Republic of Korea has improved and the country has been able to attract large investments in the short term, relying on an active investment strategy (Figure 2).


FDI AND EXTERNAL FINANCIAL RESOURCES

Financial flows

(millions of US$ unless otherwise specified)	2005	2010	2015	2019
FDI inflows	(j) 13 643.20	(j) 9 497.40	(j) 4 104.10	(j) 10 565.60
FDI outflows	(j) 8 330.00	(j) 28 221.60	(j) 23 687.10	(j) 35 530.90
Personal remittances, % of GDP	0.55	0.51	0.44	0.44

+2.1 %

FDI outflows as % of GDP in 2019

Figure 2. Dynamics of foreign direct investment in the Republic of Korea (mln. USD)
Source: UNCTAD, https://unctadstat.unctad.org/countryprofile/generalprofile/en-gb/410/index.html

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