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Multinationals in Asia: The case of the Republic of Korea

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1. Introduction

Although foreign direct investment (FDI) and international production are largely dominated by multinational enterprises (MNEs) originating from the major industrialized countries, there are signs of a growing participation by MNEs from the developing economies. It is estimated that these enterprises account for approximately 4 per cent of the world stock of outward FDI. However, their overseas investments have grown rapidly in recent years and in Asia they have become main channels for industrial restructuring and regional economic integration.

The rapid growth of Asian multinationals (excluding those from Japan) has been one of the distinctive feature of FDI trends in the late 1980s and early 1990s. Annual FDI outflows from Asia were negligible in the 1970s and in the first half of the 1980s, but averaged over 5 billion dollars between 1985-89 and 10 billion dollars in 1990-91 (Jungnickel, 1993). These flows originated mainly from the four newly industrializing economies (NIEs) of east Asia - Hong Kong, the Republic of Korea, Singapore and Taiwan (Province of China). Multinationals from the Asian NIEs can be estimated to have accounted in 1991 for a mere 5 per cent of worldwide FDI outflows but over 80 per cent of the outflows from developing countries (Parisotto, 1993). Significantly, those investment flows accrued mainly to the Asia-Pacific region, where in the late 1980s the Asian NIEs supplanted Japan as the main source of foreign investment in China, Malaysia, Indonesia and the Philippines. The increasing intra-regional nature of this FDI has considerably strengthened economic integration in Asia, pulling together the economies of the region through an intricate network of investment and trade linkages.

It is of interest to observe that while they were the main recipients of FDI in the 1970s, the NIEs are now significant foreign investors and are therefore likely to contribute to economic development in the neighbouring developing Asian countries.

The NIEs achieved fast economic growth and rapid industrialization thanks mainly to their aggressive export-oriented policies. In the 1970s, in order to boost their exports they generally welcomed FDI in assembly and other activities requiring low-grade technology. In the international division of labour, the four emerged as the main suppliers of low-cost and efficient labour for carrying out routine tasks. This trend was part of a process of industrial restructuring which was taking place at the global level. The

economies of the industrialized countries experienced a gradual shift from large-scale production of standardized goods for mass consumption markets to more flexible arrangements such as small batch production for segmented final markets. While those new patterns required, inter alia, a supply of skilled labour capable of carrying out a number of different tasks, cost-saving strategies were actively pursued by relocating the labour-intensive stages of production to other plants or delegating those tasks to subcontractors based in low labour-cost sites in Asia.

In the late 1980s, the NIEs rapidly became exporters of capital, linking a second tier of neighbouring Asian countries in the international division of labour. A quick change in the distribution of locational advantages across the countries of the region helped to accelerate that transition. In the mid-1980s, the NIEs were confronted with sharp increases in domestic wage levels, large trade surpluses, high exchange rates and growing protectionism abroad. In order to face those pressures, they adopted policies to promote a selective transition to capital-intensive production using advanced technologies and redirected their investment into simple, labour-intensive, export-oriented manufacturing in new recipient countries. Those host countries could provide a vast supply of cheap labour, a liberal climate for FDI and, in some cases, preferential access to markets in industrialized economies. The main recipients of that investment were Malaysia, Thailand, Indonesia and the Philippines, and the special economic zones (SEZs) of Mainland China. In the strategies of multinational enterprises, those areas substituted the NIEs as a low-cost production base for exporting to the region and the rest of the world. The host governments encouraged FDI in manufacturing by reducing restrictions on capital inflows and providing facilities and incentives.

The evolution of FDI in Asia is often described in literature as being represented by the so-called "flying-geese" formation. Japan is at the top, being the largest and most advanced economy and traditionally the major foreign investor in the region. Japanese FDI in Asia, in the second half of the 1960s and during the 1970s, was characterized by its concentration in labour-intensive industries and the relatively small size of investment projects. The NIEs were the main recipients. One decade or more later, the original hosts have become prime investors in labour-intensive, export-oriented industries in neighbouring Asian countries and increasingly receive FDI in more complex activities in manufacturing and services. Currently, the main destinations for FDI from the NIEs are China, Indonesia,

Malaysia and Thailand, which are experiencing rapid growth similar to that of the NIEs. In the case of Malaysia and Thailand, the Governments recently took steps to direct foreign investment into technologically advanced industries, while a few enterprises from these two countries have started to invest abroad.

The other Asian countries have remained largely peripheral to the expansion of FDI in the region. However, the recent liberalization of investment regimes in a number of countries may bring about more favourable prospects for foreign investors, primarily in India and Vietnam, and pave the way for the emergence of a third tier in the FDI ladder.

Among the four NIEs, the largest investor was Hong Kong, with an estimated stock of outward FDI of over 20 billion dollars in 1991 (Jungnickel, 1993). Uncertainty about the colony's economic and political future has been a strong motivating factor for the "outward" flow of capital in recent years. However, there has also been a tendency towards closer economic relations between Hong Kong and China as reflected in FDI flows between both countries. Current estimates are that investors from Hong Kong employ between 2 to 3 million mainland Chinese (at about one-sixth of wages in Hong Kong) engaged in the manufacture of simple consumer goods. Hong Kong enterprises have also invested substantially in Indonesia, Thailand, Sri Lanka, Bangladesh and the other NIEs - principally Singapore and Taiwan. Most FDI has been in the production of export-oriented light manufactures such as toys and apparel. However, in Indonesia and Thailand, electrical and electronic products are also produced.

Taiwan, Province of China, is the next largest investor. The growth of FDI was so rapid in 1989-90 that its stock may well have overtaken that of Hong Kong. In 1991, however, FDI outflows declined considerably, although the economy remained a net exporter of capital. Official policy has been strongly influenced by huge balance of payments surpluses, which have been the second largest in the world after Japan. Large investments were undertaken in industrialized countries - mainly in industries producing electrical appliances, chemicals and plastics, and also in the service sector. The United States was the main destination of that investment. Taiwanese investment in China was either unrecorded or routed via Hong Kong. Apart from the industrialized countries and China, FDI from Taiwan is channelled mainly to Malaysia, Thailand and Indonesia.

Singapore, with a stock of outward FDI of about 3 billion dollars in 1989, has invested primarily in China, Thailand, Indonesia and Malaysia. FDI in the manufacturing sector has tended to concentrate on export-oriented labour-intensive products. None the less, capital-intensive activities, trade and financial services and, increasingly, tourism have also become important recipients of investment capital. Local subsidiaries of MNEs from Singapore, based in industrialized countries, account for a significant share of FDI from this country.

This paper reviews the experience of the Republic of Korea. The stock of FDI from the Republic of Korea is not comparable with that of Hong Kong or Taiwan, but it has been growing rapidly and steadily in recent years. The country has the largest and most advanced economy of the four NIEs. Its industrial structure is dominated by a small number of large private industrial conglomerates which play a leading role in Korean FDI. This feature is not replicated in any of the other NIEs, where the industrial structure is highly fragmented. It is likely to account for the sustained growth of international production by Korean firms and an increasing diversification of Korean FDI in the long run. The general characteristics of outward FDI from the Republic of Korea are highlighted in section two (2), while the motivating factors are discussed in section three (3). Section four (4) makes a preliminary attempt at assessing some employment effects which are associated with FDI from and into the Republic of Korea. Some concluding remarks are presented in section five (5).

2. General characteristics of foreign direct investment from the Republic of Korea

2.1 Trends in outward foreign direct investment

Foreign direct investment by Korean firms remained quite limited during the 1960s and the 1970s, but it increased rapidly after 1986. Investment outflows in the 1986-90 period were about six times greater than total FDI outflows from 1968 to 1986 (see table 1). In 1991, annual FDI outflows reached 1 billion dollars and the value of cumulative FDI stood at 3.3 billion dollars or about 1.5 per cent of the country's gross domestic product (GDP).

The first meaningful example of Korean investments abroad dates back to 1959, when the Korean Mining Corporation purchased some real estate in New York. In 1969, the Korean Nam-Bang Development Corporation invested massively

in the forestry industry in Indonesia. Korean firms in transport, trading and manufacturing started to invest overseas in the 1970s. Over the decade, Korean FDI registered a slow but steady rise, and reached a peak in 1978, mainly because of the establishment of overseas branches of trading companies. After an erratic growth in the early 1980s, investment grew rapidly in the latter half of the 1980s. That period of rapid growth coincided with large trade surpluses, as shown in table 1. Considerable outward investment was also made in 1990 and 1991, when the balance of payments became negative. Despite this increase, FDI by Korean firms can still be considered to be in its "infant stage", with good prospects for the future.

An important factor in explaining the growth of Korean FDI was the gradual lifting of domestic regulations on capital outflows. The legal basis for outward FDI was first established in 1968. Thereafter, various guidelines and administrative procedures were introduced by the Government in order to monitor and control the international activities of Korean investors. All investment projects overseas had to be granted permission by the Korean authorities and a committee was established for this purpose in 1981. Since 1986, in order to avoid the inflationary pressures from foreign exchange inflows and to maintain a competitive exchange rate, the Government has made it easy for Koreans to export capital. It has adopted a more liberal investment policy, actively encouraging domestic companies to expand abroad. In its new policy, the Government simplified the procedures for approval of FDI projects, exempted investment of up to 1 million dollars from screening by the competent authorities, allowed individuals to make foreign direct investment and offered tax incentives, credit and other facilities to promote FDI by small and medium-sized firms.

2.2 Geographical and industrial distribution

Traditionally, foreign investment by Korean firms has been mainly directed to two regions: North America and south-east Asia. The two regions together accounted for over 50 per cent of the cumulative FDI outflows over the period 1968-84 (see table 2). That geographical concentration increased further, following the rapid growth of FDI in the late 1980s. In 1990, North America and south-east Asia received 52.3 and 34.4 per cent of annual outflows and their percentages of total cumulative outflows reached 47.3 and 30.6 per cent respectively. That represented about 32 and 42 per cent of the number of

existing FDI projects. Together with the United States and Canada, Indonesia has been the largest destination for Korean FDI and accounts for about one-half of the country's total investment in south-east Asia.

Table 1. Trends in Korean FDI and balance of payments, 1968-91
(US\$ million)

Year	FDI outflows		Cumulative FDI outflows		Current account
	Number of projects	Amount	Number of projects	Amount	
1968-78	181	278.7	220	107.6	...
1979	49	18.8	269	126.4	-4 239
1980	18	15.5	287	141.9	-5 231
1981	34	31.7	321	173.6	-4 640
1982	31	115.9	352	289.6	-2 649
1983	49	96.8	401	386.4	-1 606
1984	31	58.3	432	446.7	-1 372
1985	11	31.5	443	476.2	-887
1986	32	157.2	475	633.3	4 617
1987	59	332.7	534	966.1	9 853
1988	134	153.1	668	1 119.2	14 160
1989	231	324.9	899	1 444.1	5 055
1990	345	891.2	1 243	2 335.4	-2 179
1991	...	1 037.6	...	3 373.0	-8 726

Source: The Bank of Korea: Statistics on foreign investment, various years.

... = Figures not available.

This bi-polar geographical distribution is a main structural feature of Korean FDI and distinguishes Korean investors from those based in the three other NIEs of east Asia. FDI from Hong Kong, Taiwan (China) and Singapore has increased sharply in recent years. However, it has remained overwhelmingly

concentrated in south-east Asia, including the coastal areas of China. Recently there have been signs of a growing diversification in the destination of Korean FDI. In Europe, for instance, it has risen. Europe has been the only other destination to register a relative increase in the late 1980s (see table 2), although investment in this region has not been large. In addition, despite higher than expected local production costs, poor infrastructure and high administrative costs, the Korean firms are endeavouring to invest in the former centrally-planned economies of Asia, and Central and Eastern Europe in order to establish a base in those vast untapped markets. For instance, two leading industrial groups, Samsung and Daewoo, have started to invest heavily in the textiles, consumer electronics and car industries as well as in trading, in the Commonwealth of Independent States (Lilley, 1993).

The impressive growth of investment in manufacturing was a main feature of the surge in Korean FDI. On average, manufacturing accounted for 20 per cent of the value of FDI outflows until the early 1980s. It rose to an average of 40 per cent in the mid-1980s and reached 60 per cent in 1990. In 1991, manufacturing accounted for about 50 per cent of total cumulative FDI outflows. Investment in the primary sector - mainly mining, forestry and fishing - accounted for another 20 per cent. The remaining 30 per cent was made up by the tertiary sector, with investment in trading and, to a lesser extent, in construction and real estate.

Several factors have contributed to make manufacturing the largest source of outward FDI from the Republic of Korea. Overseas investment and international production can be seen as a natural evolution of the aggressive export-oriented growth strategy which was adopted by manufacturers and made an important contribution to the industrial and economic development of the country. From the mid-1980s, FDI was increasingly used as a source of competitiveness by Korean firms which were faced with spiralling local labour costs and shrinking access to the markets of the industrialized economies (see table 3). The hike in wages had an impact on the costs of producing standardized, labour-intensive products, and it significantly reduced the international competitiveness of Korean producers in these export-oriented industries.

More recently, the desire to acquire advanced managerial skills and high-grade technology has been stimulating foreign investment, particularly by the largest enterprises.

Table 2. Geographical distribution of cumulative FDI outflows from the Republic of Korea (selected periods)
(US\$ million)

Region	1968-84				1968-90			
	Number of projects	%	Amount	%	Number of projects	%	Amount	%
North America	156	36.10	144.7	32.50	394	31.70	1 105.5	47.30
South-east Asia	127	29.40	101.6	22.80	522	42.00	714.7	30.60
Europe	43	9.90	10.3	2.30	98	7.90	151.8	6.50
Oceania	18	4.20	81.3	18.20	66	5.30	145.3	6.20
Central and Latin America	29	6.70	56.2	6.70	104	8.40	120.9	5.20
Middle East	38	8.80	31.9	7.20	34	2.70	56.1	2.40
Africa	21	4.90	18.7	4.20	25	2.00	45.1	1.90
Total	432	100.00	444.7	100.00	1 243	100.00	2 335.4	100.00

Source: Bank of the Republic of Korea: Statistics on foreign investment, various years.

Table 3. Annual changes in monthly wages in manufacturing, 1981-89
(per cent)

	Nominal wages	Real wages (a)	Real wages (b)
1981	20.1	- 1.2	5.0
1982	14.7	7.1	9.2
1983	12.2	8.6	7.8
1984	8.1	5.7	2.8
1985	9.9	7.3	13.2
1986	9.2	6.2	4.7
1987	11.6	8.4	15.1
1988	19.6	12.4	18.5
1989	25.1	18.3	21.5

Source: Economic Planning Bureau: Economic white paper, 1990.

Notes: (a) CPI deflator.
(b) GDP deflator.

2.3 Size of the investment and the investors

The average value of foreign investment projects from the Republic of Korea is not large. The 345 projects undertaken in 1990 had an average value of US\$2.6 million, while the total of 1,243 FDI projects had an average value of US\$1.9 million (see table 1). These averages vary widely across regions and industries. By region, the average value of Korean FDI projects was highest in North America and the lowest in south-east Asia and Central and Latin America. By industry, investments were, on average, the largest in the primary sector (US\$21.3 million in mining and US\$7.1 million in forestry), while they were considerably small in transport and warehousing (US\$184,000 on average), construction and trading.

The size of investments also differed according to the size of the investor. The average FDI project by the ten largest Korean corporations was of a value of approximately US\$3.7 million in 1990. Overall, the largest conglomerates played a major role in the expansion of FDI from the Republic of Korea. In 1990, the ten largest Korean corporations invested US\$1.2 billion,

i.e. about 43 per cent of the total FDI outflows. Hyundai had the largest investments overseas (38 projects valued at US\$289 million) followed by Ssangyong, Lucky Gold Star, Samsung and Daewoo. FDI from these five major conglomerates totalled US\$841 million, or 36 per cent of total FDI outflows in 1990.

Korean FDI in the late 1980s was characterized by the emergence of a new category of investors: the small and medium-sized enterprises (SMEs) which employ less than 300 workers (see tables 4 and 5). The share of outward FDI by these establishments rose from 2.7 per cent in 1985 (12.9 per cent of the number of projects) to 9.8 per cent in 1989 (32.6 per cent of the number of projects). In general, FDI from small and medium-sized Korean enterprises was concentrated in manufacturing. According to a recent report, 45.2 per cent of investments by Korean SMEs in 1988 was in manufacturing and 30.6 per cent in trading. The corresponding figures for the large enterprises (i.e. establishments with more than 300 workers) were 18.8 per cent and 50.3 per cent (KIET, 1989).

Table 4. Ownership structure of Korean FDI projects by region, 1988
(number of projects and percentage)

FDI project	Industrialized countries		Developing countries		Total	
	Number of projects	%	Number of projects	%	Number of projects	%
Wholly owned	16	57.0	21	41.0	37	46.8
Less than wholly owned	12	43.0	30	59.0	42	53.2
Total	28	100.0	51	100.0	79	100.0

Source: KIET: FDI in the era of globalization, 1989, p. 24.

The sudden shift to international production by Korean SMEs is likely to reflect the division of labour in the country's manufacturing sector. The SMEs have been relatively more affected by growing domestic labour costs and have increasingly resorted to FDI to regain competitiveness, by relocating production in low labour-cost countries. A similar trend has taken place in

Japan, although there is an important difference in that FDI from Japanese small and medium-sized firms has been more oriented to trading and other services.

Table 5. Ownership structure of Korean FDI projects by size of the investor, 1988 (number of projects and percentage)

FDI projects	Large enterprises		Small and medium-sized enterprises		Total	
	No. of projects	%	No. of projects	%	No. of projects	%
Wholly owned	21	44.7	16	50.0	37	46.8
Less than wholly owned	26	55.3	16	50.0	42	53.2
Total	47	100.0	32	100.0	79	100.0

Source: KIET: FDI in the era of globalization, 1989, p. 24.

3. Why do Korean firms go abroad?

Over the last 30 years, the Republic of Korea has experienced rapid industrialization and high economic growth. In a short period of time, a large and diversified economy has developed, with an industrial structure which is quite advanced when compared with those of other developing countries. Indeed, it is in some respects closer to that of the industrialized nations. The Government has played a major role in this process. Through its seven Five-Year Plans, it heavily and successfully supported selected industries which were thought to be crucial for the economic development of the country. National ownership was protected through a generally restrictive policy on inward FDI. Although it is said that the policy created regional economic disparities, this selective "pick the winner" policy has been quite effective in promoting industrialization. It also fostered the emergence of a few giant conglomerates engaged in large-scale production in industries with a relatively advanced technological content (eg. steel, shipbuilding and consumer electronics).

As a result of its very quick and selective growth, the Korean industrial structure is polarized, with a handful of large conglomerates on the one hand and a myriad of small producers in labour-intensive activities using low-grade technologies (e.g. footwear, garments, low-end consumer electronics, toys, etc.) on the other. This feature must be borne in mind if the scope of and motives for, international production by Korean firms are to be fully appreciated. The bi-polarization of investment between the United States and south-east Asia, for instance, is likely to reflect to a certain extent, the imbalance in the industrial structure of the Republic of Korea. The largest companies had the resources and motivation to set up production units in the sophisticated economic environment of the industrialized countries.

3.1 Outward FDI in manufacturing

Table 6 summarizes some main features of the Korean manufacturing sector. Electrical equipment and electronics, transportation equipment, steel, textiles and food are the largest industries. Together, they accounted for about 50 per cent of both the stock of domestic capital and production in manufacturing in 1990. Korean FDI in the secondary sector is concentrated in the steel industry (23 per cent of total FDI outflows), the transportation equipment industry (13.9 per cent) and in the electrical equipment and electronics industry (13.4 per cent). The share of those three industries in total FDI was slightly over 50 per cent. It mirrored the importance of the largest conglomerates in Korean investment activities abroad. Small and medium-sized producers are involved in industries producing the following products: food; textiles; apparel; leather; footwear; furniture and miscellaneous items. They have also been an important source of FDI, accounting for about 30 per cent of the total.

The aforementioned table allows us to compare the cumulative value of FDI outflows with the value of domestic capital stock and production in each branch of manufacturing. Columns 7 and 8 show two ratios which reflect the relative importance of FDI compared with capital stock and production in each branch. Both ratios indicate that the footwear, apparel, furniture, steel and miscellaneous products industries are those in which outward FDI is relatively more important. International production in these industries is more common and the propensity to invest abroad is highest. They are all among the leading exporting industries in the country. No close correlation could be found between the labour intensity of each branch and the incidence of outward FDI.

Table 6. Domestic capital stock, production and FDI in manufacturing in the Republic of Korea, 1990 (US\$ million)

	Domestic Capital Stock	% (a)	Production	% (b)	FDI Cumulative Outflows	% (c)	c/a	c/b	Labour Index
Food products	3792154	6.41	10625236	7.16	70,868	6.68	1.04	0.93	0.0205
Textiles	6047901	10.22	12235308	8.24	62,075	5.85	0.57	0.71	0.0450
Wearing apparel	1015071	1.72	5104887	3.44	78,415	7.39	4.31	2.15	0.0845
Leather	445057	0.75	2487676	1.68	11,676	1.10	1.46	0.66	0.0374
Foot wear	173522	0.29	826709	0.56	31,026	2.92	9.97	5.25	0.0374
Lumber & wood products	574762	0.97	1387062	0.93	7,992	0.75	0.78	0.81	0.0482
Wooden furniture	1668864	0.61	1152201	0.78	18,981	1.79	2.95	2.31	0.0482
Paper & paper products	1176734	2.82	3994718	2.69	12,885	1.21	0.43	0.45	0.0259
Printing & publishing	3673697	1.99	2403092	1.62	3,704	0.35	0.18	0.22	0.0507
Industrial chemicals	2107637	6.21	6775310	4.56	30,408	2.87	0.46	0.63	0.0103
Other chemicals	1721086	3.56	5847648	3.94	16,330	1.54	0.43	0.39	0.0248
Petroleum refining	265380	2.91	5736216	3.86	2,140	0.20	0.07	0.05	0.0015
Other petroleum & coal products		0.45	1429340	0.96	240	0.02	0.05	0.02	0.0124
Rubber products	1384927	2.34	4144058	2.79	16,181	1.52	0.65	0.55	0.0622
Plastic	1777377	3.00	4048310	2.73	54,370	5.12	1.71	1.88	0.0305
Pottery china & ware	177398	0.30	265022	0.18	2,000	0.19	0.63	1.06	0.0326
Glass	519772	0.88	900033	0.61	1,698	0.16	0.18	0.26	0.0326
Nonmetallic mineral products	2736106	4.63	4739020	3.19	35,570	3.35	0.72	1.05	0.0326
Steel	5995685	10.14	10692289	7.20	244,647	23.05	2.27	3.20	0.0119
Nonferrous metal	1040266	1.76	2821887	1.90	3,375	0.32	0.18	0.17	0.0195
Metal assembly	2885720	4.88	7061301	4.76	13,450	1.27	0.26	0.27	0.0350
General industrial machinery & equipment	3283966	5.55	8834795	5.95	6,290	0.59	0.11	0.10	0.0301
Electrical equipment and electronics	7391148	12.50	21987657	14.81	141,975	13.38	1.07	0.90	0.0297
Transportation equipment	6229528	10.53	13956546	9.40	147,624	13.91	1.32	1.48	0.0257
Measuring medical & optical instruments	577610	0.98	1675950	1.12	4,960	0.47	0.48	0.41	0.0480
Miscellaneous manufacturing products	842773	1.42	2612911	1.76	41,370	3.90	2.74	2.22	0.0694
TOTAL	59150008	100.00	143745082	100.00	1061,150	100.00			

Sources: National Statistical Office: Report on mining and manufacturing survey, 1991; Bank of the Republic of Korea: Current statistics on FDI (unpublished), 1991.

3.2 Motives for FDI

Historically, FDI from the Republic of Korea has been driven by the need to gain access to natural resources and to expand sales in foreign markets. Throughout the 1980s, efforts to service established export markets - by relocating production in low-cost countries, as labour costs rose at home, and establishing production and marketing facilities in final markets - were the main factors motivating Korean FDI.

According to a 1988 survey by the Small and Medium Business Promotion Association, access to final markets has been the main motivation for Korean firms to invest abroad. According to 25 per cent of the replies to the survey, the single most important motive was to overcome protectionism by the industrialized economies. Other motivating factors were to protect established market shares and to take advantage of lower costs of production.

The importance of the various considerations differed according to the characteristics of the host country. Korean FDI has been overwhelmingly directed to the industrialized countries. The major Korean manufacturers have established production facilities in the United States and in the European Community in order to avoid import restrictions and to enjoy the special tariff treatment which is granted to EC producers. The main examples can be found in the consumer-electronics industry. Incidentally, it can be observed that, in the longer run, a commercial presence in the host economy could enable Korean producers to increase the volume of local sales once they have become more familiar with local consumer tastes.

Another way of circumventing protectionist barriers, especially in those industries in which Korean export quotas had already been fully utilized, was to relocate production to those developing countries which had unused export quotas and preferential access to the markets of industrialized countries. The examples can be found mainly in the food, textiles, clothing and footwear industries. Some firms established plants in those Caribbean countries which, by virtue of the Caribbean Basin Initiative, could export more easily to the United States.

According to the aforementioned survey, the desire to obtain advanced technologies and know-how has been a marginal consideration in making decisions to invest abroad. However, in recent years Korean firms, especially the largest corporations, have increasingly invested abroad with the aim of

gaining management skills and advanced technological know-how. For instance, they either acquired small "high-tech" companies in member countries of the Organisation for Economic Co-operation and Development (OECD) or formed joint ventures. A few leading manufacturers in electronics, including Hyundai, have also established research laboratories and plants in Silicon Valley in the United States.

On the whole, however, about 65 per cent of investment outflows to North America - which is the largest destination of Korean FDI - are still in the area of trading. The industrialized countries have been attractive to Korean investors because they provided opportunities for real estate investment.

Table 7. Factors motivating Korean FDI in manufacturing (per cent)

	Motivating factors	Per cent
Horizontal integration	Protect current markets	18.8
	Expand markets	12.5
	Sale of machinery and know-how	6.3
Import protection	Overcome import protection/ export indirectly through a third country	25.0
Vertical integration	Supply of raw material	12.5
Comparative advantage	Lower costs of production	18.6
Acquisition of technology know-how		6.3
Total:		100.0

Source: Small Industry Promotion Corp.: Management of overseas corporation, 1988, page 8.

3.3 Korean FDI in south-east Asia

Foreign investment by local firms, for the purpose of gaining access to markets and technology, is less common in developing countries. The main motivating factors for Korean FDI in such cases have been to take advantage of low labour costs and abundant natural resources. Investments in the south-east Asian region have been mainly in forestry, fishing and mining, as well as copper and petroleum. However, in the second half of the 1980s, the bulk of Korean investment went into manufacturing.

As a result of currency appreciation and a sharp increase in domestic wages, Korean manufacturers gradually lost their international competitiveness, particularly in labour-intensive industries such as clothing, footwear and electrical equipment. The problem was further compounded by industrial disputes and serious labour shortages. Korean workers began to show a preference for employment in the fast-growing service sector, where there are better working conditions. As a result, employers in some industries have been requesting permission to employ foreign workers on a short-term basis.

Korean firms, particularly those that are small and medium-sized, have been relocating to neighbouring Asian countries, often to the export processing zones (EPZs) in Indonesia, Malaysia, Thailand and Sri Lanka as well as the SEZs in China. According to a survey by the Korean Institute for Economics and Technology (KIET, 1989b), low wages have been the main factor motivating Korean firms to invest in the region (see table 8). Access to natural resources and local markets is another major reason.

Table 8: Main factors motivating Korean FDI in manufacturing in south-east Asia, 1988 (number of FDI projects)

Reason	Textiles, footwear and toys	Electronics, electrical products	Chemicals	Others (a)	Total
Low wages	17	21	2	8	48
Access to local markets	-	3	6	4	13
Access to third country markets	2	1	-	2	5
Access to raw material	1	-	1	9	11
Trade barriers	-	-	-	2	2
Other	-	1	-	-	1
Total:	20	20	9	25	80

Source: KIET: World economy and technology news-brief, Nos. 302 (89-213) and 255 (80-166), 1989.

(a) Others: Wood and wood products, cement, etc.

According to data from a sample of Korean firms operating in south-east Asia, the prices of raw materials and other factors of production were higher than envisaged. However, most were optimistic in their expectations for profits. In general, they anticipated the profits to be 1.5 times higher than those which would have accrued from equivalent investment in the Republic of Korea. Sixteen out of 31 firms expected to recover their entire investment within three to five years.

As shown in table 9, firms that had invested in the textile, footwear and toys industries were the most optimistic.

Table 9. Expected recovery time for Korean FDI in south-east Asia, 1987 (number of FDI projects)

Industry	Less than 3 years	3-5 years	5-10 years	Over 10 years
Textiles, footwear and toys	1	6	2	1
Electronics and electrical products	1	2	3	1
Chemicals	-	3	2	2
Other	-	5	3	1
Total:	2	16	10	5

Source: Small Industry Promotion Corporation: Management of overseas corporation, 1988, p. 8.

3.4 Korean FDI in industrialized countries: The competitive advantages of Korean multinationals

In the literature on FDI it is often argued that enterprises investing overseas carry an additional burden - which may be termed "the cost of foreignness" - i.e. the cost of doing business in an unfamiliar environment. Local competitors have the advantage of knowing the markets better and of having privileged relationships with the local economic actors and institutions. Foreign investors, however, have to rely on certain ownership-specific advantages which can be transferred to their operations abroad. These advantages, such as technological know-how, marketing skills and brand names, are the key to their success.

Unlike enterprises from the other Asian NIEs, those from the Republic of Korea have invested heavily in the industrialized countries, largely in the United States and Canada. This FDI, however, can be thought of as being more of a defensive reaction by export-oriented Korean firms than a strategic move to exploit their firm-specific, internationally transferable advantages (Jun, 1985). In other words, while FDI from the industrialized countries is generally motivated by the desire to capitalize on firm-specific advantages, Korean firms have been "forced" to invest abroad primarily in order to defend their market shares in the face of growing tariff and non-tariff barriers in the industrialized countries. As Jun also pointed out, Korean investors did not seem to possess strong firm-specific advantages. They were generally weak in product development and in marketing and technological capabilities, and, obviously, lacked experience in the management of overseas operations. Jun provides figures which show that the costs of production in some Korean plants in the United States and the EC were higher than those incurred before trade barriers were imposed. He also indicates that by investing in industrialized countries, Korean firms tried to maintain their low labour-cost advantage by importing parts from the home country, for final assembly in the overseas plants. That strategy, however, was soon hampered by the imposition of higher local content requirements by host country governments (ibid., page 12).

Over the past few years, the nature of FDI in the industrialized countries by the largest Korean firms has been changing. For example, they have set up research facilities in the United States and acquired small high-tech companies. The number of business alliances and joint ventures with leading foreign firms has also grown. Firm-specific competitive advantages are also gradually emerging and likely to increase in the long term. Korean investors have been learning from their experience in foreign countries. Moreover, the largest conglomerates have become heavily involved in research and development (R&D) and are becoming significant players in the international market for technologically advanced products such as semiconductors, notebook computers and optical fibres (Clifford, 1991). The large size of these corporations enables them to mobilize huge resources, cross-subsidize research and adopt a long-term perspective with regard to their operations. They also have strong government support and benefit from the pool of highly qualified human resources, which is available in the Republic of Korea.

4. Employment effects of FDI

4.1 Employment effects of Korean multinationals abroad

The analysis of the employment effects of foreign-based Korean firms is seriously hampered by the lack of statistics. This section draws on unpublished data on the activities of one major Korean corporation. This corporation, "A", is included in the Fortune list of the top 500 companies worldwide. In 1991, it had 95 affiliates in 27 countries, of which ten were in Asia, seven in Western Europe and five in South America. Thirty-nine of the 95 affiliates were wholly owned. The total capital invested abroad was about 50 million dollars (see table 10), largely concentrated in clothing (32 per cent), trading (31 per cent) and electrical and electronic products (29 per cent). Annual sales were about 4 billion, most of which was generated by the affiliates involved in trading. Overall, the 95 affiliates employed 9,293 workers, including 308 Korean expatriates.

Employment generation was the highest for FDI by corporation "A" in clothing and the lowest in trading. Labour intensity, i.e. the ratio between the number of employees and the value of the stock of capital invested was also higher for the clothing industry. The reverse was true for investments in the electrical and electronics industry. However, as the data in table 11 illustrate, activities in this industry tended to be labour-intensive in the affiliates in developing countries (e.g. China) and capital-intensive in those in the industrialized countries (e.g. the United Kingdom).

On average, for every 1 million dollars invested abroad by corporation "A", 184 jobs were created. By applying this ratio to the overall value of Korean outward FDI, the total direct employment abroad by Korean multinationals could be estimated to be around 60,000 jobs (about 0.3 per cent of total employment in the Republic of Korea). This is a tentative and risky estimate, which is unavoidable because of the lack of data. Most of the jobs would have been generated by affiliates in south-east Asia, where labour-intensive production had been relocated. It is of interest to note that the loss of jobs in the Republic of Korea as a result of FDI is considered to be negligible.

Table 10. Korean FDI and the generation of employment abroad: The case of corporation "A", 1990

	Textiles and clothing	Electrical and electronic products	Trading	Transport	Others	Total
Authorized FDI (US\$ '000)	16 534	19 173	53 527	51	3 360	92 645
Actual investment (US\$ '000)	16 421	14 817	15 576	51	3 360	50 225
Annual foreign sales (US\$ '000)	17 466	372 319	3 595 000	7 748	25 436	4 017 969
No. of Korean employees	116	49	138	1	4	308
No. of local employees	6 331	2 054	512	4	84	8 985
Total employees abroad	6 447	2 103	650	5	88	9 293
No. of employees per US\$1 million invested abroad	392	141	40	97	26	184

Source: Based on unpublished data from corporation "A", 1990.

Since most affiliates only recently established operations abroad, indirect employment generated by these enterprises is probably limited. It is quite likely that this may increase once they become well established in the host countries and procure more goods and services from local suppliers.

Table 11. Average labour intensity of investment by corporation "A", by industry and location, 1990

Industry	Labour (workers/ invested capital)	Index	Comparison with domestic investment
Clothing	Domestic investment	0.0845	
	Outward investment:	0.5178	6.13
	o/w: Indonesia	0.5309	6.23
	Costa Rica	0.2432	2.88
Electrical and electronic products	Domestic investment	0.0297	
	Outward investment:	0.0136	0.46
	o/w: China	0.0725	2.44
	United Kingdom	0.0009	0.03

Source: Based on unpublished data from corporation "A", 1990.

4.2 Employment effects of inward FDI in the Republic of Korea

Foreign direct investment in the Republic of Korea is relatively small by the standards of most developing and industrialized countries. Moreover, given the capital-intensive nature of many foreign ventures, the employment effects of FDI have not been very significant. In both 1978 and 1986, for instance, jobs in firms with foreign participation accounted for less than 3 per cent of total employment in all sectors and less than 10 per cent in manufacturing (see table 12). The impact has been more noticeable in those branches of manufacturing where foreign FDI is concentrated. In 1978, four industries (electrical and electronic products, machinery and equipment, textiles and clothing, and chemicals) accounted for more than two-thirds of total employment in the affiliates of foreign firms in Korea.

As regards the employment that may be generated by foreign investment, two points should be considered. In the case of a merger between foreign and

domestic firms, the number of jobs created is likely to be rather limited. However, such cases are rare in the Republic of Korea. It is also possible that the establishment of foreign ventures may crowd out domestic firms. Thus, the new job opportunities resulting from foreign investment could be lower than indicated in table 12, since workers in local firms may have been displaced following the entry of foreign investors. This is very difficult to measure and so far there have been no attempts to undertake such an exercise.

There are no data on the indirect effects of inward FDI on employment. However, a study on the Masan EPZ, which was established to attract foreign investors in the southern part of the country, suggests that employment in local subcontracting firms has grown considerably since the EPZ was set up in the early 1970s. According to the study, there were 75 firms in the Masan EPZ in 1988, with a total of 33,080 workers. Those firms had subcontracting arrangements with 525 Korean suppliers located outside the EPZ. The workforce in those enterprises soared from 4,518 in 1976 to 16,686 in 1988. It was estimated that about 50 per cent of those workers were hired primarily to fulfil contracts which those firms had concluded with enterprises in the zone (Lee, 1990, page 85).

Table 12. Employment in firms with foreign participation in the Republic of Korea, selected years (thousands of workers)

	1974	1978	1986
Employment in foreign firms:			
All sectors	159	315	416
Manufacturing	153	288	363
Total Korean employment:			
All sectors	11 586	13 490	15 505
Manufacturing	2 012	3 016	3 826
Percentage share of foreign firms:			
All sectors	1.4	2.3	2.3
Manufacturing	7.6	9.5	9.5

Sources: Economic Planning Board, Republic of Korea for 1986 data; UNCTC for 1992 data.

Note: The data on employees in foreign firms in the Republic of Korea for 1974 and 1976 refer only to Korean employees (excluding expatriates).

5. Concluding remarks

Although it started from a very low base, foreign direct investment from the Republic of Korea has grown considerably in recent years. In the second half of the 1980s, and particularly in the early 1990s, FDI in manufacturing increased sharply in North America and south-east Asia. The drive to promote outward investment was a response to changing economic conditions which manifested themselves in the form of rising wages, labour shortages, increased trade surpluses and currency appreciation, as well as the loss of preferential status for Korean exports to industrialized countries.

These developments had an impact on the international competitiveness of Korean producers in export-oriented labour-intensive industries such as textiles and clothing, footwear, toys and consumer electronics, and created a strong incentive to relocate certain operations to low-wage developing countries. Another main outlet for Korean FDI was the industrialized countries. Investors were motivated mainly by the need to maintain market shares in the face of growing protectionist policies that were adversely affecting trade in consumer products such as refrigerators, television sets and video cassette recorders.

The factors motivating overseas investment by Korean firms in the 1980s did not seem to conform to the conventional explanations, according to which foreign investment was undertaken to maximize firm-specific competitive advantages. In recent years, there have been other forms of investment primarily by the largest Korean conglomerates, which are seeking to acquire advanced technologies and to rationalize their operations by creating global networks for production and marketing.

The need to expand market shares in those industries in which Korean producers are well-established leading exporters, is likely to remain a key "push factor" for the expansion of FDI. Korean investors also seem to be very keen on having a commercial presence in those countries where, in spite of relative economic and political instability, there are vast potential markets (e.g. China and the Commonwealth of Independent States).

The outlook for Korean FDI should also be considered within the framework of the general process of industrial restructuring which is taking place in the country. Domestic production in labour-intensive low-tech activities is declining because of rising labour costs and the tightening of the market for

unskilled labour. Factory automation is being introduced and investment is being channelled to capital-intensive industries that require the use of complex technologies. Investment in research and development (R&D) is now a key component of the strategies of Korean firms seeking to maintain their international competitiveness by moving into higher value-added production. The Government is also actively supporting investment in R&D in high-tech industries. The allocation of resources for overseas investment and domestic R&D in manufacturing will become a critical issue in the coming years.

The impact of Korean FDI on employment in host countries cannot be accurately assessed due to the dearth of comprehensive data. Overall, the number of those employed in the foreign affiliates of Korean firms may not be very large. Considerable job creation, however, has most likely occurred in labour-intensive operations in the developing economies of Asia. Since most Korean affiliates have been established fairly recently, there are not many backward and forward linkages with local firms in developing and industrialized countries. Indirect employment cannot be expected to be significant, although it may increase with time and with the growth of local procurement arrangements. Finally, the nature of Korean FDI is such that the qualitative impact on host countries in the areas of training and the transfer of skills and know-how has been relatively limited.

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