

The Impact of China's Increasing Influence
in the ROK on US-South Korea Relations

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Government and Politics of the Korean Peninsula
Johns Hopkins SAIS
Spring 2004

Introduction

The United States (US) and the Republic of Korea (South Korea or the ROK) have enjoyed a strong relationship over the past fifty years. The ROK has benefited from the presence of US military forces and trade links with the US, while the United States' support of South Korea helped a democratic regime grow where Communism threatened. However, the world changes and the ideological battlegrounds of today have little to do with Communism. The so-called 386 generation, with no experience of the Korean War, has become an increasingly potent force in ROK politics at a time when the US military is questioning its presence in the Korean peninsula due to manpower shortages from its newfound roles of state-securing and nation building.

These changes come against a backdrop where the People's Republic of China (China or the PRC) is surging economically across the region and globe. The PRC's economic growth has led to increasing affinity between it and the ROK. In addition, China has shown a nascent willingness to translate its economic power into political action, thus distinguishing itself from its neighbor to the east. These geopolitical and economic changes call into question the future of the US-ROK relationship. We will examine briefly in this paper the increased economic, political, and cultural linkages between the ROK and PRC, and then attempt to understand the implications for the US-ROK relationship.

China and South Korea

ECONOMICS

The growing relationship between South Korea and China is driven by economics. As the US focuses on Afghanistan and Iraq, China concentrates on job growth to avoid social unrest. It faces large numbers of unemployed from reformed state owned enterprises, soon to be joined

by millions more unemployed from restructuring and reforms agreed to in China's WTO accession that affect its agricultural sector. Korea is currently embroiled in politics after President Roh's impeachment, however, its overall focus is increasingly on how to survive China's economic resurgence.

China's WTO entry presents a major threat to the ROK's economic well being. The reduction in tariffs on South Korean goods relative to the reduction on goods from other Asian countries as a result of Chinese WTO entry is smaller, such that e.g., Korea's electronics sector will likely not see much of an upsurge in exports to China.¹ In addition, the size of the PRC's economy means that it is pursuing both import substitution growth (ISG) and export led growth (ELG), rather than pursuing ISG first then later shifting to ELG. The impacts for Korea are multiple: in the short term, it will be able to sell China more primary goods such as steel and petrochemicals, supply more value added manufactures such as electronics, automobiles and shipbuilding, and benefit from increased demand for services. Low value added sectors such as textiles are being somewhat protected now by increasing apparel production in China, but when the PRC's textile restrictions are removed in 2008, Korea's textile sector will likely be decimated. In addition, as China builds up its internal production capabilities, it is likely that it will no longer need most of its current imports of South Korean steel and petrochemicals within five to ten years. Moreover, China is attempting to move up the value chain in manufacturing to produce higher technology products such as computers, semiconductors, and telecommunications equipment, areas which will compete directly with Korea. Finally, it is investing heavily in rationalizing its automobile production capabilities and attempting to improve its capabilities in the services sectors also posing potential problems for the ROK.

The economic peril posed by these changes means that the ROK must invest in research and development to keep its advantage in areas such as technology and automobiles ahead and develop additional service and extremely high technology industries. The South Korean government also needs to help push entrepreneurship as a way to generate new jobs. Moreover, Korean companies will likely find pressure to move manufacturing plants in less sophisticated industries offshore to China or to other places where labor costs are lower such as Vietnam. Overall, China's WTO entry is expected to benefit the ROK until 2008, at which point the PRC will start to profit at South Korea's expense.²

This threat comes at a time when South Korea's economy is shifting from export led growth to post industrial conditional growth. The Asian Financial Crisis spelled the end of complete reliance on export markets for most of East and Southeast Asia. Governments were no longer willing to rely fully on portfolio and foreign direct investment (FDI) from abroad to help develop domestic production capability to sell to those same offshore markets. The crisis and its aftermath showed that producing for export needed to be matched by a robust domestic market. Moreover, because so many of the ROK's neighbors pursued similar growth patterns with similar export products, sustained economic expansion now requires increases in productivity rather than just increases in production. This economic maturity puts South Korean companies more directly in competition with US and other global companies in areas such as mobile phones and shipping. This combination of threat from below from China and threat from above from the US and other OECD economies has resulted in Korea and Taiwan being labeled "sandwich" economies.

As shown on the following page, the PRC has replaced the US as the most important country for South Korea's trade. China became the ROK's largest trading partner in 2003 with

exports of \$35.1B from the ROK to the PRC helping to contribute to a positive trade balance of \$13.2B.³ By comparison, exports to the US were \$34.2B and the trade balance was \$9.4B.⁴ The trend is accelerating as China is expected to account for almost 30% more trade volume in 2004 than the US.⁵ This export growth has also allowed China to surpass the EU in importance for South Korea's economy. ROK export growth to the PRC is concentrated in high technology,

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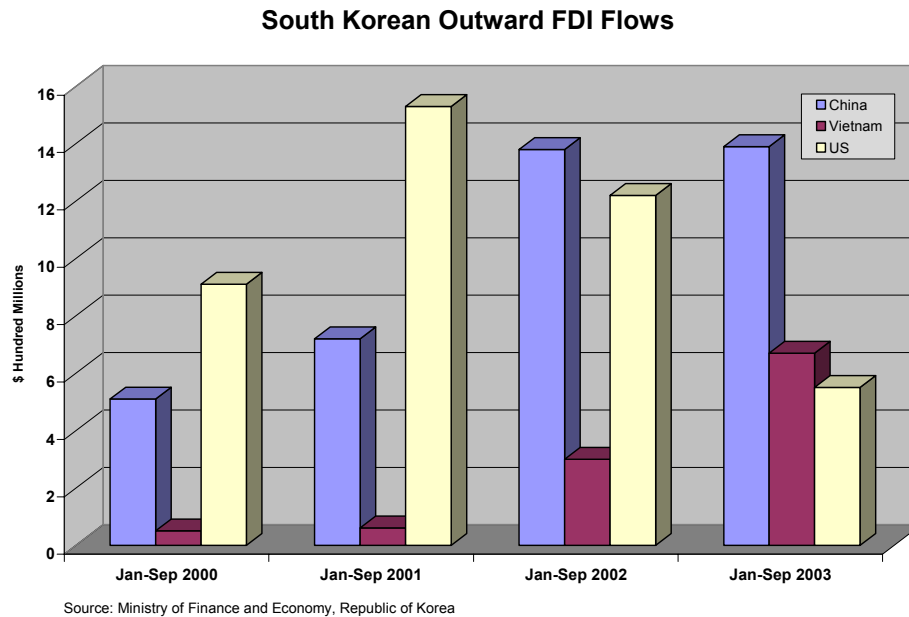
Yearly	Japan		USA		PRC	
	Value	Change (%)	Value	Change (%)	Value	Change (%)
1994	13,522,860	16.9	20,552,796	13.3	6,202,986	20.4
1995	17,048,871	26.1	24,131,474	17.4	9,143,588	47.4
1996	15,766,827	-7.5	21,670,465	-10.2	11,377,068	24.4
1997	14,771,155	-6.3	21,625,432	-0.2	13,572,463	19.3
1998	12,237,587	-17.2	22,805,106	5.5	11,943,990	-12.0
1999	15,862,448	29.6	29,474,653	29.2	13,684,599	14.6
2000	20,466,016	29.0	37,610,630	27.6	18,454,540	34.9
2001	16,505,766	-19.4	31,210,795	-17.0	18,190,190	-1.4
2002	15,143,183	-8.3	32,780,188	5.0	23,753,586	30.6
2003	17,276,137	14.1	34,219,402	4.4	35,109,715	47.8
2004(01 ~ 03)	5,222,870	30.8	9,280,150	19.8	11,045,819	50.7

Source: Korea International Trade Association

construction and automobiles. As China builds up its manufacturing capabilities, its trading relationship with the ROK will likely change; South Korea's \$13B trade surplus with the PRC is expected to turn into a deficit by 2011.⁶

FDI from the PRC into South Korea and vice versa is also increasing at a strong pace, creating additional ties between the two countries. South Korea's strong FDI outflows to the PRC in 2003 allowed it to move past the US into second place.⁷ It now lags only Japan in the PRC FDI inflow tables. Investment is primarily in manufacturing and assembly plants, such that Korean companies as diverse as computer manufacturer LG and zipper maker JS International are already producing significant output from facilities in the PRC. Many of the Korean owned factories in China assemble intermediate products produced in Korea into final products, thus

further reinforcing the trade relationship between the two countries. The decrease in importance of the South Korea-US relationship is magnified by the United States' fall behind Vietnam as a target for ROK FDI, as shown below.



South Korea's increased FDI into the PRC is being paralleled by an upsurge in Chinese FDI into the ROK. South Korea was one of the top five targets for PRC outward FDI in 2002 after not being in the top ten in 2000. Although still dwarfed by US FDI into South Korea, China's increased investment has been going into sectors such as high technology manufacturing and services. This has led to concerns that China is buying its way up the knowledge curve and closing the technology gap with South Korea. Recent studies project that China may overtake the ROK in technology capability as early as 2006.⁸

Additional problems in the bilateral relationship are beginning to appear in the jobs sector. Evidence is mounting that the increased production in China by ROK companies is coming at the expense of South Korean jobs. ROK-owned enterprises have created 1,000,000 new jobs in China since 1992, while 770,000 manufacturing jobs have been lost in South Korea during the

same period.⁹ Another source of tension between Seoul and Beijing is the status of the approximately 200,000 illegal ethnic Chinese who are working in the ROK.¹⁰ This is a particularly thorny issue as the South Korean government attempts to overhaul its work permit system for foreign laborers. Finally, China's massive growth is driving up prices of most basic commodities, raising the cost of inputs for many of South Korea's industries. For example, China's consumption of iron ore, which is a key ingredient in the production of steel, grew by 18% in 2003. The PRC's needs also caused price spikes in oil, lumber, and coal, negatively impacting the ROK as well as other regional and global economies.¹¹

Overall, China's major economic growth is causing increased linkages with the ROK in the short term and presents a longer term threat to the viability of the South Korean economy. Whether positive or no, China has become South Korea's number one policy issue and will dominate its economic thinking for the near and medium term future.

POLITICS AND CULTURE

The ROK's and PRC's growing economic linkages are starting to be paralleled on the political front. Japan has long been politically impotent, preferring to focus on domestic issues and competing globally in business rather than translating its regional financial power into the political sphere. China appears to be somewhat reluctant to take the political bull by the horns lest it cause regional countries and the US consternation over potential regional domination. Nevertheless, it is showing a willingness to become a player at the regional political table to a strong degree, taking the leading role in the most important issue in East Asia, North Korea.

China arguably has taken the lead in resolving the North Korean nuclear crisis because it has more to lose than the US if the situation spirals out of control. The US is focused on Southwest Asia while the PRC and South Korea are concerned about the nuclear threat posed by

North Korea (the DPRK) and the economic consequences of a potential collapse in the regime of Kim Jong Il. The Bush Administration's stance of complete verifiable irreversible dismantlement (CVID) of the North Korean nuclear arsenal prior to any direct bilateral talks appears to have made Pyongyang adopt a more aggressive stance. China and South Korea share a common worry about the economic refugees that could pour into their countries if there is military engagement between the DPRK and the US. China is already having a hard time with labor dislocations, as discussed above, from North Korea and would not like to see additional refugees coming across its borders.

China's efforts to move the six party talks ahead on a logical, productive footing are also driven by other regional stability concerns. The preferred method for rapprochement between the North and South is for North Korean economic reforms to continue, thereby attracting much needed FDI and helping the move toward expansion. This would set the stage for reintegration with the ROK. If the DPRK regime collapses due to political and economic pressure, the PRC could face a hastily unified Korea that is economically and politically volatile, and/or one where there is a US military presence that would now extend up to the Chinese border.

Overall, China wants to maintain the status quo on the Korean peninsula for as long as possible, so it is willing to make an effort to attempt to diffuse some of the tension over the DPRK nuclear issue. Although the last round of six party talks in late February 2004 in Beijing were not very productive, China will likely continue to take the lead in resolving the DPRK nuclear situation. North Korea is an important issue for the Bush Administration, but it is obvious to everyone, including the politicians and people in the ROK, that it is secondary to the war on terrorism and the Iraq War. Thus, South Korea may know that the US will be the

ultimate guarantor of a solution to the nuclear issue, but it rightly views China as the driver of finding a diplomatic solution.

In addition to China's role in the North Korean nuclear crisis, there have been other improvements in relations between Beijing and Seoul. There have been a number of meetings between senior military officers from the ROK and the PRC in the last years, including a November 2003 meeting between South Korean Joint Chief of Staff Kim Jong-hwan and China's top military man, Cao Gangchuan. At this last meeting Kim and Cao highlighted the importance of China in finding a solution to the North Korean issue and also agreed to pursue a "full cooperative partnership"¹² that would include exchanges between the two country's militaries and efforts by China to induce the DPRK to resume inter-Korean military contacts. This cooperation is paralleled in other areas, including a visit by the ROK's Foreign Minister Ban to meet with Chinese Foreign Minister Li in Beijing in March 2004 to discuss strategy for moving toward a solution to the North Korean issue.¹³

This increased political involvement is paralleled by growing cultural affinities between the PRC and the ROK. President Roh Moo-hyun highlighted the political and soft linkages in a speech last fall at Chinghua University in Beijing. He pointed out that China is the largest tourist destination for South Koreans, while 40% of the foreign students studying in the PRC are from the ROK.¹⁴ This latter figure is evidence of a growing link between the youth in South Korea and China. For example, in the ROK there is growing study of Chinese language, while in China, young people increasingly are interested in South Korean music and films.

The US and South Korea

South Korea and the US remain strong military allies, however the economic and foreign policy priorities facing the two countries have never been more divergent. Tension over the

differences in approach toward the resolution of North Korea and over economic priorities means that support for the US-ROK relationship has ebbed. The weakness of conservatives in the recent parliamentary elections and the rise of Generation XP (born in the 70s and 80s, thus Generation X, and aspiring to professional success, thus P) is only reinforcing anti-Americanism, as shown at right. For example, after President Roh's May

KOREAN VIEWS OF THE US, GROUPED BY AGE

Age	Like		Dislike		Neutral	
	2001	2003	2001	2003	2001	2003
20s	25.8	7.2	21.3	47.3	52.9	45.1
30s	22.6	11.6	22.5	33.5	54.9	33.5
40s	29.3	24.5	18.2	26.7	52.5	26.7
50s	42.1	45.0	15.5	13.4	42.4	13.4
Avg.	30.2	23.0	19.4	29.5	50.4	46.0

Source: "Public Opinion in Korea," *Dong-A-Asahi* survey (face-to-face interviews with 2,000 people; margin of error 2.19%), 19-30 November 2001, p.3, as shown in Youngshik, 2003

2003 summit meeting with President Bush, he was publicly discomfited upon his return to the ROK when student protests against the visit to the US delayed his entry into a commemoration ceremony for the Kwangju uprising.¹⁵ Other events such as the December 2002 not guilty verdict for two US soldiers who ran over two junior high school students have fed calls for a more equal alliance.

The political strains and rise of China are threatening the US-ROK relationship. Although Anti-Americanism in Korea is neither violent nor virulent, many South Koreans view the US as a political ally with diverging economic goals. This is driven by the regionalism that is at the core of the ROK's major issues versus the globalism that the US is pursuing. Whether it is greater economic integration or finding a solution for North Korea, the PRC and the ROK share a commitment to do so on a regional basis. The US meanwhile, is focused on global economic issues and development and finds a difficult time fitting North Korea neatly into its global war on terrorism.

Prescriptions for the Future

The question then becomes what is the US to do? Korea's economic fortunes increasingly are reliant upon the PRC and this trend will only continue. One possible solution could that could allow the trilateral relationship to function well, would be to have the US as the technology base, the ROK as the value added manufacturer and China as the low cost assembler.¹⁶ However this requires that South Korea maintain its manufacturing edge over China, which is far from a given. More troublingly, it implies that US technology licensed to Korean companies could migrate over to China through FDI flows, which is problematic for the United States as it also attempts to maintain its technological edge against China.

The best economic policies for the United States are to support the economic reforms that are continuing in the ROK and to consider setting up a new free trade agreement (FTA) with South Korea. As discussed above, the growing economic relationship between China and South Korea is a major danger to the medium and long term viability of the ROK economy. South Korea is facing the threats to its export markets and value added manufacturing at a time when it still has inflexible labor markets and government ownership in the private sector remains high. Assuming the Constitutional Court reinstates him later this week, the US should support President Roh in efforts to reform the chaebol and improve the functioning of a free market economy in South Korea.

A second method to help South Korea maintain its technological and manufacturing edges over China is to support a bilateral free trade agreement between the US and the ROK. This would help offset negative impacts of NAFTA for South Korea and provide a competitive edge for our allies in their fight to maintain their trade importance. Moreover, South Korea is increasingly looking to FTAs to counter its growing China problem, and this initiative will likely

include a regional FTA within the next several years. Whether or not this regional FTA includes China is uncertain, but what is definite is that it will compel South Korea to focus its economic fortunes even more on the region and not on the US. Thus, an FTA between the US and the ROK would have the added benefit of helping to offset growing economic regionalism.

The political question is more difficult. The bifurcation of US and South Korean economic and regional political strategies threatens the ability of the US to achieve its goals as it cannot have a strong political alliance with weakening economic ties. The US is making a good step by moving its military headquarters south from Seoul. Although this sent red flags up for some South Koreans, the less obvious day to day presence will likely help in relations with Generation XP. Overall, the sustained US military presence in South Korea is a good counterbalance to the rising political influence of China. The most important thing the US can do is to maintain this presence at a strong level. Force commitments elsewhere will likely require scaling down the number of US troops in the ROK, however the US must maintain a significant presence otherwise it risks losing the political support of a still important ally.

Thus, the shifting influence of the US in South Korea is to some degree inevitable given the PRC's growth. The US cannot stop the relationship between South Korea and PRC from deepening just as its relationship with the PRC is growing stronger. However, the closer economic relationship between South Korea and the PRC will be balanced by increasing competition between the two countries as China attempts to move up the value chain. It is important for the US to support the ROK in continuing to modernize its manufacturing and services sector, as well as reforming labor markets and government ownership in the private sector. On the political side, it must maintain a strong military presence in the Korean peninsula, while taking into account the growing demographic dichotomy in attitudes toward the United

States and the evolution of Korean politics toward a liberal dominant system. Overall, the PRC poses major threats to the future of the US-ROK relationship, but with forward thinking the US should be able to ensure that one of its most important allies during the last five decades remains one for decades more to come.

Endnotes

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