SOUTH KOREA'S NEW SOUTHERN POLICY: AN ECONOMIC ASSESSMENT

CHIANG Min-Hua

EAI Background Brief No. 1593

Date of Publication: 18 June 2021

Executive Summary

1. South Korea announced an upgraded version of its New Southern Policy (NSP) in November 2020 to strengthen ties with the Association of Southeast Asian Nations and India (hereafter NSP countries) to meet emerging challenges from the COVID-19 crisis, rising nationalism and protectionism, digital transformation and non-traditional security.

2. South Korea's trade with NSP countries has expanded gradually after the launch of the NSP in 2017; however, due to the US-China trade war and the ongoing COVID-19 pandemic, bilateral trade between South Korea and NSP countries had deteriorated in 2019 and 2020.

3. South Korea's trade with Vietnam has remained resilient thanks to the strong global demand for information and communications technology goods. In comparison, South Korea's trade with other NSP countries has been weakening over the past few years.

4. South Korea's outward foreign direct investment (OFDI) in NSP countries increased from US$5.8 billion in 2017 to US$10 billion in 2019 but slowed down to US$7.3 billion in 2020. The OFDI rise in recent years has been driven by services, which accounted for 73% of Korea's OFDI in the region in 2020.

5. Singapore is attractive to South Korean firms in the financial industry. Vietnam's active involvement in various free trade agreements (FTAs) makes it appealing to South Korean investment in trade distribution and retailing business.

6. After relocating labour-intensive manufacturing production from China to other developing countries, South Korean firms turned to focus on investing in high-end production in China. As such, China remains an important manufacturing site, accounting for 27%-29% of South Korea's total OFDI in manufacturing during the 2018-2020 period, higher than NSP countries' 22%-24%.

7. South Korean firms responded to the US-China trade war by increasing their investment in manufacturing production in the United States, from US$1 billion in 2017 to US$2.6 billion in 2020. In comparison, South Korea's OFDI in NSP countries' manufacturing industry remain unchanged during the same period (US$3.1 billion annually).

8. The relatively low income of NSP countries on average suggests their limited potential contribution to South Korea's inbound tourism revenue. Conversely, there are a growing number of South Korean visitors to the region, driven by closer business ties between South Korea and Vietnam in particular.

9. South Korea may encounter difficulties shifting its economic reliance on big powers to NSP countries. The growth of South Korea's economic relations with NSP countries has been driven by the development of regional division of labour, with China, Japan and the United States playing important roles.

10. South Korea can enhance the strategic importance of the NSP by linking it with other regional initiatives and by inviting more countries to join the NSP. It may also seek to join the Comprehensive and Progressive Agreement for Trans-Pacific Partnership to increase its importance in the evolving regional political economy.

SOUTH KOREA'S NEW SOUTHERN POLICY: AN ECONOMIC ASSESSMENT

CHIANG Min-Hua*

Diplomatic Response to Economic Challenges

1.1 In November 2017, South Korean President Moon Jae-in announced the launch of the New Southern Policy (NSP) to uplift relationship with the Association of Southeast Asian Nations (ASEAN) and India (hereafter NSP countries) to the level of relations with four major powers (the United States, Japan, China and Russia).

1.2 The NSP was a diplomatic response[1] to the threat faced by the Republic of Korea's (ROK) economy as a result of political clashes with China. In 2017, South Korean retailor giant Lotte suffered severely from China's sanction when it sold land to the ROK government as a site for the deployment of the Terminal High Altitude Area Defence's (THAAD).[2]

1.3 The sanction led to a sharp drop in Chinese tourists to the ROK and to a dive in South Korea's tourism revenue to US$13 billion in 2017, from US$17 billion in the

* Chiang Min-Hua is research fellow at the East Asian Institute, National University of Singapore.

[1] The NSP is an integral part of South Korea's grand diplomatic strategy. Together with "Northeast Asia Peace and Cooperation Platform" and "New Northern Policy", the three policies formed "Northeast Asia Plus Community for Responsibility-sharing" which purports to promote peace and prosperity in the region. Lee Jaehyon, "Korea's new southern policy: motivations of peace cooperation and implications for the Korean Peninsula", The ASAN Institute for Policy Studies, Issue Brief, 21 June 2019, <http://en.asaninst.org/ contents/koreas-new-southern-policy-motivations-of-peace-cooperation-and-implications-for-the-korean-peninsula/> (accessed 12 February 2020); and Sohn JiAe, "President moon unveils New Southern Policy for ASEAN", Korea. Net, 10 November 2017, <http://www.korea.net/NewsFocus/policies/view?articleId=151092> (accessed 12 February 2020).

[2] Lotte Mart's 2017 financial report showed that its loss in China reached 268 billion won (about US$0.2 billion). "South Korea's Lotte seeks to exit China after investing $9.6 billion, as THAAD fallout ensues", *The Straits Times*, 13 March 2019, <https://www.straitstimes.com/asia/east-asia/south-koreas-lotte-seeks-to-exit-china-after-investing-96-billion> (accessed 12 March 2021).

previous year. The overall travel service deficit widened to US$1.8 billion in 2017, from US$1billion in 2016.[3]

1.4 The South Korean economy has been hit further by the US-China trade war since 2018. South Korea's economic growth in 2019 was stalled partly due to the trade conflict with Japan following Japan's restrictions on high-tech exports to ROK.

1.5 As the COVID-19 pandemic adds uncertainties to the global political economy, South Korea regarded cooperation with NSP countries as imperative. An advanced version of NSP (NSP Plus) was announced in November 2020, detailing measures for deepening cooperation between South Korea and NSP countries.[4]

1.6 Before the launch of the NSP, South Korea had already established close economic ties with NSP countries which are South Korea's second largest trade partners, after China. South Korea's outward foreign direct investment (OFDI) in NSP countries grew from US$4.6 billion in 2010 to US$10 billion in 2019, far ahead of its OFDI in China (US$5.8 billion).[5]

1.7 Institutionalised economic ties have also progressed. A basic ASEAN-ROK Free Trade Agreement (AKFTA) was reached in May 2006. The AKFTA in the trade of goods and services went into force in 2007 and 2009 respectively. In 2010, ROK-India Comprehensive Economic Partnership Agreement went into effect.

1.8 Although bilateral economic ties between South Korea and NSP countries have gradually deepened, they still could not be compared with Korea's economic relations with China and the United States. ROK's total trade with China and its

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[3] Data source: CEIC.

[4] The "NSP Plus" comprises seven areas for cooperation, including comprehensive health and medical cooperation to tackle the COVID-19 pandemic; sharing Korea's education and human resource development models; promotion of cultural exchanges by utilising *hallyu* content; developing mutually beneficial trade relations and investment; cooperation in the development of farming and urban infrastructure; collaboration in future industries; and cooperation in non-conventional security. Do Je-hae, "Moon announces NSP Plus strategy", *The Korea Times*, 12 November 2020, <https://www.koreatimes.co.kr/www/nation/2020/11/356_299218.html> (accessed 8 March 2021). There are four principles in the NSP Plus, including people-centralism, reciprocity, deepening cooperation and openness. New Southern Policy Plus, Presidential Committee, Republic of Korea.

[5] Data source: CEIC.

OFDI in America have increased more rapidly than its trade with and investment in NSP countries over the past few years.

1.9 The NSP is one of the "hedging" options for South Korean firms amid the growing US-China rivalry. Being important world manufacturers and investors, South Korean firms adopted a worldwide business strategy to counterbalance the mounting geopolitical risks in the region.

1.10 The effectiveness of the NSP so far has been curtailed by the intensified regional economic integration. The well-established regional production network in East Asia would prevent ROK from effectively mitigating the risks of an over-reliance on China through the NSP as NSP countries (notably ASEAN) have increasingly close economic ties with China.

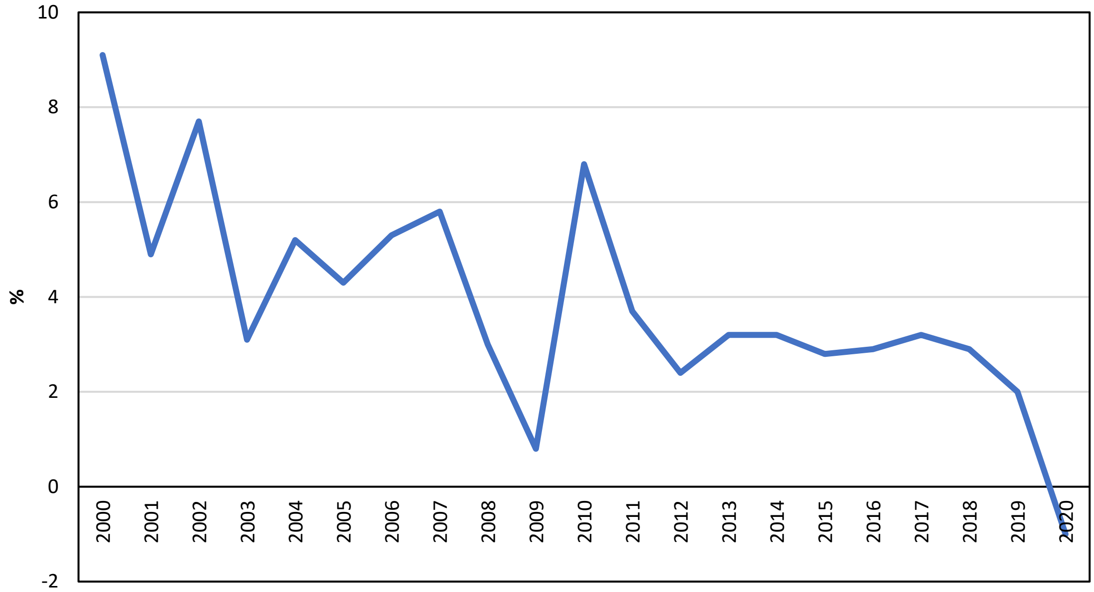
Explaining South Korea's Economic Vulnerability

2.1 South Korea's economic miracle could be attributed to the regional division of labour, constructed since the cold war era: importing high-tech industrial goods from Japan and exporting final consumption goods to the United States after manufacturing in South Korea. China's participation in this regional production network did not change the basic economic structure but only enlarged the region's production scale.

2.2 China's economic opening up, rising production cost in South Korea and establishment of ROK-China diplomatic relations in 1992 gradually shifted South Korea's economic growth model from exporting final consumption goods to the United States to exporting intermediate goods to China for the final assembly.

2.3 Nonetheless, this growth model based on exporting to China has reached its limit a decade ago. After the post-crisis rebound in 2010, South Korea's economic growth rate has remained stagnant at an annual growth rate of 2%-3% during the 2012-2019 period. The economy had slid even more in 2020 due to the COVID-19 pandemic (Figure 1).

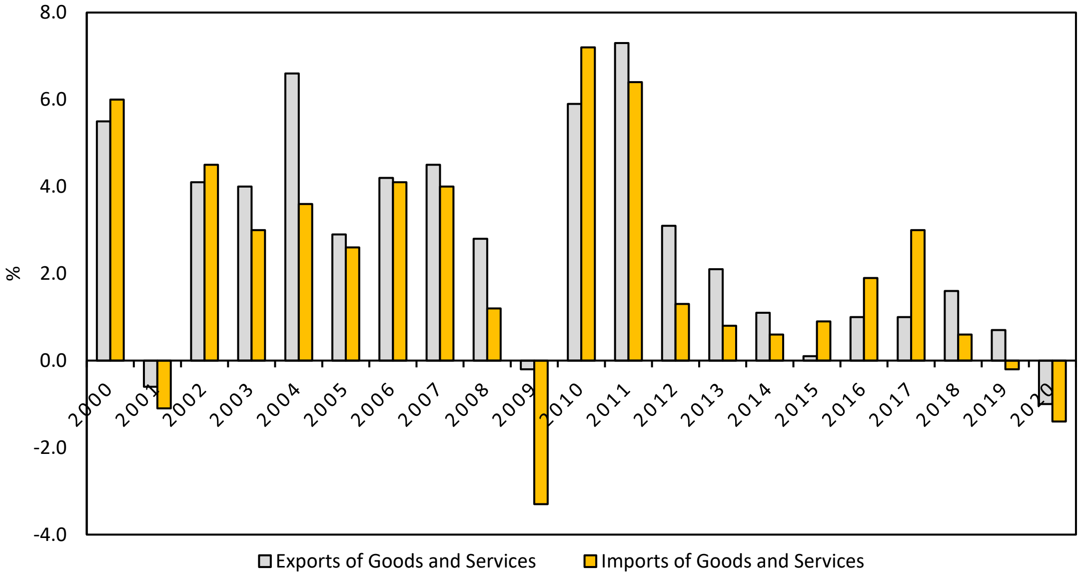
FIGURE 1 SOUTH KOREA'S ANNUAL ECONOMIC GROWTH RATE 2000-2020



Source: CEIC.

2.4 The contribution to GDP (gross domestic product) growth by expenditure showed that the economic deceleration is mainly due to the slowing exports. After the peak in 2011, the contribution of exports to South Korea's GDP growth has clearly lessened, compared to pre-global financial crisis level (Figure 2).

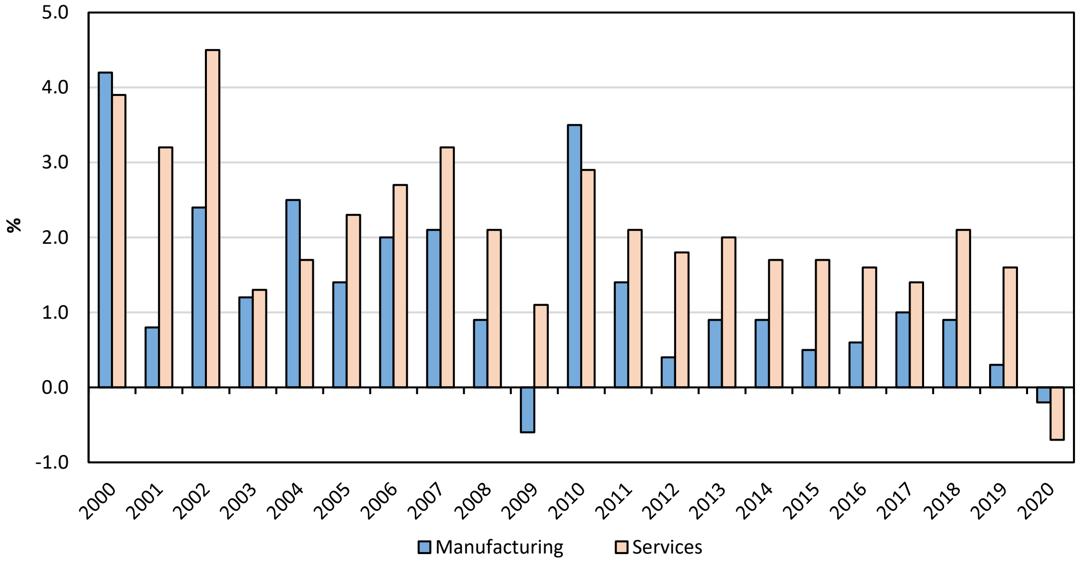
FIGURE 2 CONTRIBUTION TO SOUTH KOREA'S GDP GROWTH BY SELECTED EXPENDITURE ITEMS 2000-2020



Source: CEIC.

2.5 The GDP growth by sector showed that despite the steady growth in services, the economy remained sluggish (Figure 3). Although services accounted for a larger share in the economy, it was the booming manufacturing industry that has provided the impetus for the service sector's development over the last few decades.

FIGURE 3 CONTRIBUTION TO SOUTH KOREA'S GDP GROWTH BY SELECTED SECTORS 2000-2020



Source: CEIC.

2.6 A fiscal expansion policy has been adopted to stimulate economic growth when exports were waning. As such, South Korea's government debt as a percentage of GDP had been growing from 29% in 2010 to 48% in 2020.[6] Even with the extra government spending, the economy was still unable to regain its momentum of the early 2000s.

2.7 Although China remained the largest export destination for South Korea, China's increasing manufacturing strength has reduced its dependence on intermediate goods from Korea.

2.8 Over the last decade, China has been quickly catching up in the production of several high technology goods, such as organic light-emitting diode (OLED),

6 Data source: IMF.

semiconductor chips and dynamic random-access memory (DRAM). The high technology goods are South Korea's main export items.

2.9 China's policy to increase the "made in China" content in high technology goods by 2025 also indicates the potential decreasing imports of intermediate goods from South Korea. With China's strong determination to upgrade industries, South Korea's comparative advantage in producing and exporting goods with high capital and technology intensity is challenged.

2.10 Another risk for ROK's economy is its dependence on Japan for key components. Japan's stricter control of its exports of key components to South Korea since 2019 has posed great challenges to South Korea's semiconductor industry.[7]

2.11 South Korea's vulnerability is hence in its over-reliance on a few big countries for its economic survival. This economic dependence has been key to South Korea's high economic growth rates for decades. That dependence has become a threat to ROK's economy when political relations with and between big powers have soured.

The NSP in South Korea's Economic Rationale

3.1 NSP countries' economic size is comparable to that of big countries in the world. ASEAN and India's combined GDP is the world's third largest, after those of the United States and China.

3.2 ASEAN and India's two billion population surpasses China's 1.4 billion and far outstrips America's 328 million. The abundant cheap labour in NSP countries is advantageous for South Korean firms to pursue labour-intensive manufacturing production at the least cost.

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7 Since 2019, more than 1,100 products were exposed to enhanced Japanese regulatory scrutiny after Japan removed South Korea from its "white list" of countries that are accorded preferential treatment for export licensing. Stephen Ezell, "Understanding the South Korea-Japan trade dispute and its impacts on US foreign policy", Information technology and innovation foundation, 16 January 2020, <https://itif.org/publications/2020/01/16/understanding-south-korea-japan-trade-dispute-and-its-impacts-us-foreign> (accessed 17 March 2021).

3.3 The population of NSP countries is relatively young. The average medium age in NSP countries is 30 years old, younger than China's 38, the United States' 39 and Japan's 49.[8] Apart from manufacturing production, the large and young population signifies a huge consumption market in the region.

3.4 The region's huge consumption potential has already attracted Hyundai, one of South Korea's largest carmakers, to invest in car making factories to grasp the booming local market (in particular Indonesia, Thailand, Malaysia, Vietnam and Singapore are Hyundai's main market targets). [9]

3.5 Before the launch of the NSP, ROK had gradually developed close economic relations with NSP countries through its OFDI. The wage hike, currency appreciation and growing protectionism against South Korean products in the late 1980s encouraged South Korean firms to relocate labour-intensive manufacturing production to developing countries.[10]

3.6 China replaced ASEAN to become a more favoured OFDI destination in the early 2000s. When production cost in China began to rise more than a decade ago, South Korean manufacturers have gradually shifted their manufacturing production from China to developing NSP countries where the production cost remains at a relatively low level.

3.7 The expansion of South Korean OFDI in NSP countries in the past few years is mainly driven by the greater investment in Vietnam and Singapore. Vietnam accounted for most of South Korea's OFDI during the 2010-2019 period. In 2020, nearly 40% of South Korea's OFDI went to Singapore (Figure 2).

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8 Data source: CIA World factbook, <https://www.cia.gov/the-world-factbook/field/median-age/country-comparison> (accessed 6 May 2021).

9 Hyunjoo Jin, "Hyundai motor to invest $1.55 billion in first Indonesia car plant", Reuters, 26 November 2019, <https://www.koreatechtoday.com/hyundai-motor-to-invest-in-indonesia-to-boost-presence-in-asean/> (accessed 18 May 2021).

10 Chung H Lee, "Korea's direct foreign investment in Southeast Asia", *ASEAN Economic Bulletin*, Vol. 10, No. 3, 1994, pp. 280-296. Most of the South Korean OFDI in the region at the initial stage was by small and medium enterprises with an aim to export final consumption goods to the United States and Europe. Large South Korean companies have started to invest in ASEAN after the late 1980s.

3.8 Vietnam's foreign investment promotion policy, political stability and relatively low wages are a draw for greater South Korean investment in the country. Vietnam's active participation in various bilateral and multilateral free trade agreements (FTAs) has also transformed the country into a regional trade platform.

3.9 On the other hand, South Korean firms are attracted by Singapore's highly developed financial sectors and advanced technology. Overall, the region presents a fertile ground for the convergence of technological and financial expertise and abundant cheap labour force.

3.10 Nonetheless, South Korea's quick OFDI development in Vietnam and Singapore has squeezed the importance of other NSP countries in its OFDI. In 2010, over 70% of South Korean OFDI in the region went to NSP countries (except Vietnam and Singapore), but in 2020, this percentage shrank to only 34% (Figure 4).

3.11 The economic complementarity is the main driving force behind the development of bilateral trade. With exports substantially more than imports, South Korea has consistently run a large trade surplus with NSP countries, swelling from US$10.8 billion in 2009 to US$41.1 billion in 2020 (Figure 5).[11]

3.12 Induced by its OFDI in manufacturing, ROK's trade with NSP countries is overwhelmingly concentrated in Vietnam. In 2020, Vietnam accounted for 53% of South Korea's exports to and 40% of its imports from all NSP countries.[12]

3.13 The launch of the NSP reinforced the recognition of the fact that the region is a focal point for great powers' advancement of economic and strategic interests. Not only would South Korea benefit from economic diversification through the NSP, but also

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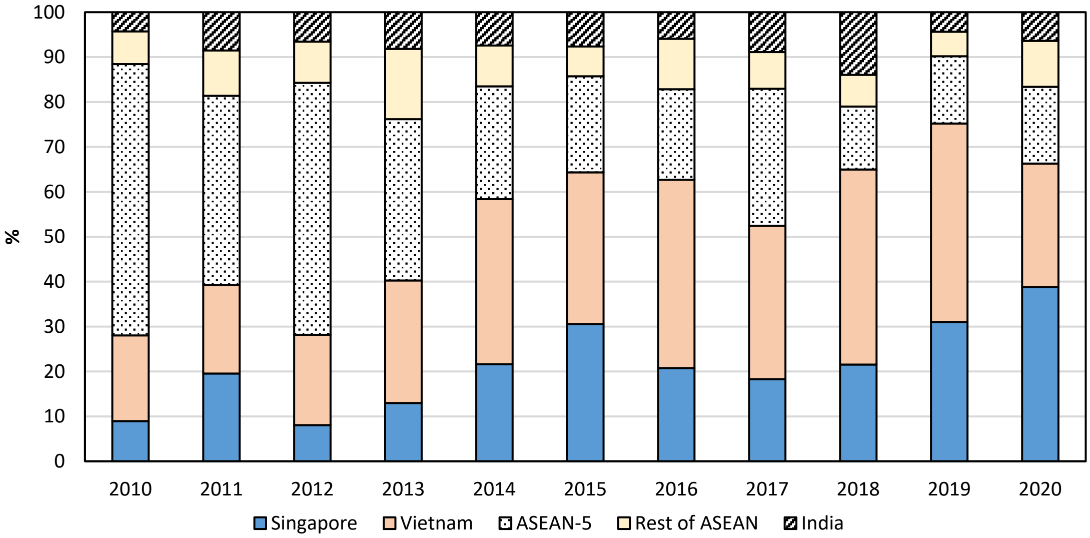
[11] South Korea supplied intermediate goods with high technology and capital intensity to South Korean firms in these countries in exchange for manufactured goods and raw materials.
Data source: CEIC.

[12] Data source: CEIC.

NSP countries could benefit from having an alternative source of economic power presence in the region.[13]

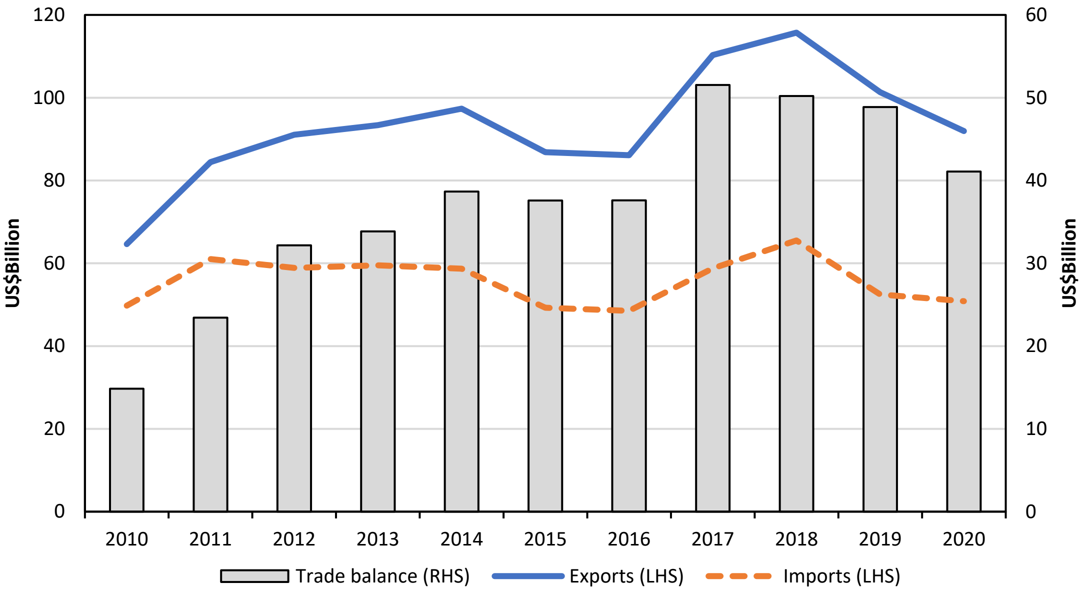
FIGURE 4 BREAKDOWN OF SOUTH KOREA'S OFDI IN ASEAN AND INDIA 2010-2020



Source: Korea Exim Bank.

Note: ASEAN-5 includes Malaysia, Thailand, Indonesia, the Philippines and Brunei. The rest of ASEAN includes Myanmar, Cambodia and Laos.

FIGURE 5 SOUTH KOREA'S TRADE WITH NSP COUNTRIES 2010-2020



Source: CEIC.

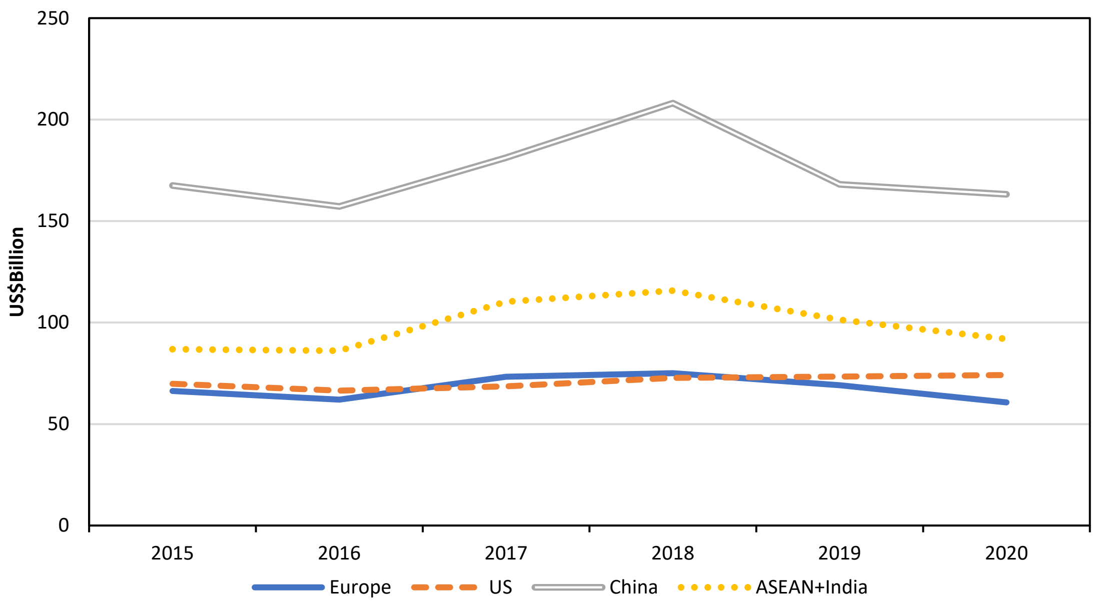
13 Seventy-two per cent of respondents in ASEAN expressed their worries of China gaining economic influence and 85% expressed concerns about China's rising strategic and political influence. Tan, S M et al, *The state of Southeast Asia: 2020*, ISEAS-Yusof Ishak Institute, Singapore, 2020.

Trade Diversification through the NSP Remains a Challenging Task

4.1 The higher US tariffs on Chinese products affected Korea's exports of intermediate goods to China for final production and for the American market. South Korea's total exports declined by 10%, with exports to Hong Kong (-31%) and China (-16%) registering the most significant drop in 2020.[14]

4.2 Meanwhile, South Korea's exports to NSP countries also deteriorated (Figure 6) in 2020 even though NSP countries were not the targets of America's sanctions. Korea's imports from NSP countries declined as well amid the US-China trade war (Figure 7).

FIGURE 6 SOUTH KOREA'S MAJOR EXPORT DESTINATIONS 2015-2020



Source: CEIC.

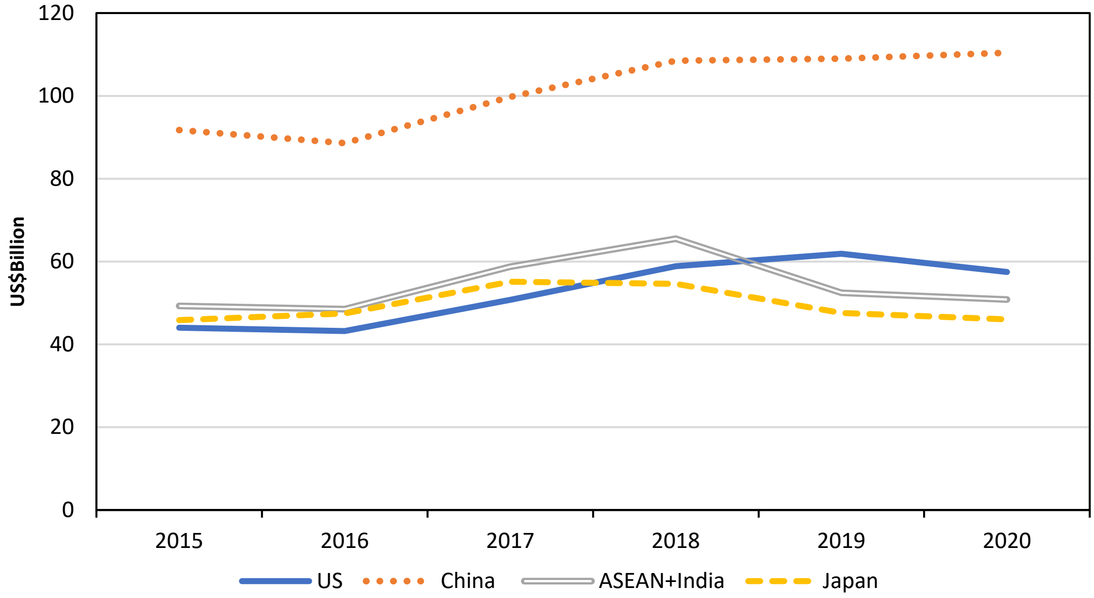
4.3 The waning trade exchanges with NSP countries indicated that the US-China trade war has impacted not only Korean exports to China, but also a wider regional supply chain network. East Asian economies are closely intertwined with each other in manufacturing production.

14 Data source: CEIC.

4.4 Despite Korea's progressive trade exchanges with NSP countries in the past few years, China and Hong Kong still accounted for most of Korean exports. In 2020, 32% of Korea's exports went to China, compared to 18% to NSP countries.[15]

4.5 Unlike the decreasing imports from NSP countries, Korea's imports from China have been gradually increasing. In comparison, imports from the United States and Japan have been sluggish (Figure 7). China's industrial upgrading has made itself an increasingly important supplier of industrial goods for Korea.

FIGURE 7 SOUTH KOREA'S MAIN SOURCES OF IMPORT 2015-2020



Source: CEIC.

4.6 China's official figures show the strong industrial partnership in bilateral trade ties. Nearly two-thirds of China's imports from and almost half of its exports to Korea were machinery and electrical equipment in 2019.[16]

4.7 Apart from manufacturing final consumption goods for multinational corporations (MNCs), part of China's strong demand for South Korea's key components came from local Chinese firms. China's Huawei particularly relied on Samsung's advanced semiconductor chips for its smartphones.

[15] Data source: CEIC.

[16] Data source: CEIC.

4.8 Hence, Samsung's semiconductor production benefitted from Huawei's large share in China's smartphone market despite being competitors. Samsung may lose an important source of revenue if the United States requests for a ban on components supply to Huawei.

4.9 Given China's strong demand for South Korea's components, China is likely to remain a key export destination for South Korea. China market-oriented Korean firms may still opt to stay in China while continuing to procure capital equipment and intermediate goods from Korea.

4.10 South Korea's trade with China was nearly two times that with NSP countries in 2020. The heavy reliance on China for trade suggests that the process of trade de-coupling could be lengthy and costly for South Korean firms.

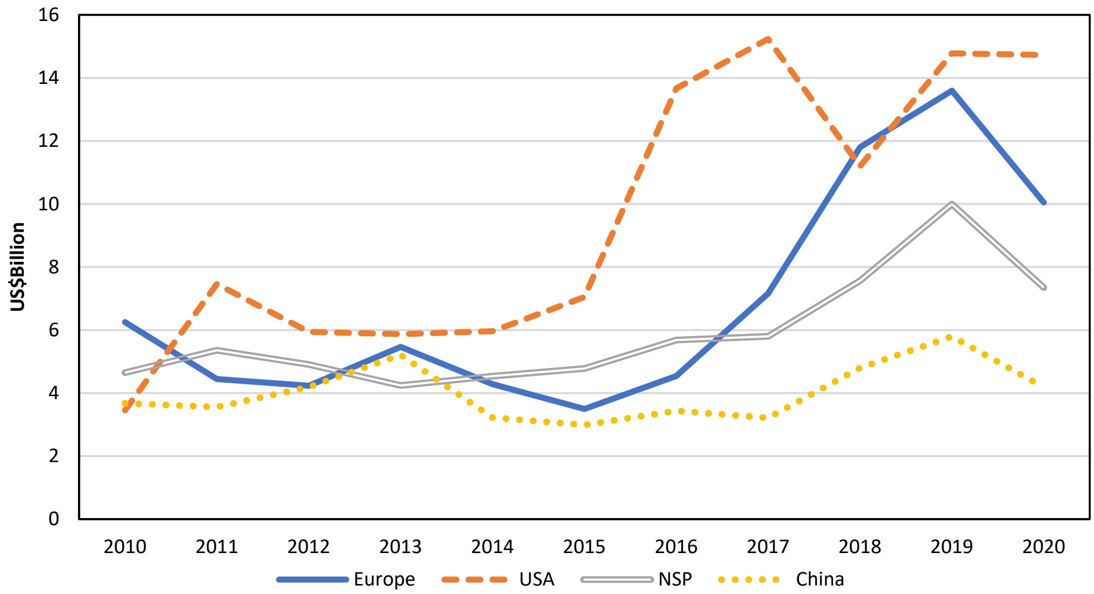
4.11 ASEAN's close trade ties with China is another hurdle. China is ASEAN's largest trading partner. The full implementation of ASEAN-China free trade area (ACFTA) since 2015 has facilitated China's exports of intermediate goods to ASEAN, notably to Vietnam.

4.12 Hence, South Korea's trade relations with NSP countries should be viewed as part of a wider regional production network, with China playing an essential role. The greater institutionalised regional economic integration would enhance not only South Korea's trade connections with NSP countries, but also its economic ties with and between other regional economies.

Worldwide OFDI Expansion in Response to Geopolitical Uncertainty

5.1 With the launch of the NSP, South Korea's OFDI in NSP countries has been growing since 2018. This growth is however not particularly significant as Korea's OFDI in the United States and Europe grew even more at the same time (Figure 8).

FIGURE 8 SOUTH KOREA'S OFDI BY SELECTED DESTINATION 2010-2020



Source: CEIC.

5.2 Although South Korea's OFDI in NSP countries has surpassed its OFDI in China, NSP countries have not replaced China's role as the main overseas production site for Korean firms. Korea's OFDI by sector shows that its manufacturing investment has been shifting to the United States and Europe in the last few years (Table 1).

5.3 The United States accounted for 11% of South Korea's OFDI in manufacturing in 2015 and 20% in 2020. The investment surge in the United States has been especially clear since 2018 as a response to the US-China trade war (Table 1).

5.4 In comparison, Europe's share in Korea's OFDI rose from eight per cent in 2015 to 15% in 2020. NSP's share once grew to 35% in 2017 but declined to 24% in 2020. China's weight remained relatively unchanged during the same period (Table 1).

5.5 Distance accounted for the relocation of Korea's manufacturing OFDI to end users' markets (such as the United States and Europe), rather than in low-cost production sites. This explains South Korea's substantial manufacturing OFDI in Europe and the United States in recent years, instead of rushing into low-cost developing countries in the region.

TABLE 1 BREAKDOWN OF SOUTH KOREA'S OFDI BY SECTOR 2015-2020

Manufacturing (%)						
	2015	**2016**	**2017**	**2018**	**2019**	**2020**
United States	11	15	12	9	21	20
Europe	8	7	11	16	16	15
NSP countries	24	30	35	22	24	24
China	30	29	27	27	29	28
Total OFDI in manufacturing (US$ billion)	8.0	8.7	8.9	16.3	18.8	12.9
Services (%)						
	2015	**2016**	**2017**	**2018**	**2019**	**2020**
United States	33	43	41	28	27	30
Europe	13	14	18	28	26	20
NSP countries	9	9	7	11	13	16
China	3	3	2	1	1	1
Total OFDI in services (US$ billion)	18.7	28.0	34.3	32.5	40.4	39.8

Source: Korea Exim Bank.

5.6 Samsung has shifted all of its smartphone production from China to other developing countries since 2019 due to its deteriorating smartphone sales in China.[17] However, Samsung has continued to invest in manufacturing semiconductor chips in China to meet the huge surge in global demand for high-tech products.

5.7 With greater economic integration, the division of labour becomes more delicate. Developing countries in the region filled the vacuum in labour-intensive manufacturing when China upgraded to produce products with higher level of technological complexity which developing countries are incapable of producing.

5.8 NSP countries' incapability to improve their investment environment could also have accounted for the reluctance of Korean firms to shift all of their manufacturing production to the region. The World Bank's Doing Business Report 2020 ranked most NSP countries as less attractive destinations for foreign investors. Only Singapore, Thailand and Malaysia are ahead of China in the ranking.[18]

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[17] Ju-Min Park, "Samsung ends mobile phone production in China", Reuters, 2 October 2019, <https://www.reuters.com/article/us-samsung-elec-china-idUSKBN1WH0LR> (accessed 6 May 2021).

[18] *Doing Business: Measuring Business Regulations*, The World Bank, <https://www.doingbusiness.org/en/doingbusiness> (accessed 30 April 2021).

5.9 The lack of infrastructure and regulatory business environment has made the less developed NSP countries less attractive to foreign business operation. The infrastructure will need long-term financial commitment whereas improving regulatory business environment will need a dramatic change in domestic politics. Both will take a long time to realise.

5.10 The United States and Europe accounted for most of Korea's investment in services. Korea's OFDI in services in NSP countries increased clearly from nine per cent in 2015 to 16% in 2020 and mostly to Singapore. In comparison, Korea's service investment in China is trivial (Table 1).

5.11 Conversely, Korea's OFDI in NSP countries is more in services. During the 2015-2019 period, Korea's manufacturing investment in NSP countries (US$6.7 billion) is less than half of its investment in services (US$15.6 billion).[19]

5.12 Apart from investing in Singapore's real estate and financial services, Korean firms also invested heavily in wholesale and retail sectors in NSP countries, notably in Vietnam. Vietnam's wide FTAs and geographical proximity to China and other ASEAN countries have much to do with the country's newly enhanced role as a regional distribution centre.[20]

Hurdles to Diversifying Sources of Inbound Tourism through the NSP

6.1 South Korea's foreign visitor arrivals and tourism revenue clearly swelled during the 2012-2016 period thanks to the surging number of Chinese tourists (Table 2). However, Korea's growing reliance on China for its tourism industry's development became a tool for China to discipline Korea in the event of a political disagreement.

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[19] Data source: Korea Eximbank.

[20] Dezan Shira and associate, "Q&A: ALL EYES ON Vietnam-why and ow to enter the market", *Vietnam Briefing*, 22 April 2021 < https://www.vietnam-briefing.com/news/qa-all-eyes-on-vietnam-why-and-how-to-enter-the-market.html/> (accessed 6 May 2021).

TABLE 2 BREAKDOWN OF VISITOR ARRIVALS IN SOUTH KOREA 2010-2020

	As % of total visitor arrivals				Total visitor arrivals (million people)	Tourism revenue (US$ billion)
	China	NSP countries	United States	Europe		
2010	21.3	12.8	7.4	7.3	8.8	10.3
2011	22.7	13.6	6.8	7.0	9.8	12.3
2012	25.5	13.4	6.3	6.4	11.1	13.4
2013	35.5	13.8	5.9	6.3	12.2	14.5
2014	43.1	13.6	5.4	6.0	14.2	17.7
2015	45.2	13.3	5.8	6.1	13.2	15.1
2016	46.8	14.0	5.0	5.5	17.2	17.2
2017	31.3	17.0	6.5	7.0	13.3	13.3
2018	31.2	16.8	6.3	6.5	15.3	18.5
2019	34.4	16.2	6.0	6.3	17.5	21.5
2020	27.2	19.8	8.7	8.5	2.5	10.4

Source: CEIC.

6.2 The number of Chinese tourists to South Korea declined by 48% in 2017 to less than 4.2 million. With better bilateral relations, the number of Chinese tourists gradually increased to six million in 2019. However, it is still far below the peak of 2016 (eight million) before China's sanction.[21]

6.3 In comparison, visitors from NSP countries to Korea has been slow in developing. Before the COVID-19 pandemic, visitors from NSP countries to Korea rose slowly from less than one million in 2009 to nearly 2.7 million in 2019. The number of visitors from NSP countries was less than half of visitors from China in 2019.

6.4 Thailand is Korea's largest source of inbound tourism among ASEAN countries. In 2019, 571,610 Thai tourists visited Korea, followed by 553,731 from Vietnam and 503,867 from the Philippines.[22]

6.5 NSP countries' huge population size suggests that South Korea could diversify its tourism dependence on China. Nonetheless, the relatively low income of most NSP countries will restrain its potential contribution to Korea's tourism revenue.

[21] Data source: CEIC.

[22] Data source: CEIC.

6.6 Tourist expenditure of NSP visitors to Korea's tourism industry pales in comparison with Chinese tourists' average expenditure per capita of US$1,633, which is even higher than those of more developed NSP countries, such as Singapore (US$1,218), Malaysia (US$947), Thailand (US$945).[23]

6.7 Most visitors from NSP countries went to Korea for work or study. Migrant workers from Thailand, Vietnam and the Philippines on the other hand form an important source of inbound tourism for Korea. Vietnam is the second most important source of foreign students for South Korea.[24]

6.8 The greater exchanges in cultural and education tourism through the NSP may be helpful in increasing the number of visitors from NSP countries to Korea. However, it will need substantial financial commitment from Korea, such as providing scholarship and fellowship for students and scholars from NSP countries.

6.9 As part of the NSP, the South Korean government has allowed multiple entry visa application for highly skilled professionals from NSP countries to boost inbound tourism from NSP countries.[25]

6.10 Korean visitors to NSP countries on the other hand have surged. The intensifying economic relations have brought more Korean visitors to ASEAN countries, rising from 2.4 million in 2009 to over 10 million in 2019 (Figure 9).

6.11 Vietnam is the most popular destination for Korean travellers, accounting for 41% of Korean visitors to ASEAN countries in 2019. This growth in South Korea's outbound travellers to Vietnam is largely triggered by the development of trade and investment relations between the two countries

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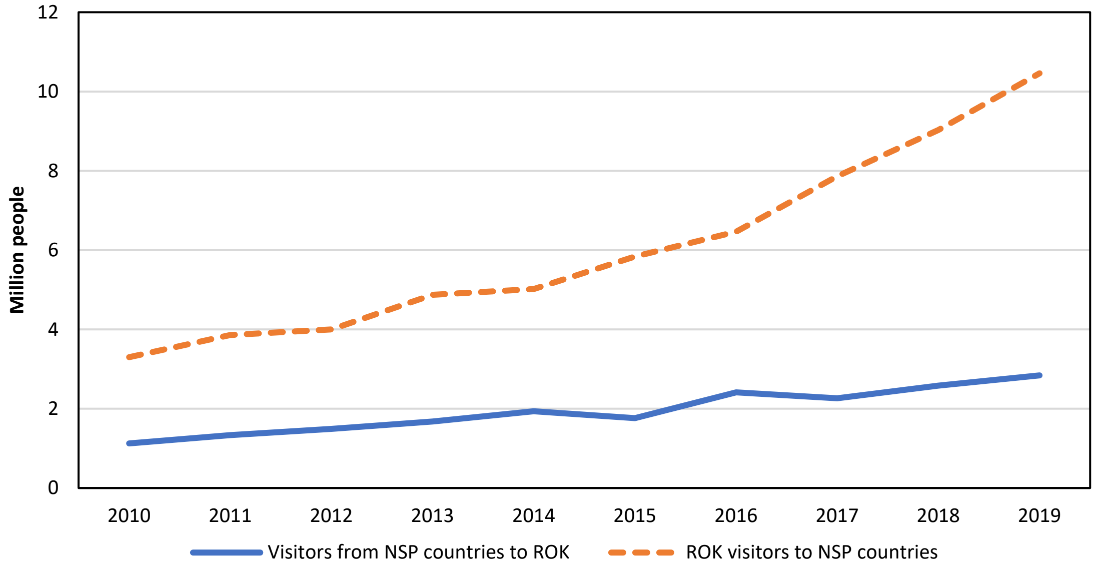
[23] Data source: CEIC.

[24] Of the total number of foreign students in South Korea in 2019, 23% were from Vietnam, after China's 44%. Nam Kyung-don, "Nearly 15% of foreigners in S. Korea illegal immigrants", *The Korea Herald*, 21 October 2019 (accessed 18 March 2020).

[25] Park Hye Ri and Lee Hana, "11 Southeast and South Asian countries granted multiple-entry visa for Korea", Ministry of Culture, Sports and Tourism and Korean Culture and Information Service, 3 December 2018, <https://www.korea.net/NewsFocus/policies/view?articleId=166059> (accessed 6 May 2021).

FIGURE 9 BILATERAL TOURISM BETWEEN ROK AND NSP COUNTRIES 2010-2020



Data source: CEIC and *ASEAN Statistical Yearbook 2020*.

6.12 The greater number of visitors to Vietnam is hence business-driven tourism (as Vietnam is Korea's most important OFDI destination and trade partner). The rise of Korean visitors to Vietnam also made South Korea the second largest source of inbound tourism for Vietnam, after China.

The NSP's Outlook amid US-China Rivalry

7.1 South Korea has been caught between a rock and a hard place after US-China trade war intensified. While Korea has been relying on the United States for its national security, it has depended on China for settling North Korean issues, apart from its economic reliance.

7.2 So far, the Biden administration has maintained its higher tariff on certain Chinese goods, indicating that South Korea's export-oriented investment in China for the US market could gradually decelerate. To minimise the impact of uncertain geopolitical factors, Korean firms will likely invest in countries beyond China, including in NSP countries to diversify the risks.

7.3 On the other hand, both the Biden administration and Chinese government have indicated that they do not seek economic de-coupling. The less severe US-China rivalry on the economic front will facilitate Korean firms' business operation in the whole region, including Korea's greater economic integration with NSP countries.

7.4 Indeed, US' "anti-China" trade policy under the Trump administration went counter to South Korea's long insisted policy of diversified trade relations. After two decades of efforts, South Korea has secured economic agreements with 12 countries and four trade blocs in the world.[26] Korea is one of the two countries in Asia[27] that has implemented FTA with China, the European Union and the United States.

7.5 Korea may face tremendous difficulties withdrawing from its multilateral trade network strategy to side with one in the G-2 economic structure. South Korea's hesitance to side with the United States could also be attributed to the United States' inactive response to China's economic sanction on Korea against the deployment of the THAAD.

7.6 The NSP does not seem to be effectively diverting Korea's economic dependence from big powers to NSP countries so far. Instead, Korean firms reacted to US-China trade war by investing more in America. Although Korea's exports to China have declined, its imports from China continued to grow.

7.7 Korea's growing economic ties with NSP countries over the past decades have been driven by the development of wider regional division of labour, in which the United States, China and Japan have played a key role. Any economic disruption between the three would significantly impact on Korea's economic ties with NSP countries.

7.8 As such, despite close economic links with NSP countries, South Korea's economic growth will still be severely impacted by the United States' unilateral trade sanctions against Chinese exports. Ironically, Korea's high technology firms benefitted from US sanctions against Chinese high-tech giants.

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[26] The 12 countries include Canada, the United States, Colombia, Peru, Chile, China, Vietnam, Australia, New Zealand, Singapore, India and Turkey. The four economic blocs include ASEAN, the European Union (EU), European Free Trade Association (EFTA) and Regional Comprehensive Economic Partnership.

[27] The other is Singapore.

7.9 While being a key component supplier to China's branded ICT products (such as Huawei and Xiaomi), Samsung is also an important global maker of ICT products and a competitor to Chinese branded products. Samsung is also in serious competition with its Chinese counterparts in other essential components such as in producing semiconductor chips and 5G equipment.

7.10 In areas where it is not as competitive as its Chinese counterparts, South Korea is shifting its OFDI in final assembly away from China. NSP countries are not only an alternative cheap production site, but also a booming market for South Korea's consumption goods.

7.11 To minimise the impact of external powers on its economy, South Korea may consider enhancing the importance of NSP countries by incorporating more members (example Australia) or cooperating on other regional initiatives (such as China's Belt and Road, India's Act East policy and America's Indo-Pacific strategy).

7.12 The inclusion of more regional economies in NSP is in line with the development of greater regional economic integration (example Regional Comprehensive Economic Partnership). South Korea may also need to join the Comprehensive and Progressive Agreement for Trans-Pacific Partnership to make its presence felt in the evolving regional political economy.