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2010 Modularization of Korea's Development Experience: Export Promotion

2011

MINISTRY OF STRATEGY AND FINANCE

KDI Korea Development Institute

2010 Modularization of Korea's Development Experience:
Export Promotion

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Preface

In the 21st century, knowledge is one of the key determinants of a country's socio-economic development. In recognition of this fact, the Ministry of Strategy and Finance (MOSF) and the Korea Development Institute (KDI) launched Knowledge Sharing Program (KSP) in 2004. The KSP aims to share Korea's development experience and knowledge to assist socio-economic development of partner countries.

The KSP is comprised of three parts: 1) the systemization and modularization of Korea's development experiences into case studies, 2) policy consultation through knowledge sharing with partner countries, and 3) joint consulting with international organizations. The systemization and modularization of Korea's development experience researches and documents Korea's successful policy experiences, such as the 'Five-Year Economic Development Plan' and 'Saemaul Undong (New Village Movement).' The policy topics are 'systemized' in terms of the background, implementation and outcome, and then, presented as case studies in order to achieve a complete understanding of the actual policies. These systemized policy case studies are further 'modularized' by sector so they can be utilized as concrete examples by partner countries to meet their interests in specific institutions, organizations or projects. For example, Korea's 'Export Promotion Policy' has been prepared as a systemized case study while 'the Establishment of the Export-Import Bank' has been modularized to provide a specific example of Korea's export promotion experience in export financing. The modularization of Korea's development experience traces back to a policy's inception and recapitulates the rationale for its introduction; its main content; and its implementation mechanism. The case studies also evaluate a policy's outcome and draw insights with a global comparative perspective. These case studies include literature reviews, surveys and in-depth interviews with the policy practitioners and experts who participated in the implementation process.

The systemization of Korea's development experience was initiated in 2007 and finished in 2009. Under the new Modularization Project, launched in 2010, the plan has been set out to modularize 100 case studies by sectors and topics in three years.

I would like to take this opportunity to express my sincere gratitude to Project Manager, Dr. Wonhyuk Lim, and all the Korean experts for their immense efforts in successfully completing the '2010 Modularization of Korea's Development Experience.' I am also grateful to Managing Director, Dr. Kwang-Eon Sul, and Program Officer, Ms. Ja-Kyung Hong, the members of the Center for International Development, KDI, for their hard work and dedication to this Program.

I earnestly hope that the final research results will be fully utilized in assisting the development partner countries in the near future.

Oh-Seok Hyun
President
Korea Development Institute

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Chapter 01

Establishment of Free Export Zones

Chapter 01

Establishment of Free Export Zones

DoHoon Kim(Korea Institute for Industrial Economics & Trade)

<Summary>

Korea undertook a variety of supplementary export promotion measures to build on the successful export promotion policies of 1960s. In this regard, the Korean government established “Free Export Zones (FEZs)” in Masan and Iksan after adopting “the establishment act of Free Export Zones” in 1970 and let foreign firms enter Korea to produce export products in these zones.

FEZs were established on the back of governmental-wide efforts. The Ministry of Construction was in charge of land and infrastructure, while the Ministry of Commerce and Industry was in charge of managing the FEZs. Investors in FEZs were in principle foreign firms. They benefited from tariff exemptions on imported goods to FEZs as well as from tax incentives and low cost of installation, etc. Among the two FEZs, the Masan FEZ has been regarded as having been more successful than the Iksan FEZ. The Masan FEZ not only brought about the expected outcomes such as increased exports, foreign exchange earnings, investment inflows and jobs, but also contributed to improving the industrial strength in the vicinity of the FEZ via import of advanced technology. On the other hand, the Iksan FEZ fell short of expectation due to the underdeveloped of supporting industries and inconvenient logistics nearby.

Other countries have also established industrial zones similar to Korea’s FEZs. Singapore has been operating Free Trade Zones focused on logistic competitiveness. Taiwan and China have managed export processing zones similar to Korea’s FEZs, which are focused on manufacturing production of foreign investors. The United States have established Free Trade

Zones targeting both logistics and production at the same time.

These FEZs faced new economic challenges, including the successful Masan FEZ, in the late 1990s, as Korea's wage advantage for export-oriented foreign firms rapidly declined at the expense of other developing countries. Therefore, the Korean government wanted to transform these FEZs into "free economic zones," which allow for greater competitiveness in logistical and urban functions as well as manufacturing production.

Based upon Korea's experience with FEZs, we can suggest the following lessons for developing countries: firstly, locations with good infrastructure and supporting industries should be selected; secondly, adequate incentives should be provided to investors, and the legal and institutional system should be appropriately adapted based on the economic development level.

1. Introduction

Korea started an additional export promotion policy in the 1970's to build on the success of the 1960's when the economy began to develop and exports showed an explosive growth.

Korea established various export promoting organizations, adopted new ways of supporting exports and promoted general trading companies to improve the export capacity of the private sector. Also, the export-based industrial complex in Guro, Seoul boosted export growth.

The Free Export Zone that this article will discuss demonstrates the will of the Korean government to grow exports. However, it also helped to attract foreign investment, to enhance the industrial structure of manufacturing, and to adopt advanced technologies. Furthermore, Korea needed to create new job opportunities as the economy largely depended on traditional agriculture. So the policy objective to expand employment should be considered as well.

Therefore, we analyzed the reason, the process, and managing method of the FEZ and tried to evaluate the impact of the Free Export Zone. Applying the outcome evaluation method, we will compare successful and unsuccessful Free Export Zones, and identify the causes of success and failure. Next, similar overseas cases are also analyzed and compared.

The structure of Korean economy underwent great change in the 1990's. Also, pressures for competitive cost brought on by the next-tier developing countries including China and ASEAN led to a shift toward the Free Export Zone policy. So the Korean government began a policy shift to upgrade the domestic industrial structure and the environment. This article analyzes the process of change over time and discusses the policy on the present Free Export Zone. Also the development direction of the present policy will be discussed.

Lastly, the article tries to draw policy insights and lessons for developing countries that seek to adopt the policy.

2. Establishment Process of Free Export Zones

2.1. Background

There were several background stories to the Korean government's legislation of the 「Free Export Zone Establishment Act」, which designated the Free Export Zones in Masan, Gyeongsangnam-do and Iksan, Jeollabuk-do, and introduced various incentives to lure exporters in these FEZs.

Firstly, there was a great deal of political will to develop the economy based on exports as the government was encouraged by the success of the export drive policy in the 1960's. The export promotion policy was propelled by the Korean government in the 1960's with wide and systematic support such as exchange rate depreciation, financial and tax support, lower tariffs on exporting equipment and preferential support to exporters earning foreign exchange. Also, monthly export promotion meetings under the supervision of the president and other administrative supports including awards given to exporters were added to those systemic supports so that manufacturing exports grew explosively. The world average export increase rate in the 1960's was about 10%, Japan's relatively high average was about 20%, but Korea's was up to 40%, which shows that the export promotion policies led to good results. Also, the national economy grew rapidly on the back of exports which gave the government confidence that export growth would drive economic development. The establishment of Free Export Zones was among alternative policies considered for promoting export growth.

Next, the success of the Korean export industrial complex, Guro Industrial Complex, a result of the 「Export Industrial Complex Development Act」, became the leading reason to establishing Free Export Zones to create similar effects. Exporting companies started their businesses in the Guro Industrial Complex in 1965. At the time, there were only eight companies including seven overseas Korean companies and one domestic company. By 1967, there were 31 companies including 18 overseas Korean companies, 11 domestic companies, and two foreign companies. The types of businesses were usually labor-intensive light industries such as electronics, wigs, optic lenses, textile goods, bicycles, synthetic resin goods, toys and leather wears which moved from Japan to Korea, because of Japan's weakened export competiveness due to the lack of a competitive labor force.[1]

The Korean government decided to establish Free Export Zones that not only aimed at exports but also seeked to create better investment conditions to attract more high-tech companies.

Despite the success achieved in growing exports in the 1960's unfortunately, the downside of the export promotion policy in the 1960's was that foreign investment companies did not come and the technology transfer itself was not enhanced. To solve these problems, the government tried to create conditions to attract foreign companies with high technology, especially Japanese companies. Indeed, the Free Export Zones were mostly established in the southern coast of Korea to attract Japanese companies.

Lastly, the goal to use Korea's rich labor force and create new jobs in the late 1960's was pursued too. The fact that the Guro Industrial Complex had created a lot of jobs was considered too. Though not explicitly stated, one of the policy objectives was to create job opportunities for local workers. To conclude, the establishment of the Free Export Zone contained a complex set of policy objectives including promotion of exports, inducement of foreign investment, creation of jobs, and upgrading of technology.

2.2. Selection of Free Export Zones

「Export Industrial Complex Development Act」 was enacted in 1964. When the government was discussing the Free Export Zone, businessmen from Masan opened a grand meeting to establish a Free Export Zone in Masan and enthusiastically pursued to have a Free Export Zone. In January 28th, 1969, the 「Electronics Promotion Act(Act no. 2098)」 allowed the Ministry of Commerce and Industry to build an electronics industrial complex to promote exports. On July 2, 1969, Kim Hak Ryul, the head of the Economic Planning Board and Deputy Prime Minister proposed the establishment of a Free Export Zone in the southern coast of Korea. On July 5, a commission was created to lead its establishment. The commission selected Masan, Pohang, Incheon, Yeosu, Samcheonpo, Mokpo, Geojedo and Ulsan as potential candidates. Next, after on-site assessments of possible locations, Masan Harbor was selected as the primary site, because of its logistical infrastructure including harbor and airport, which were nearby the city, the ability to secure water and power, and the possibility to attract labor force.[2]

1. KITA, *History of International Trade in Korea*, 2006, p.164.
2. Ibid., p.137.

Debate on the「Export Industrial Complex Development Act」 intensified in September1969, going through the National Assembly in December, and officially going into effect in January 1970. The Free Zone Intendance was put under the Ministry of Commerce and Industry, which managed and operated the Free Export Zone. The Masan Intendance was established on April 3, 1970, and the independently operated Iksan Local Industrial Complex was designated as another Free Export Zone. The Iksan Intendance was established on January 15, 1973 which started the free export. With the announcement of the heavy and chemical industrialization drive, President Park Jung-hee stated that "a mass electronics component production complex will be introduced and we are planning to make 2~3 more FEZs like the Free Export Zone in Masan".

2.3. Designation, Establishment and Operation of Free Export Zones

The establishment of a Free Export Zone is supposed to be based on the recommendations of the Ministry of Home Affairs who takes into consideration the suggestions made by the Ministry of Construction and finally to be designated by the Ministry of Commerce and Industry[3]. Eventually, the Ministry of Commerce and Industry who is responsible for export promotion and industrial development is in charge of managing the FEZ in cooperation with the two other ministries.

The Ministry of Construction is responsible for the construction of the infrastructure such as the land, roads, drainage facilities, sea dredges, and harbor facilities[4]; in other words, the construction of the basic conditions needed for the companies to move in, produce, and export.

However, once a Free Export Zone becomes operational, the Ministry of Commerce and Industry should be responsible for the management and operation of the Free Export Zone. This is because the same law prescribes that every FEZ should have a Free Zone Intendance under the supervision of the Ministry of Commerce and Industry. Because the Ministry of Commerce and Industry is in charge of export and industrial management, this is fairly reasonable allocation of responsibility. The responsibilities of the intendance include[5]:

1. Establishment of various supporting facilities
2. Recommendation of companies and supporting companies that can operate in the FEZ
3. Supervision of construction of factories, etc.

3. Free Export Zone Establishment Act(FEZEA, Law No.2180, 1970.1.1), Clause 3.
4. FEZEA, Clause 4.
5. FEZEA, Clause 5.

4. Permitting export and import of products
5. Supervision of companies and supporting companies in the FEZ
6. Cooperation for job placement
7. Other aspects related to management and operation of the Free Export Zone

Under the Free Export Zone Establishment Act, the regulations of the Ministry of Commerce and Industry and those of other ministries should be entrusted to the intendances that manage FEZs to facilitate smooth investment, production, and exporting by FEZ companies. The important objective was to attract foreign investment into the Free Export Zone, which led the Economic Planning Board to entrust most of the regulations of the「foreign capital introduction law」to the Ministry of Commerce and Industry[6].

A committee was created to deliberate on big issues related to the operation of the Free Export Zone[7]. This was a way to solve problems related to several ministries. The head of the committee is the Deputy Minister of Commerce and Industry and is comprised of 17 members including the head.

The Free Export Zone Establishment Act states that the members of the committee should be comprised of the following[8].

1. Deputy Minister of the Economic Planning Board
2. Deputy Minister of the Ministry of Foreign Affairs
3. Deputy Minister of the Ministry of Home Affairs
4. Deputy Minister of the Ministry of Finance
5. Deputy Minister of the Ministry of Justice
6. Deputy Minister of the Ministry of Construction
7. Deputy Minister of the Ministry of Transportation
8. Head of the Labor Office
9. Head of the intendance that is designated by the Minister of Commerce and Industry
10. Head of the Korean Exchange Bank
11. Others who are appointed by the Minister of Commerce and Industry among qualified candidates

6. FEZEA, Clause 12.
7. Presidential Decree based on FEZEA(Decree No.4682. 1970.2.2), Clause 3.
8. The same Decree, Clause 3, No.3.

2.4. The Investment Conditions in the Free Export Zone

2.4.1. Conditions for Qualification as a FEZ Company

Favorable conditions and incentives for establishing a company in FEZs were given by the Korean government to support investment, production and export. Due to these reasons, the demand was expected to be big. As such, companies that sought to operate in the FEZs were made subject to the following conditions[9]:

1. The company should produce or process export products and the type of business and items should be in line with the objectives of the free zone.
2. The Korean investment ratio should not be over 50 out of 100.
3. Export prospect should be sure
4. Foreign exchange earning rate should be high
5. Manufacturing technology should be advanced
6. Labor integration should be high

In other words, companies could only operate in FEZs if it was exporting goods. While domestic companies were excluded, foreign investment companies (independent venture or joint venture) were targeted. Also, extents of the transfer of high technology and creation of jobs were considered too.

2.4.2. Incentives to Companies in the Free Export Zone

In the Free Export Zone, companies are basically exempt from the application of the customs law. In other words, a company in the Free Export Zone is exempt from tariffs when building a factory or importing necessary goods in the FEZ[10]. Companies in FEZs are also exempted from export inspections except under specific conditions[11].

However, products produced in the Free Export Zone were strictly banned from the domestic market. This also included imported goods and by-products of the Free Export Zone. However, when the goods were judged not to hinder the domestic industry, they were permitted on a case by case basis[12].

When a strike occurred in a company in the Free Export Zone, the regulations related to the

9. The same Decree, Clause 8, No.1.
10. FEZEA, Clause 13.
11. FEZEA, Clause 12.
12. FEZEA, Clause 14.

public services in the 「Conciliation Act」were applied to protect the interest of the company as much as the government could[13]. Also, the companies did not have to follow the「Employment Supplying Act」which gave preference to job seekers who had completed their military service requirements to ensure that companies could employ only the most efficient workers[14].

The more important point was that various types of financial and tax incentives were given. Firstly, the companies in the FEZs paid lower rental fees for the land or buildings (factories). Usually they paid a favorable rent, which was around 1%, compared to the average 10-20% outside of the zone.

Next, foreign investment companies which meet specific conditions were exempted from corporate and income tax (100% for five years and 50% for the subsequent two years), and could also be exempted from acquisition, registration, property and general income tax for a maximum of 15 years. Also, FEZ companies were exempted from the value added tax for domestic products and labor used in the zone[15].

Also numerous administrative services were offered by the free zone intendance in the Free Export Zone.

3. Outcome of the Free Export Zone Operation

The fact that the Masan Free Export Zone which was established in 1970 is still being operated today in 2010, after it was changed into a Free Trade Zone, shows the policy's successful outcome. The Iksan Free Export Zone, established in 1973, had not shown the same kind of results. So after the two Free Export Zones changed into Free Trade Zones in 2000, the Iksan Free Trade Zone was closed down in 2005 and the Free Trade Zone moved to Gunsan nearby.

3.1. Outcome of the Masan Free Export Zone

Here, we will examine the results of the Free Export Zone, based on Masan's experience which has well organized data. The Masan Free Export Zone has been the most successful FEZ, and is the only Free Export Zone that is still operating today, though the initial goals of the zone

13. FEZEA, Clause 18.
14. FEZEA, Clause 20.
15. KIET, *How to Build Facilitation and Effective Management System of Free Export Zones*, July 2007.

have changed somewhat.

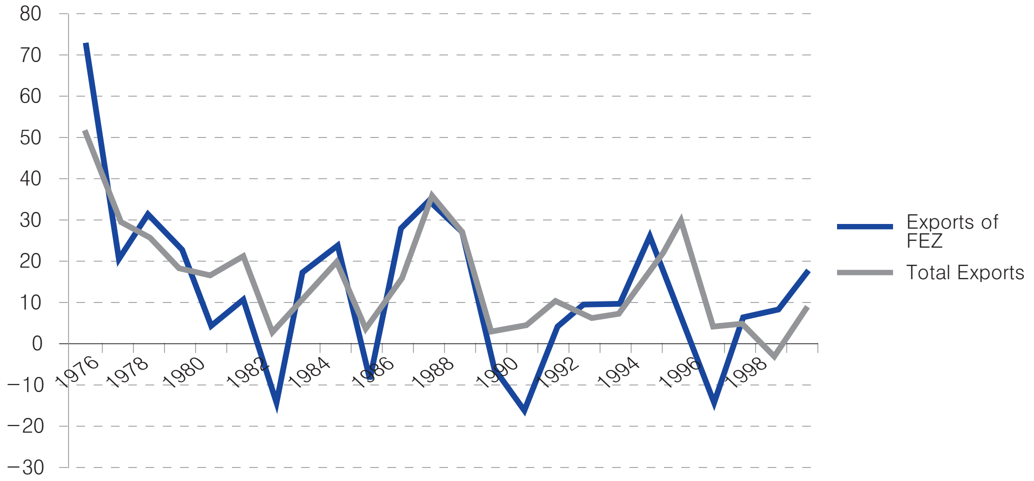
3.1.1. Impact on Exports

In respect to the goal of export promotion, The Masan Free Export Zone generated 4.07% of Korea's gross export, three years after its establishment. After that, it maintained a share of about 3% for approximately 10 years, falling under 3% after 1981, and at times under 2% after 1996.

If you look at the export growth pattern (excluding the initial period (1971-1975) which is irrelevant for comparison) from 1976 to 2000 when it was changed into a Free Trade Zone, the rate of export growth is similar and at sometimes a bit lower compared to the rate of Korea's gross export growth. (Refer to <Figure 1-1>)

Therefore, it is hard to say that the Masan Free Export Zone contributed greatly to the growth of total exports. Though, the fact that it maintained a growth rate of 2%-3% does show that it played a part in Korea's export growth.

Figure 1-1 | Export Growth Rate in the Free Export Zone(Compared with Gross Export)

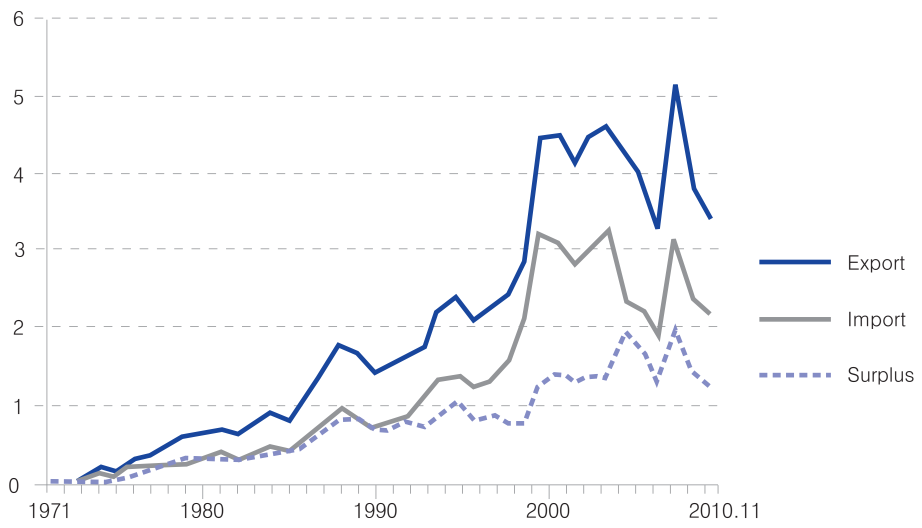


3.1.2. Impact on Foreign Exchange Earning

The most eminent result of the Masan Free Export Zone is the steady surplus of exports, which is much higher than the amount of import materials needed, thus resulting in foreign exchange earnings. Especially, after the Free Export Zone was established, as Korea showed a loss in trade for a long time, the trade surplus from the Free Export Zone contributed much to foreign exchange earnings.

Also after Korea suffered from the Asian financial crisis for the three years of 1998-2000, it made 800 million dollars of trade surplus annually which helped rebuild its foreign exchange reserves. Recently, the Masan FEZ's surplus has been expanding. From 1998 to November 2010, its trade surplus was up to 17.8 billion dollars which is 6.9% of the total trade surplus of Korea.

Figure 1-2 | Impact on Foreign Exchange Earnings



3.1.3. Impact on Foreign Investment Attraction

In 1973, three years after the Masan Free Export Zone was established, it attracted the largest number of companies in its history, totaling 115 with 82.83 million dollars. The number of companies decreased to less than 90 companies in the 1980's and under 80 companies after 1984, but the FEZ has attracted 75 companies since then. The total amount of investment went over 100 million dollars in 1977, over 200 million dollars in 1989, which has been maintained since then. The ratio of foreign investment has been maintained at a level of 70%-80%. Therefore, it can be said that the FEZ succeeded in inducing foreign investments after attracting foreign companies with preferential conditions in a short amount of time but also maintaining this success over time. The amount of foreign investment does not show a big increase, but as the Free Export Zone is designated within a limited area, a positive evaluation can be given. Due to this reason, the Masan Free Export Zone was evaluated as a succeeded Free Export Zone, along with the Kaohsiung Export Processing Zone in Taiwan.

In late 2010, the level of investment was 120 million dollars with 94 companies including 51 foreign investment companies.

3.1.4. Impact on Employment

The Masan Free Export Zone has led to rapid job growth and maintained a steady amount of jobs. Three years after the zone was established in 1973, the number of employees in the FEZ was over 20 thousand people, and was over 30 thousand people in the late 1970's. The number of employees was about 30 thousand people in the 1980's and about 15 thousand people in the 1990's. Therefore, it shows that job growth increased quickly at first before declining slowly as time went on.

However, the effect of employment growth is not limited only to the Free Export Zone because the companies in supporting industries that were outside the zone were estimated to be in large numbers, and these companies employed a great number of workers, too[16].

3.1.5. Impact on Technology Transfer

The multinational companies in the Masan Free Export Zone introduced high technologies and advanced management techniques. Especially, the effects from the transfer of technology guidance, quality management, and advanced facilities and equipment on the supporting industries outside of the zone were great. Furthermore, the workers employed in the Masan Free Export Zone were able to learn skills, which contributed to the development of related industries. An OECD study (2007) concludes that 3000~4000 people were estimated to have been professionally trained in Japan, and the study shows that these people moved to other companies and contributed to developing related industries[17].

This transfer of technology and know-how through the movement of labor is thought to be essential in the development of higher value-added industries and knowledge-intensive industries.

16. In 2007, the number of companies of outside supporting industries reached 314, and the number of their employees stood 5,330.
17. Michael Engman, Osamu Onodera, and Enrico Pinali, *Export Processing Zones: Past and Future Role in Trade and Development*, OECD, May 2007.

In addition, advanced corporate management techniques such as transparent corporate management and cooperative labor and management relations were also shown to have been transferred too. This can be indirectly proved by the fact that after 1994, there was not a single labor dispute in the Masan Free Export Zone.

3.2. Evaluation of Free Export Zones before Being Turned into Free Trade Zones

3.2.1. Factors that Led to Free Trade Zones

According to the studies by ILO and UNCTAD (1988), Export Processing Zones in developing countries like the free export zones in Korea showed a similar pattern of change[18]. At the beginning, the zones attracted foreign direct investments and one or two labor intensive industries such as electronics, textile or clothing grow. After the take-off, production and export increased drastically, but when it matured, foreign direct investment dropped off and the rate of increase slowed. At the same time, the cost of labor increased and the upgrading of manpower proceeded while high value-adding industries replaced basic processing and assembly industries. In the final step, the impact of export growth decreased and the export processing zone underwent a structural change.

The structural change is different for every country depending on the level of the country's economic development. In this step, the export processing zones in Korea and Taiwan changed into advanced industrial complexes producing high value-adding products and the exclusive industrial zones of China became a development foothold that includes service to agriculture.

3.2.2. Conditions Preceding the Change

Korea's Free Export Zone is seen to have undergone structural change in the late 1990's. It was ultimately changed into a Free Trade Zone in 2000 which has a similar objective but is structurally different.

Right before it changed into a Free Trade Zone in 2000, a comprehensive evaluation of the Free Trade Zones in Masan and Iksan showed the following[19].

18. ILO and UNCTAD, *Economic and Social Effects of Multinational Enterprises in Export Processing Zones*, Geneva, 1988.
19. KIM, Young Soo, How to Reform Free Export Zones, *Monthly Industrial Economy*, KIET, 1999.

In 1999, the two Free Trade Zones showed big differences. The Masan Free Export Zone had 78 companies, while most of the workers were employed less than half of the level of its peak time, but still maintained an employment level of 13 thousand. Also, it produced exports of up to 2.38 billion dollars (1998) and imports of only 1.59 billion dollars, leaving a trade surplus of 0.79 billion dollars. The number of workers decreased significantly, but based on the amount of export per area unit of free zone, it was still maintaining a high level of employment. Therefore, it can be evaluated that the decrease in the level of workers was owed the fact that labor intensive industries have been replaced by technology intensive industries such as electronics and precision tools.

Table 1-1 | The State of Free Export Zones in 1999

	Area (Ha)	Number of Companies (One)	Investment (Million Dollars)	Export (Million Dollars)	Import (Million Dollars)	Employment (Person)
Masan	79.3	78(26)	242.5	2,378	1,590	12,987
Iksan	31.1	26(6)	36.8	96	73	1,546

Source: Masan Free Export Zone Intendance, *State of Masan National Industrial Complex*, 1999
Iksan Free Export Zone Intendance, *State of Iksan National Industrial Complex*, 1999
Kim Young Soo, 『Way of Reforming Free Export Zone』, *Monthly Industrial Economy*, Korea Institute for Industrial Economics & Trade(KIET), re-quoted in 1999
Note: The figure in (parenthesis) is the number of foreign investment companies.

On the other hand, the Iksan Free Export Zone decreased in size, declining to one third of its initial size in 1973. This is because other parts of the zone were used for general industrial complexes for domestic companies. In 1999, there were 28 companies with 1,507 employees in the Iksan Free Export Zone, showing much lower results compared to the Masan Free Export Zone. The difference in performance becomes bigger in terms of exports, showing less than 5% of the result of Masan which means it is not functioning properly as a Free Export Zone.

3.2.3. Main Causes of Failure of the Iksan Free Export Zone

The Masan Free Export Zone benefited from having well-developed related industries that already existed in Ulsan and Changwon industrial sites. It also benefited from being near the export hub Busan, located near Masan. Unlike the Masan Free Export Zone, the Iksan Free Export Zone was not as successful because the industrial linkages with industries near the zone did not materialize. Moreover, compared to Masan which is located near the sea and thus can benefit from convenient distribution, Iksan is situated inland and has a disadvantage from a logistics standpoint.

Also, besides its poor location, industries in the Iksan Free Export Zone were falling behind a lot, compared to those of the Masan Free Export Zone. In 1999, many of the 78 companies in the Masan Free Export Zone, totaling 44, were high-tech businesses that produced precision instruments and electronics, while five were the fiber makers; however, about half of all the companies, or 13 out of 28 companies, in the Iksan Free Export Zone were fiber companies, which contributed to only 27.8% of all investments due to their small scale.

Table 1-2 | Comparison between Two FEZs in 1999

(Unit: $1,000)

		Fiber	Precision instrument	Electrical/ Electronics	Metal	Others	Total
Masan	Investment	7,940	57,109	157,900	16,887	9,707	249,543
	Number of enterprises	5	19	25	10	19	78
Iksan	Investment	11,360	7,222	17,610	1,042	3,625	40,859
	Number of enterprises	13	4	3	3	5	28

Source: Identical with 〈Table 1-1〉.

History of the Masan Free Export Zone

1970. 1. 1	Free Export Zone Establishment Act was proclaimed (Law Number 2180)
1970. 4. 3	Intendance of the Masan Free Export Zone was established
1971. 3. 12	First companies entered within the Free Export Zone
1973. 1. 16	Renamed to Intendance of Industrial Estate Administration Office of Masan Free Export Zone was established
1974.	The amount of annual export exceeded 100 million dollars
1977. 3. 12	Reorganized as Administration Office of the Masan Free Export Zone under the Ministry of Commerce and Industry
1981. 11. 2	Reorganized Administration Office of the Masan Free Export Zone
1986.	The amount of annual export exceeded one billion dollars
1993. 3. 6	Renamed as Administration Office of the Masan Free Export Zone under the Ministry of Commerce, Industry and Energy
1994.	The amount of annual export exceeded two billion dollars
2000. 7. 13	The Masan Free Trade Zone was established
2000	The amount of annual export exceeded 4.4 billion dollars
2002. 11. 21	The Masan Free Trade Zone was enhanced and proclaimed (Area of 302 thousand㎡ was enhanced)
2004. 3. 22	Designation and Operation of Free Trade Zone Act was proclaimed (Law Number 7201)
2008	The amount of annual export exceeded 5 billion dollars

History of the Iksan Free Export Zone

1970. 1. 1	Free Export Zone Establishment Act was proclaimed (Law Number 2180)
1973. 1. 15	Intendance of Iri Industrial Estate was established
1973. 10. 18	Part of the local industrial complex was designated as the Free Export Zone (922 thousand ㎡)
1975. 2. 5	Administration Office of Iri Free Export Zone was established
1976. 1. 26	The size of the Free Export Zone decreased. (922 thousand ㎡ → 233 thousand㎡) Others would be operated as export industries complex. (Domestic companies entered)
1986. 11	Separated into a smaller Free Export Zone (310 thousand㎡) and a general industrial complex.
1999. 1	Requested to designate the Gunsan Free Trade Zone. (by North Jeolla Province)
2000. 1. 12	Designation of the Free Trade Zone was proclaimed (Law Number 6142)
2004. 3. 22	Designation and Operation of Free Trade Zone Act was proclaimed (Law Number 7201)
2005. 10. 24	Transferred into the Intendance of Gunsan Free Trade Zone Institute
2010. 12. 31	The Iksan Free Trade Zone ceased operation

4. Similar Examples from Abroad

The function and the name of Free Export Zone or Free Trade Zone vary depending on the country's economic circumstance, the purpose of establishment, the degree of historical development, geographical condition of the established area, and so forth[20].

The Free Export Zone is known to have originated from the Free Ports in the Middle Ages. The current model of Free Trade Zones began to spread out after the Foreign Trade Zone Act of 1934 was legislated, and a Free Trade Zone was established in the United States, starting from 1936 in New York. At the time, intermediary trades such as shipping, storing, packaging, re-exporting and commercial trading activities were considered to play important roles in the Free Trade Zone.

During the 1960s and 1970s, Export Processing Zones and Free Trade Zones concentrated in

20. Beside Free Trade Zone, various other names are used: Foreign Trade Zone, Free Economic Zone, Free Port, Free Zone, Industrial Free Zone, Export Processing Zone, Foreign Access Zone.

manufacturing activities, began to appear and spread in developing countries. The Masan Free Export Zone in Korea and the Kaohsiung Export Processing Zones in Taiwan are good examples.

These Free Export Zones could be categorized into three types, depending on their function.

First, the trade-centered Free Trade Zone mainly seeks to stimulate distribution and trading activities by liberalizing regulations for international commerce. It is usually established in ports, airports, and their surrounding areas. Free Ports, which are Free Transit Zones, are good examples.

Second, production-centered Free Trade Zone mainly seeks to stimulate development of the industrial structure and technology transfer by inducing direct foreign investments. It is usually established in industrial complexes that are near coastal areas. The Export Processing Zone is a good example.

Third, more complex Free Trade Zones for production and trade are combination of production-centered and trade-centered zones. Most of Free Trade Zones are moving toward this type of hybrid model.

4.1. Free Trade Zone Centered on Logistical Hub Model

4.1.1. Concept and Features

A Free Trade Zone based on the Logistical Hub Model designates certain areas as non-tariff districts. Within this zone, imported goods are exempt from or subject to lower tariffs, excise taxes, quotas, foreign exchange restrictions and various regulations.

Products imported into a Free Trade Zone can take any forms of storage, classification, packaging, labeling and exhibition; they can even be re-exported after a certain manufacturing and assembling procedures. But goods that go into the country directly from the FTZs are subject to customs including import quota, tariff and exercise tax.

Free Trade Zones based on the Logistical Hub Model are normally located in or around a port and airport with the purpose of inducing and promoting international distribution, using the country's geographic location to its advantage. Traditional free ports and Free Trade Zones in Singapore serve as examples of this type, which were basically introduced to promote international trade, including trading of intermediate goods and re-exporting. The scale of these Free Trade Zones varies from small and duty-free shops at airports to big cities like Hong Kong or Singapore. Before 1965, when Singapore became independent, the nation was a free port city, but nowadays it operates as a Free Trade Zone, having designated its airport, harbor and nearby regions as FTZs.

From a functional standpoint, the processes of manufacturing production and assembly are combined with processes of distribution, transportation, storage, packing, and labeling to accelerate trade and distribution.

Free Trade Zones based on Logistical Hub Models are focused on easing barriers of international trade by exempting or lowering tariff and quantitative restrictions and administration regulations. Main functions of the Free Trade Zone are distribution, business and exchange, and production, which entail simple manufacturing and assembly functions.

- Distribution functions include loading, installing, transshipping, classification, storage and transportation.
- Business functions include trading of intermediate goods, import and export trade, exhibitions or sales.
- Exchange functions include international convention centers, such as international conference, tour, display and advertisement.

4.1.2. Typical Case: Free Trade Zone in Singapore

In 1819, Singapore was established as a free port, but it was abolished when it became independent in 1965. Instead, five regions were designated as Free Trade Zones and operated as part of the state's development efforts in 1969. After legislating the 'Free Trade Zone Act' in 1969, Singapore installed and operated Free Trade Zones in four harbor areas - Keppel, Pasir Panjang, Sembawang, and Jurong - and Changi airport.

The total area of the five FTZs are 4,810,000㎡, while the total area of the four harbors alone are 4,570,000㎡, accounting for 95% of the total area.

FTZs in Singapore do not apply tariff and VAT, and they are operated separately from areas subject to tariffs. A key feature of these FTZs is that loading, transportation, storage, display, sale, separation, repacking, distribution, classification and class investment are possible with minimum processing. Tariff is applied to goods from FTZs that are imported into Singapore. On the contrary, tariff is refunded for goods imported into FTZ because it is regarded as exports.

- Harbor: Port of Singapore Authority (PSA), private enterprise
- Jurong: Jurong Town Cooperation (JTC), affiliate of Commerce-Industry Ministry
- Airport: Civil Aviation Authority of Singapore (CAAS), affiliate of the Ministry of Transportation

Table 1-3 | State of Singapore's Free Trade Zones(as of 2005)

Classification	Name of region	Area (1,000㎡)	Major features
Harbor	Keppel FTZ	2,550	• Container dedicated terminal
	Pasir Panjang FTZ	840	• Container dedicated terminal • Kate lane : 12
	Jurong FTZ	615	• Conventional multi-purpose terminal (Construction freight)
	Sembawang Wharves FTZ	566	• Conventional multi-purpose terminal (Bulk and general freight) • Storage : 180,000㎡
Airport	Changi FTZ	240	• 6 airport terminal

The function of distribution and its value-adding processes are playing central roles in the Free Trade Zones in Singapore, however, manufacturing is also performing a considerable role.

Singapore established distribution-centered Free Trade Zones because of its favorable geography provided an advantage as a distribution hub, its history of having been established as a free port, and its limited manufacturing base. Singapore also lacks natural resources as a small nation-state, being slightly larger than Seoul. Nevertheless, Singapore's manufacturing industry also takes up a significant share, as there are about 50 international manufacturing companies located in the Free Trade Zones in Singapore.

4.2. Free Trade Zone Centered on Production

4.2.1. Concept and Features

Export Processing Zones could be classified as a typical Free Trade Zone centered on a Production Model. Export Processing Zones are free of tariff, established to promote the manufacturing industry and exports, creation of jobs, and transfer of technologies by attracting foreign investment based on benefits such as tariff exemptions, simplification of customs, and provision of streamlined administration.

One of the common features of Free Trade Zones is the provision of a variety of incentives to attract export-centered foreign investment in manufacturing. Several benefits can be provided including reduced corporate and income taxes, lower rentals, infrastructure equipment such as electricity and water, simplified customs for exports and imports, and streamlined permit approval process.

Because Free Trade Zones attract foreign investment in manufacturing aimed at promoting exports, the majority of the goods produced are shipped from the FEZ, located near major harbors, which are easily accessible and operated separately from other regions. Free Trade Zones has been used to promote foreign investment, exports, employment; additional objectives to develop the region, to acquire advanced management techniques and to strengthen the connections among the related regional enterprises can be found in the recent days.

By way of partial opening, developing countries use Free Trade Zones as an alternative to attract foreign investment in export industries[21]. As a Free Trade Zone offers a point of contact with the global market, developing countries can gradually promote liberalization in trade and investment. As developing countries advance, it promotes an open-door policy and general economic liberalization, which lessens the importance of Free Trade Zone. As typical cases, Masan and Iksan's Free Trade Zones in Korea and the Kaohsiung Free Trade Zone in Taiwan are evaluated as successful cases.

Mexico's Maquiladora, which lies along the US-Mexico border, could also be classified as a Free Trade Zone centered on the production model, though the way it was formed is different compared with Free Trade Zones in Taiwan and Korea, which were formed as industrial sites.

Production centered Free Trade Zones perform manufacturing and assembly, and labeling, (re)packaging, repairing, cleaning, mixing, quality test and modification of products.

4.2.2. Case 1: Export Processing Zone in Taiwan

To accelerate investment in manufacturing and to promote international trade, Taiwan legislated the 'Ordinance of Installation and Management of Export Processing Zone' in 1965, and subsequently, established Export Processing Zones (EPZ), which provide incentives to liberalize exports and imports, simplify procedures, and exempt import duties. Taiwan established and operates the Nandi EPZ and Kaohsiung & Zhongdao EPZ in Kaohsiung region, and the Taizhong Tanzi EPZ in Taizhong region, which are located at southern part of Taiwan.

Since 1997, Taiwan has been transforming the EPZs into Warehouse Trans-shipment Special Zones (WTZ) and developing new EPZs by amending relevant regulations.

Unlike an EPZ, which is centered on manufacturing, a WTZ operates like a Free Trade Zone, where the functions of distribution including circulation, storage, distribution, data processing and service industry are sharply reinforced. By establishing WTZs, Taiwan is capitalizing on its geographic location and creating a center of economic activity and

21. Amirahmadi and Wu(1995), p.890.

distribution in the Americas, Europe, and Southeast Asia.

The newly developed EPZs include: Chenggong Distribution complex, Kaohsiung S/W Scientific technique complex, Linguang EPZ, Xiaogang Airport distribution complex in Kaohsiung, and Zhonggang EPZ in Taizhong.

Taiwan's Free Trade Zones tend to shift from being Free Trade Zones centered on production to Free Trade Zones centered on production and distribution by establishing EPZs, which emphasizes manufacturing, and WTZs, which emphasizes distribution.

The role of the traditional EPZ, as a production base built by inducing foreign investment, has been lessened as Taiwan has developed economically. Furthermore, the role of EPZs has also been reduced as economic liberalization has accelerated, and the importance of using EPZs as a way to attract foreign investment has been decreased as well.

Table 1-4 | Export Processing Zones in Taiwan(as of 2005)

<table>
<tr><th></th><th>Region</th><th>Name of EPZs</th><th>Establishment year</th><th>Area (ha)</th><th>Number of Enterprises</th><th>Number of Employees</th></tr>
<tr><td rowspan="4">Existing</td><td rowspan="2">Kaohsiung</td><td>Kaohsiung (Zhongdao) EPZ</td><td>1966</td><td>72.4</td><td>88</td><td>16,293</td></tr>
<tr><td>Nandi EPZ</td><td>1968</td><td>97.8</td><td>94</td><td>37,646</td></tr>
<tr><td>Taizhong</td><td>Taizhong (Tanzi) EPZ</td><td>1968</td><td>26.2</td><td>49</td><td>11,017</td></tr>
<tr><td>Subtotal</td><td>3</td><td></td><td>196.4</td><td>231</td><td>64,956</td></tr>
<tr><td rowspan="8">New</td><td rowspan="4">Kaohsiung</td><td>Chenggong Distribution complex</td><td>1997</td><td>8.4</td><td></td><td></td></tr>
<tr><td>Xiaogang Airport distribution complex</td><td>1997</td><td>54.5</td><td></td><td></td></tr>
<tr><td>Linguang EPZ</td><td>1999</td><td>9</td><td></td><td></td></tr>
<tr><td>Kaohsiung S/W Scientific technique complex</td><td>2000</td><td>7.9</td><td></td><td></td></tr>
<tr><td>Taizhong</td><td>Zhonggang EPZ</td><td>1997</td><td>177</td><td>26</td><td>1,238</td></tr>
<tr><td>Bingdong</td><td>Bingdong EPZ</td><td>2000</td><td>123.5</td><td></td><td></td></tr>
<tr><td>Douliu</td><td>Douliu EPZ</td><td>-</td><td>270</td><td></td><td></td></tr>
<tr><td>Subtotal</td><td>7</td><td></td><td>650.3</td><td></td><td></td></tr>
<tr><td colspan="2">Total</td><td>10</td><td></td><td>846.7</td><td>257</td><td>66,194</td></tr>
</table>

Source: Export Processing Zone Administration, MOEA (www.epza.gov.tw)

4.2.3. Case 2: Export Processing Zone in China

In April 27th, 2000, ratified by China's State Council, 15 Export Processing Zones were established in China's national economic development zones. Later, two Export Processing Zones - Jinqiao in Shanghai and Zhongjing, Shichuan - were added. The Jinqiao EPZ has been the most productive among them. In 2002, 234 manufacturing related companies from the auto and electronics industries, including GM, Bell, Siemens, and NEC, established operations in the Jinqiao EPZ. Furthermore, 80 major projects with over ten million dollars of investment were also initiated.

The establishment of Export Processing Zones in China are restricted within economic development zones and their scale is limited to 2~3㎢[22]. China installed Export Processing Zones within economic development zones with the purpose of distinguishing Export Processing Zones from development zones. Total scale of the planned area for the 15 Export Processing Zones was 39㎢ while the designated area was 18㎢.

Table 1-5 | Operation Condition of China's Export Processing Zone (2002)

Name	Planned Area (㎢)	Designated Area (㎢)	Designated Period
Kunshan, Jiangsu Province	2.86	1.86	2000. 9. 6
Shanghai Songjiang	1.98	1.98	2000. 11. 8
Weihai, Shandong Province	2.6	1.34	2001. 1. 8
Yantai, Shandong Province	1.1	0.64	2001. 1. 9
Suzhou Industrial Park	2.9	0.44	2001. 1. 10
Guangzhou, Guangdong Province	3	0.9	2001. 3. 30
Shenzhen, Guangdong Province	3	3	2001. 3. 31
Dalian, Liaoning Province	2.95	1.5	2001. 5. 16
Hangzhou, Zhejiang Province	2.92	2.007	2001. 5. 18
Hunchun, Jilin Province	2.44	0.6	2001. 5. 31
Beijing Tianzhu	2.726	0.4	2001. 6. 12
Wuhan, Hubei Province	2.7	0.3	2001. 6. 20
Chengdu, Shichuan Province	3	0.6	2001. 6. 22
Tianjin	2.54	1	2001. 6. 29
Xiamen	2.244	1.4585	2002. 1. 23
Total of 15	38.96	18.0255	

Source: Internal data of China Customs

22. The Jinqiao EPZ takes the size of 19km^2 exceptionally.

The purpose of China's Export Processing Zone is mainly summarized into two. First, the EPZs sought to provide a favorable economic environment to induce FDI as a way to promote China's economic development. Second, the EPZs sought to simplify and streamline administration in line with international standard for potential companies.

As the Export Processing Zone is sanctioned by China's State Council and administrated by customs authorities, the companies that operate in the Export Processing Zone are classified as foreign companies and goods from the customs. The Export Processing Zone's board has total responsibility and authority over the administrative functions for inducing foreign funds and for approving imports and exports.

China's Export Processing Zones provide the following benefits and incentives to induce foreign investment.

- Tariff exemption and deferment
  - Tariff exemption on machinery installation, component, equipment and office supplies for building factories
  - Deferred Tariff: to defer tariff of related raw materials until exporting of final products
  - A tariff is imposed on daily living goods and employee vehicles
- Tariff refund
  - To refund tariff on imported raw materials, mainly architecture goods and office supplies are subject to tariff refund

4.3. Complex Free Trade Zone

4.3.1. Concept and Features

The above-mentioned Free Trade Zones are becoming more complicated with multiple functions working together.

The zones based on a logistical hub model are only involved in intermediate trade, including loading, transportation, storage, transfer and packing, at the beginning; but over time, the zones have tended to develop into complex FTZs involved in manufacturing, assembling, and marketing.

The Free Trade Zones centered on production have also tended to evolve into more complex ones taking on the functions of distribution and business, which seems logical, as economic liberalization and opening proceed with the goal of fostering a production base by inducing foreign direct investment.

The main functions of Complex Free Trade Zones are production, distribution, business and exchange. For complex FTZs, either production or distribution, can be the main function based on the history of the FTZs' development or initial intended purpose of establishment.

The Complex Free Trade Zones ensure free economic activities through liberalization and less regulation in various fields. The Complex Free Trade Zones provide the following benefits and incentives.

- Implement free trade through exemption on import duties
- Ensure open international financial activities through foreign exchange liberalization
- Minimize regulations on foreign investment
- Provide various incentives to induce foreign investment
- Provide strong support of international business activities by providing infrastructure including airport, harbor, distribution center, and business center

Free Trade Zones in the US, which are distribution-centered general zones but were allowed to develop production subzones together, could be considered representatives of complex FTZs. For China, zones developed at the beginning of the open door policy, including Shenzhen, concentrated on inviting foreign direct investment, however, the zones developed later, including Pudong in Shanghai, are more like Complex FTZs with the development of trade, financial and service fields.

4.3.2. Typical Case: Free Trade Zone in the US

Free Trade Zones operated in the US combine two functions: it designates and operates airports and harbors and the surrounding area as general regions, and it also designates and operates subzones in certain areas. The US enacted the 'Foreign Trade Zone Act' in 1934 to accelerate local business activities, promote foreign trade, create employment, and prevent domestic companies from going overseas. As such, the US began to establish Free Trade Zones.

At first, FTZs used to be utilized as intermediate trade and distribution centers for storage, examination, packing, and labeling; but their role and scope were greatly extended to include manufacturing and marketing when the law was amended in 1950.

Distribution activities such as storage, examination, packing, and circulation are permitted in every FTZ; however, production activities such as manufacturing and assembly are required to obtain the FTZ Board's approval. The organizations and the administrators of Free Trade Zones include the FTZ Board, grantee, operator, and user whose roles are arranged as follows.

- FTZ Board under the US Department of Commerce is in charge of the FTZ's approval.

- Grantee is usually a local government or a public institution that proposes the establishment and takes charge of a FTZ's approval, but it can also be a private enterprise.
- After the grantee has been established as the central organization in charge of the Free Trade Zone, it acts as the operator of the FTZ, which can also be a private enterprise.
- Domestic and foreign enterprises can both establish operations in the FTZ.

Free Trade Zones in the US are classified into general purpose zones and subzones. General purpose zones are complexes at a port, an airport or an inland area. It mainly focuses on distribution, such as temporary custody of bonded goods, storage, transferring, exhibiting as well as production. On the contrary, a subzone lies around a general zone and is mainly for production of manufacturing. Currently in 2005, there are 250 general purpose zones and 478 subzones designated as Free Trade Zones in the US.

Table 1-6 | Comparison between General Purpose Zone and Subzone in America(as of 2005)

Classification	General purpose zone	Subzone
Position	Neighboring area to an airport or a harbor (60 Miles or within 90 minutes by car)	No limitation. Manufacturing operation is a subzone
Usage	Distribution functions such as storage, preservation, circulation, etc. Partial assembly and production are possible	Functions of a factory such as production, manufacturer, etc.
Form	Establishing dock, building, etc. for feasible access of transfer modes	Production facilities of existing individual enterprises(formation of factory)
Method of moving in	Rent of storage facility is general	Designated main agent allows existing factory location as a subzone

5. Evolution of Free Export Zones

By the end of 1990, Korea's Free Export Zones faced various limitations. Indeed, problems began to emerge with the designation and management of the Free Export Zones due to the changes in Korea's economic and industrial structure. In response, adjustments were made to the zones and new policies were added by adopting policies aimed at promoting Free Trade Zone.

5.1. Drawbacks of Existing Free Export Zones

5.1.1. Regional Limitation

The limitations of Free Export Zones are as follows.

- The size of zones was limited by the lack of available land.
- Capabilities of Free Export Zones were limited due to the entrance of too many low value added domestic firms in zones.
- The integration of distribution and circulation functions is difficult due to the initial purpose which emphasizes on manufacturing factory.

5.1.2. Limitations due to Changes in Economic Structure

The main objective of a Free Export Zone is to combine together foreign investment and technology with low domestic wages for economic development. The model of export processing zones could no longer keep in line with Korea's economic growth by the end of 1990. In other words, due to wage increases, Korea could no longer compete with China and South-East Asian countries in terms of wages.

Hence, Korea needed to attract foreign investment to advance the industrial structure and expand international trade rather than attract foreign investment in simple production methods like assembly line.

In this regard, Korea initiated the concept of developed country-type free zones based on the general free port, the US foreign trade zone, and Japan's foreign access zone, which focuses on expansion of international trade rather than inducement of foreign investment.

5.2. Key Factors that Led to Change of Free Export Zones

5.2.1. Strengthening Free Export Zones

When the Free Export Zone system was introduced in 1970, it was an innovative way of attracting foreign investment considering the lack of other institutional mechanisms to achieve that purpose.

However, several policy actions were under way to attract foreign direct investment in the 1990's. Especially, new policies such as creating complexes only for foreign companies or foreign investment zones were under way to address the domestic problem of high land price.

Therefore, newly established Free Trade Zones were reformed to function more as import and export zones by attracting foreign direct investment. To this end, strengthening the promotion of international trade activities and Free Trade Zones resulted in attracting not only foreign but also domestic companies. It also resulted in regulatory reform and establishment of global standards.

5.2.2. Complex Functions

Korea's Free Export Zones are typical free zones centered on production. Other than manufacturing in Free Export Zones, businesses are allowed to have a warehouse and processes for transportation, shipping, and packaging; but these functions are limited to support the business activities within Free Export Zones.

Hence, Free Trade Zones function as an industrial complex but also as a logistical and commercial complex much like a city. In the case of the US, FTZs operate combining the two functions.

5.2.3. Improving the Management of FTZs

There have been criticisms of inefficiencies in the government's implementation of the policy to establish Free Trade Zones due to the complex functions. Such inefficiencies were a result of the government's method of purchasing and developing the zones, acquiring the land for zones, and building or leasing factories.

Therefore, the process and organizations for designating and managing FTZs were also diversified, letting not only the central government but also local governments and public organizations share responsibility in management.

5.3. The Current State of Free Trade Zones

5.3.1. Increased Designation of Free Trade Zones

After introducing the Free Trade Zone system based on complementary and improved functions of the Free Export Zone, the Korean government expanded and reorganized the existing Free Export Zone (Masan, for example) or restructured existing Free Trade Zones (Iksan and Gunsan, for example), through a simultaneous process to designate a few areas into new Free Trade Zones.

However, the establishment of new Free Trade Zones in Korea has not progressed well, over-running their completion deadline, as the sites of the new zones are located in relatively underdeveloped regions in effort to achieve the policy objective of balanced national development.

Therefore, the only Free Trade Zones based on the model of a Free Export Zone in Masan and Gunsan (moved from Iksan) are actually in operation currently.

Table 1-7 | State of Production-centered Free Trade Zones in Korea

	Masan	Iksan	Gunsan	Daebul	Donghae	Yulchon
Date of Designation	1970.1.1	1973.10.8	2000.10.6	2002.11.21	2005.12.12	2005.12.12
Area(1,000㎡)	954	310	1,256	1,156	248	343
Number of settling firms (Foreign Investment firms)	94 (51)	32 (6)	18 (8)	29 (24)	- -	- -
Export (US$100 Million)	51	1.4	0.8	4	-	-
Foreign Investment (US$1 Million)	144	5.3	44	38	-	-
Number of Employees	5,936	1,119	559	3245	-	-
Note	Additional development until 2014	Shifts to industrial complex in 2011			Planned to develop before 2009	Planned to develop before 2009

Source: Ministry of Knowledge Economy

5.3.2. Benefits Provided by Free Trade Zones

5.3.2.1. Low Rent

Companies that moves in the zone can benefit from much lower rent relative to nearby regions or standard factories if the investment is in high-technology or a new large foreign investment.

Among these, if the amount of new foreign investment is $10 million or more or 30% or more of the foreign investment share from new foreign investment of $1 million or more, 10 years starting from the date of settlement, rent is provided free of charge and this benefit can be re-extended for 50 years.

Moreover, among foreign investment firms investing $1 million or more, those investing $500,000 or more in high technology industry, industry supporting service business, or making a new foreign investment of $500,000 or more in machinery, automobile, or a related field of industry similar in terms of process will have 50% reduction in rent according to the regulations in Industrial Development Act Clause 1, Article 5.

5.3.2.2. Internal Tax Reduction

As foreign investment firms, high technology industry, industry supporting service business, or manufacturing business with foreign investment amount of $10 million or more, or distribution industry with foreign investment amount of $5 million or more can receive benefit of internal tax reduction applied to Free Export Zones in the past.

- Companies would be subject to reduced corporate and income taxes for five years. (100% for three years and 50% for two years)
- Companies are completely exempt from acquisition tax, registration tax, property tax, and composite income tax for 15 years.

5.3.2.3. Tariff Reduction

A Free Trade Zone is outside the tariff area, and therefore, it benefits from exemptions and refunds of tariff on foreign goods imported into the zone. Also, domestic goods brought in from other domestic regions also benefit from tariff exemption or refund, etc. Of course, such tariff reduction benefits are also given with regard to supplied goods, services provided, etc.

5.3.2.4. Administration Service

Administrative processes like Settlement License and Construction License, etc. can be handled collectively by the administrator, who is in charge of corporate activities in the Free Trade Zones.

5.4. The Future of Free Trade Zones in Korea

5.4.1. Impact of Foreign and Domestic Changes on Free Trade Zones

As we have examined in Section 2, the Korean economy has been able to achieve rapid growth based on an export-oriented growth strategy in the past 30 years, and there is no doubt that Free Export Zones (or Free Trade Zones) played a role in introducing foreign capital and advanced technology. In particular, the Masan Free Trade Zone focused on attracting foreign investment firms, and has been estimated to have contributed greatly to promoting exports, acquiring foreign currency, and introducing and spreading capital accumulation and advanced technology.

Moreover, even after Free Export Zones established in the 1970's were transformed based on a more development driven model of Free Trade Zones in the late 1990's, they have been assessed to have played a role in adding value by contributing to Korea's industrial development, going from labor-intensive light industries to technology-intensive electric and electronic industries.

However, Free Trade Zones had reached a limit due to changes in the external environment such as growing trend of FTAs and internal conditions. This in turn led to a shift in policy thinking.

First, international competition has intensified and capital mobility has increased with recent spread of FTAs such as Korea's FTA with the US and EU, while the comparative advantage of Korea's Free Trade Zones has come under increased pressure from competing nations.

Therefore, rather than simply attracting direct foreign investment, a more important policy task may be raising the industrial competitiveness of the region and nation by increasing the connectivity between foreign investment firms and domestic firms, introducing advanced technology, and spreading advanced management technique and know-how.

After the 2000's, the Korean government has promoted balanced national development as an important policy objective and has demonstrated its intention to use Free Trade Zones as a policy tool to achieve balanced national development.

Establishing Free Trade Zones seem to be in line with the national economic goal of attracting foreign investment, creating employment, increasing export, promoting trade and distribution, introducing advanced technology and management know-how, etc. In fact, FTZs are considered excellent means to promote the policy objectives of developing underdeveloped regions, as the zones bring industrial linkage effects to neighboring regions.

Therefore, in the current international environment where the opening of markets is accelerating with FTA promotion, the need to formulate policies on establishing and managing Free Trade Zones while taking into account domestic policy needs for balanced national development is rising.

5.4.2. The Future Direction of Free Trade Zones

5.4.2.1. Policy Tool for Improving Investment Environment and Promoting Deregulation

Regarding the promotion to attract foreign investments, the best policy would be improving the whole nation's investment environment so that foreign investors find the whole nation attractive for their investment. However, this would have to entail not only accelerating the liberalization of the whole economy but also groundbreaking deregulation measures to remove policy and system-wide obstacles to improve the domestic investment environment. As seen from experiences of the Korean FTA process, the opening of the whole economy is not easy, while promoting deregulation measures is difficult due to opposition from vested interests, social welfare, and so on.

In this regard, establishing Free Trade Zones should be considered as a second best policy to achieve specific policy objectives of attracting foreign investment, promoting international trade, creating employment, transferring technology, etc. without promoting the opening and deregulation of the whole economy tremendously. So, as seen in not only the Free Export Zones in Korea promoted up to this day but also export processing zones promoted in other countries, most Free Trade Zones are operated separately from other areas. Those special zones are able to expand infrastructure and provide incentives to improve the investment environment quite drastically. Furthermore, deregulation measures can be carried out within the zone since it is difficult to promote deregulation on a national scale. As such, FTZs are considered to be an effective tool to achieve the specific policy objectives of attracting foreign investment, etc.

5.4.2.2. Role Model for Improving National Investment Environment

In the long run, Free Trade Zones need to be used as models for improving the investment environment for the whole nation. In particular, Free Trade Zones can improve the investment environment in a specific area only in the short run, but after the incentive effects of attracting foreign investment wear off, the possibility to move to other appropriate investment area always lingers.

On the other hand, one of the concerns on the Free Trade Zones is that introducing and managing Free Trade Zones has a high possibility to neglect the necessity of nation-wide external opening, deregulation, etc. It can also delay improvement or structural reform in the overall corporate environment.

However, nations that have experienced success with Free Trade Zones, have used them as a policy tool to improve the business environment and to let the government provide incentives in industries which are partly insufficient or in need of supplement, achieving the policy objective of attracting foreign investments.

In the end, external opening measures, deregulation, etc. applied to Free Trade Zones can be used as external open door policy and deregulation measures of the whole country in the future and be carried out experimentally, and such measures need to be used as policy-wise signals that would mostly be applied in the future to the whole nation.

5.4.2.3. Creating International Comparative Advantage in Location

For Free Trade Zones that are separately managed from other areas (zone type), selecting the location of the zone is critical to achieve policy objective.

In fact, establishing Free Trade Zones entails policy considerations such as expanding infrastructure, establishing a managing agency, providing financial incentives, etc. in order to attract FDI, promote exports, and bring about transfer of technology. Therefore, to minimize the costs of establishing Free Trade Zones (and also in order to attract as much FDI as possible, the inherent objective of establishing Free Trade Zones), a region with a certain degree of industrial development should be considered.

From the standpoint of foreign investors, the critical factors would be that the zone's location has a geographical comparative advantage and favorable investment environment, because investment firms including multinational corporations move around the world looking for an attractive investment environment.

Moreover, even if the government provides an expanded infrastructure and financial incentives in a disadvantaged area, added value and forward and backward linkage effects of investment in this area would be low and technology transfer would be limited.

Therefore, in order for Korea's policy on Free Trade Zones to have their desired effect, designation and management of a zone competitive against not only other domestic regions but foreign Free Trade Zones in China, Taiwan, etc. as well is required.

The success of the Masan Free Trade Zone and relative failure of the Iksan Free Export Zone can demonstrate this.

The important reasons that Iksan failed was due to its lack of access to harbors, which caused excessive distribution costs in importing raw materials and exporting finished goods. Other factors include a lack of integration among related industries resulting in difficulty of securing domestic parts, lack of supporting infrastructure in surrounding area, and lack of capable labor force and related service.

5.4.2.4. Focusing More on Improving Investment Environment rather than Developing Underdeveloped Regions

Korea's Free Trade Zone policy has economic as well as policy objectives, but its economic objectives should have priority over the policy objectives, although striking a balance between the two is important as well.

As we have seen above, the future role of Free Trade Zones should be considered as complex as the policy objectives for achieving specific economic goals, regional development, economic reform, etc.

If policy objectives aimed at achieving economic goals, such as attracting FDI, creating employment, increasing export, acquiring foreign exchange, transferring technology, etc., should be more emphasized among these policy objectives, focus will be on improving the industrial environment in order to achieve these.

However, if this is seen as a means to achieve regional development, political and social consideration will be emphasized more than economic or technological ones. Underdeveloped regions make it a lot more difficult to attract FDI due to their weak infrastructure, shortage in manpower, low accessibility to markets, insufficient supporting industries, etc. Even if FDI is attracted, the forward and backward linkage effect is low so that it is highly possible that effects such as technology transfer are limited.

In Korea, the designation of the Gunsan Free Trade Zone in 2000 was done mostly in consideration of balanced development. Since then, Free Trade Zones were designated and managed with focus on regional development, but none of the cases have proved successful.

Therefore, although the policy objective of developing underdeveloped regions should be considered, the policy of establishing and managing Free Trade Zones should focus on improving the investment environment and increasing industrial competitiveness of the whole nation.

5.4.2.5. Strengthening Linkage with the Local Economy

Free Trade Zones in the past have shown a tendency to be cut off from the local economy by the reason of already benefiting tariff exemption. In reality, in order to minimize the side effects, when promoting Free Trade Zones at the experimental stage, policy of operating Free Trade Zones in exclusive form the cut off from the domestic economy was effective.

However, in order to maximize the benefits of Free Trade Zones, there must be a strategy to strengthen the linkage with local industries.

First, foreign investment firms in Free Trade Zones tend to transfer technologies to related supporting industries when they procure materials, parts, half-finished goods, etc. from local firms. Therefore, it is critical to strengthen the linkage between foreign companies in Free Trade Zones with local companies outside zones to spread advanced technology, management know-how, marketing channel, etc.

Workers who have worked foreign investment firms and move to domestic firms in Korea can facilitate the spread of knowledge, especially in high-value added or knowledge-intensive industries. For example, 3,000~4,000 of workers from the Masan Free Export Zone received professional training in Japan. Since they most likely moved to other firms in Korea, it can be easily supposed that they contributed to promoting related domestic industries.

Moreover, management methods of foreign investment firms in Free Trade Zones can play role-models for local firms. For example, Korean clothing factories in Bangladesh are known to have played such roles.

However, in regions with weak foundation in regional industries, this kind of backward linkage effect will hardly occur. That is, in these regions local firms are in general small in scale and do not have strong desire to export, thus, have no incentive to train employees. Also, local firms that lack technological capacity cannot meet the demands of foreign investment firms, resulting in no linkage effects. In the case of Masan, local firms were given systematic support for supplying materials and parts to foreign investment firms, and in 1985, local procurement ratio of foreign firms in Masan scored 32%.

Due to trade liberalization, international and inter-regional competition has intensified. For multinational corporations to be attracted to FTZs, strengthening linkages with the local and national economy is required more and more. That is, in order to compete with other nations increasingly vying for location advantage with Korea, such as China, demand of foreign investment to take advantage of Korea's industrial foundation (technology, labor force, related businesses, infrastructure, etc.) needs to be considered.

5.4.2.6. Response to Changes in External and Internal Environment such as FTA

In the 1970's, when Free Trade Zones were introduced, an effective means of achieving economic growth in Korea was establishing Free Trade Zones by combining cheap labor and land with foreign capital and technology.

However, in the current Korean economy, not only are labor and land far from cheap, but capital and technology are sufficiently accumulated. Therefore, Free Trade Zones need to pursue policy objectives different from past ones and to transform themselves.

Although the US, Taiwan, etc. keep their Free Trade Zone policy, policy objectives or management methods for each nation differ according to national situations.

Meanwhile, changes in the external environment such as trade liberalization, FTAs, as well as lower trade barriers are making Free Trade Zones less attractive. The benefits of tariff exemption, the biggest incentive in Free Trade Zones, are diminishing while the comparative advantage of geographical location is weakening.

With the conclusion of the Korea-US and Korea-EU FTA and possibly Korea-China and Korea-Japan FTA in the future, Korea will lower or lift tariffs altogether with most of its main trade partners, thus, decreasing the incentive for foreign investment firms to operate in a Free Trade Zone.

On the other hand, following the conclusion of FTAs, conditions of entry for foreign firms in Korea in general should improve with the strengthening protection system for foreign investment and benefits of other financial incentives. Moreover, FTAs with major trading partners can improve exporting environment and can work as an incentive for foreign firms to invest in Korea.

To bring about such effects, Free Trade Zones need to be established in regions that are advantageous to foreign investment.

6. Policy Lessons

6.1. Selecting Locations

In establishing Free Export Zones, the most important factor is how attractive a region can be made for foreign investment firms. Moreover, as attracting foreign manufacturing exporters to Free Trade Zones is the most important goal of this policy, how advantageous the region can be made for importing and exporting activities of foreign investment firms is an important factor.

Therefore, Free Export Zones should be located near the sea as much as possible. Of course, it could also be located inland near an international port, but as seen in Iksan's case, if the distribution cost of importing and exporting goods is too high, it would not be attractive to foreign investment firms aiming to cut costs.

Another important factor to consider when selecting the location is the accessibility to the labor force: a nearby urban region with a sufficient population to work in Free Export Zones is a must. It is important that they can easily commute and have an environment in which they can enjoy appropriate everyday and cultural lives after work.

Lastly, Free Export Zones must have the necessary infrastructure.

6.2. Preparation of Appropriate Incentive System

Most developing countries these days and some developed countries as well employ Free Trade Zones or free economic zones that are similar in form to Free Export Zones. Therefore, to attract foreign investment firms from all over the world, similar or higher level of incentives compared to other countries must be provided.

Tariff reduction on export and import goods is the basic incentive for establishment of Free Export Zones, and internal tax reduction related to production and export activities, and cheap land and factory rent are judged to be basic incentives to be provided.

6.3. Purpose-tailored Management System

Developing countries commonly aim to achieve balanced regional development while seeking to achieve other policy objectives. However, as Korea's experience has shown, it is difficult to realize policy objectives for balanced regional development and growing exports, attracting foreign investment, and so on, all at the same time.

Therefore, in the case of Free Export Zones, as the main purpose of their establishment is focused on the external businesses, they should be placed and made in favor of such purposes.

Even when establishing a management center to manage a Free Export Zone at the local and support settled foreign investment firms, department in charge of exportation and foreign investment must be at the center. Of course, in order to improve investment environment, local autonomous group's participation and support of other government departments and local autonomous groups in Free Export Zones will be necessary.

6.4. Selecting the Appropriate Model based on the Level of National Economic Development

In Korea, Free Export Zones were transformed into Free Trade Zones at an appropriate time based on the development of its economic and industrial structure, so that not only foreign investment firms but domestic firms could operate in these zones. Moreover, the conditions for investing in FTZs were established to provide an advantage to firms possessing high technology.

Therefore, developing countries planning to introduce a Free Export Zone system must choose either a production location-type Free Trade Zone model, aimed at labor-intensive manufacturing and assembly industry, thus, offering advantageous conditions to manufacturing and exporting activities or a complex Free Trade Zone model, aimed at attracting high technology and technology-intensive service industry based on the country's level of national economic development.

The forms of incentive provided by Free Trade Zones must change according to differences of these models as well.

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Chapter 02

Introduction to the Export-Import Bank of Korea: Implications on the Establishment and Operation of an Export Credit Agency

Chapter 02-1

Establishment of the Export-Import Bank of Korea

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<Summary>

In the late 1960s, the Korean government pursued export-oriented growth driven by light manufacturing sectors although the nation had a weak infrastructure in the heavy and chemical manufacturing industry. The structural limitations of such strategy became clear as the balance of payments deteriorated, foreign debts increased, and the number of corporate insolvencies rose. In order to achieve continued rapid economic growth, the Korean government aggressively pursued strategies to develop the heavy chemical manufacturing industry and industrialized exports.

As competition for contracts became fiercer in the global capital goods market, exports on a long-term deferred payment basis became more of a commonplace and each country competed by proposing favorable deferred payment conditions. Accordingly, Korea established the Export-Import Bank of Korea(Korea Eximbank) in 1976 as an official Export Credit Agency (ECA) for the purposes of comprehensively supporting the export of capital goods. Korea Eximbank assumed the duties of supplying facilities with medium-to-long-term deferred payment terms and greatly contributed to the successful execution of Korea's export-led growth strategy.

Financing support provided through Korea Eximbank played a large role and contributed significantly to the growth of Korea's export industry from one which was centered on mainly labor-intensive, light industry goods to one centered on capital goods such as ships and plants. When Korea achieved a positive current account balance in the late 1980s, Korea Eximbank assumed a more diversified role as well. Furthermore, as Korea's technology-based and high value added industries developed, Korea Eximbank expanded its role as a channel for

international economic cooperation and as a core bank for international trade to meet increasing demand for short-term export credit and support of high-technology industries.

As competition for contracts continue to intensify under the WTO regime, export credit has become an effective tool allowed by the international community for developing countries to achieve export-driven economic development. Export credit through Korea Eximbank has become a leading pillar of Korea's export industry, contributing to 64% of the ships exported and 15.7% of Korea's total export volume in 2009.

1. Establishment of the Export-Import Bank of Korea

1.1. Korea's Economic Development at the Time of Establishment

1.1.1. Economic Development Plans in the 1960s and Industrialization Process of Korea

Based on the policy goal to establish a self-sufficient industrial sector and promote exports, the Park Chung Hee administration developed and executed a series of 5-year economic development plans which set the foundation for South Korea's astounding economic development now referred to as the "Miracle on the Han River."

The first 5-year plan (1962-1966) was initiated in 1962 and aimed to transition Korea's aid-dependent and consumption driven economic structure to one driven by manufacturing in order to rectify socioeconomic problems and establish a foundation for self-reliance. In order to foster an industrial structure emphasizing manufacturing, all resources were dedicated to core industries such as electricity, fertilizers, oil refining, steel, and cement. During this period, Korea recorded average annual GDP growth rates of 7.8%, exceeding original targets of 7.1%, and the agriculture and fishing industry decreased its share in Korea's industrial structure from 37.0% to 34.8% while the manufacturing sector increased its influence from 14.4% to 18.6%.

The second 5-year economic development plan (1967-71) emphasized modernizing Korea's industrial structure and establishing a self-sufficient economy. The government worked to promote import-substitution industries such as steel, machinery, and chemical industries while developing labor-intensive light industries for production of export goods. From initiation of the second development plan in 1967 to 1973 when the government announced full-out plans for conversion to the heavy chemical industry, the Korean economy grew by 9.2% annually due to continuous inflows in investment and rapid increases in exports. The industrial structure also largely improved as the share of the manufacturing sector in the GNP grew from 19.1% in 1967 to 22.2% in 1972.

1.1.2. Initiation of Export-Oriented Development Plans and Establishment of an Export Support System

One of the goals of the 5-year economic development plans was to improve the industrial structure through industrialization while adopting an export-oriented strategy providing incentives to exporting companies. The government's export-led growth strategy was challenging given that exports comprised only 3% of Korea's GNP in 1962 and the fact that it was rare to find a developing country implementing export-oriented strategies for economic development as there was low awareness of the rapidly growing world trade.

During the initial stages of economic development in the early 1960s, the government emphasized import-substitution industries and construction of social overhead capital (SOC) to lay down the basis for development. However, after initiation of the second 5-year economic development plan in the mid-1960s, the government executed an aggressive export-oriented industrialization strategy to increase exports of labor-intensive light industries.

During the first 5-year economic development plan period (1962-66), Korea's exports grew from 55 million dollars in 1962 to 250 million dollars in 1966, increasing by an average of 44% annually. During 1967-69, exports grew by 36% annually, and the quality of export goods also improved. Among exported goods, the share of mineral products and agricultural and fishery products decreased while that of labor-intensive light industry goods and capital-intensive products increased.

The government prepared various systems to promote exports in accordance with the development strategy of achieving industrialization through expansion in exports. It also established the export support system by providing benefits in taxation and finance. In March 1962, the administration proclaimed the Export Promotion Law, which allowed preferential treatment to imports of raw materials used for export goods. It also gave special treatment to trade finance and strengthened economic diplomacy. In 1964, the government changed export promotion methods from direct support, such as export subsidies or restriction on imports, to indirect support, such as adopting a floating exchange rate system. In 1965, the Comprehensive Export Promotion Policy was initiated abolishing duties on imports of raw materials used for export goods and giving exporting companies business tax exemptions as well as 50% reductions in income taxes and corporate taxes.

In 1967, trade liberalization was expanded as the positive list system for Export-Import Notice was switched to a negative system. As a result, the demand for imports of raw materials and capital goods needed for export increased greatly while the government was forced to seek comprehensive import control measures and implement export promotion policies providing taxation and financial benefits.

1.2. The Necessity of Korea Eximbank Establishment

Beginning in the late 1960s, structural problems such as weakening balance of payments, increasing foreign debts, and growing corporate insolvencies were beginning to accumulate because the government pursued an export-oriented growth strategy focused on light industries without a sufficient foundation in the heavy chemical industry. In order to realize continued rapid growth, the Korean economy needed to develop the heavy chemical industry and industrialize exports.

From the initial stages, Korea's heavy chemical industry was developed with the aim of overcoming domestic market conditions and realizing an economy of scale. As the global capital goods market changed from a supplier's market to a buyer's market during the late 1950s and 1960s, competition for contracts became fiercer. As a result, exports on a long-term deferred payment basis became more common and countries competed to propose favorable payment deferral conditions.

The competition for export credits was mainly carried out by official Export Credit Agencies of developed countries as developed countries had already established and operated official Export Credit Agencies (ECA) with the goal to support exports of capital goods by supplying facilities on a mid- to long-term deferred payment basis.

Against this backdrop, there was much progress in regards to the establishment of the Export-Import Bank of Korea, Korea's official Export Credit Agency, after President Park Chung Hee ordered support for exports of heavy chemical products on a deferred payment basis at the first Export Promotion Expansion Meeting held in 1968. The government came to an agreement that the establishment of a financial institution wholly entrusted to supply mid- to long-term facilities on a deferred payment basis was needed. Efforts to develop concrete plans for the establishment of the Export-Import Bank of Korea were thus initiated.

After comparing and examining various measures, the government adopted a policy to establish the Export-Import Bank of Korea as an organization exclusively responsible for export credits, as most exporting countries already had such financial organizations to support exports of capital goods, and the area of export finance on a deferred payment basis was specialized.

1.3. Establishment Process and Enactment of Legislation

The Export-Import Bank of Korea Act, the foundation for the establishment of an exclusive institution for deferred payment finance, was passed in the Assembly plenary session on July 10, 1969, and was proclaimed as Act No. 2122 on July 28. On October 6, the enforcement ordinance of the Export-Import Bank of Korea Act was enacted and proclaimed as Presidential Decree No. 4009. The Act was able to be enacted in a relatively short period time due to the government's strong will for industrialization and active efforts to increase exports.

After the Export-Import Bank of Korea Act and its enforcement ordinance were enacted and proclaimed, the duties were handled by Korea Exchange Bank(KEB) in accord with Article 3 of the Annex to the Export-Import Bank of Korea Act. KEB had already created a new department for mid- to long-term credits to handle the workload. From the government, KEB received 100 million won as financial funds and started its duties on October 29th, 1969.

2. The Role of the Export-Import Bank of Korea

2.1. Economic Transition of Korea and Changes in the Role of Korea Eximbank

2.1.1. Korea Exchange Bank Period (1970 ~ 1975)

After enactment of the Export-Import Bank of Korea Act in 1969, the first loan was extended in 1971 to support overseas investment for the development of forestry resources in Indonesia. Afterwards, the Korean government announced the third 5-year economic development plan (1972-76) with policies focusing on promoting the heavy chemical industry. The government completed a master plan for the heavy chemical industry titled "Industrial Structure Reform" in 1972. The Ministry of Commerce prepared promotion plans for sub-industries such as promotion measures for the shipbuilding industry. In the "Declaration for Heavy Chemical Industrialization" released in 1973, the promotion of the heavy chemical industry was presented as one of the main policy goals.

When the first oil crisis occurred in 1973, the international trade environment deteriorated and economic activities slowed down. The necessity for changes in foreign economic policies became all too apparent. Because the Export-Import Bank of Korea Act could not accommodate all the changes, a revision of the Act was needed to supplement the functions of the Export-Import Bank of Korea and meet the various changes in internal and external conditions. As a result, the Export-Import Bank of Korea Act was revised and enacted as Act No. 2736 on December 26, 1974 and Presidential Decree No. 7561 on February 28, 1975.

In the revised Export-Import Bank of Korea Act, the major resources development fund was newly added to secure a stable supply of key resources and accelerate the development of overseas markets. Eligibility scopes for import credits, overseas investments, and overseas project credits were also expanded. In addition, the Economic Development Cooperation Fund (EDCF) and the Settlement Funds for Foreign Governments were established.

Furthermore, the repayment periods of Korea Eximbank's credits, including mid- to long-term deferred payment export financing, were extended from 6 months ~ 5 years to 6 months ~ 10 years and loan terms for the newly established main resources development fund and the Economic Development Cooperation Fund was set to 20 years.

Reflecting the expansion of Korea's Eximbank's role, the Bank's purposes for establishment were expanded from "promotion of foreign cooperation" to "sound development of the national economy and promotion of foreign economic cooperation." As a result, Korea Eximbank was charged with another tremendous mission to support Korea's heavy chemical industrialization and internationalization. Meanwhile, to expand Korea Eximbank's financing sources, the stated capital increased from 3 billion won to 15 billion won, and the scope of shareholders, which was previously restricted to the Korean government, was expanded to include financial institutions such as the Bank of Korea, Korea Development Bank, Korea Exchange Bank, and international financial organizations.

Domestic funding sources for loans were accordingly expanded and it became possible to raise funds from foreign financial institutions, international financial organizations, and foreign governments. In addition, it became possible to issue won-denominated export and import financial bonds in Korea's domestic market.

2.1.2. Establishment of the Export-Import Bank of Korea (1976)

Propelled by the government's aggressive efforts to foster the heavy chemical industry, exports of heavy chemical products increased remarkably during the third 5-year economic development plan (1972-76) period. With the completion of the Ulsan Dockyard, exports of transportation equipment, notably ships, increased greatly. Additionally, as the global shipbuilding industry was in depression with the first oil crisis and the reopening of the Suez Canal, demand for export financing of ships based on deferred payments increased substantially.

As exports of heavy chemical products on a deferred payment basis increased, the proxy system with KEB faced limits in supporting companies effectively and the need for an additional independent and dedicated institution increased.

In accord with the first revision of the Export-Import Bank of Korea Act, a temporary working committee was created and the "Export-Import Bank of Korea Deputy Regulations" was enacted in a meeting held February 20, 1975 in order to allow KEB to support the establishment of Korea Eximbank. By April 1976, an establishment committee was launched.

In June 1976, the committee resolved the budget and the articles of association needed for the establishment of Korea Eximbank, and then the Minister of Finance approved them. The government appointed In-Sang Song as the bank's first president, along with 2 directors and 1 auditor to comprise the board of executives. On June 17, 1976, the first capital for Korea Eximbank was paid. The Bank of Korea financed 2 billion won and KEB transferred 5,300 million won to Korea Eximbank on June 21, 1976. The funds from KEB had already been managed as funds for Korea Eximbank.

In accord with the Article 34 of the Korea Eximbank Act Enforcement Ordinance, the Minister of Finance designated July 1st, 1976 as Korea Eximbank's opening date, and Korea Eximbank was formally launched on that day. Although the Bank started with only 80 executives and staff members in 3 departments and 1 office, its establishment was monumental to the development of the Korean economy. Among the developing countries, Korea was the first to establish a dedicated institution for mid- to long-term deferred payment financing. As a result, Korea paved the way to growing from an economy dependent on foreign capital to one that actively exports capital goods, invests abroad, and expands foreign economic cooperation.

2.1.3. Promotion of the Heavy Chemical Industry and Establishment of Business Foundations of Korea Eximbank (1976 ~ 1985)

After Korea Eximbank was established in 1976, demand for export credits on a deferred payment basis and overseas investment credits increased rapidly. In addition, improvement of its decision making procedure was also required. As a result, the Korea Eximbank Act was revised for the second time in December 1977. Through this revision, the stated capital greatly increased from 150 billion won to 500 billion won and the board of directors, which had been dissolved with the establishment of the operating committee, was reorganized to enable swift decision making and responsible management.

After the second revision, the Bank prepared a support system for exports of capital goods and overseas investment and increased its scale of credits. Korea Eximbank also built a secure business foundation by increasing its fundraising activities in the international financial market. Export finance, which had been limited to Export Credits and Overseas Investment Funds, was expanded to Direct Loans and Interbank Export Credit, while Export Guarantees and Documentary Credit services were also greatly expanded. In 1977, Korea Eximbank made great strides in becoming a financial institution fully entrusted with export credits and began handling export insurance.

During this period, loans approved by Korea Eximbank increased rapidly from 187 million dollars in 1976 to 277 million dollars in 1977, 393 million dollars in 1980, 1.3 billion dollars in 1984, and 6.6 billion dollars in 1985.

With the active support of Korea Eximbank, Korea reached a turning point in the development of the heavy chemical industry as exports of ships and plants on deferred payment basis began in earnest. Also, Korea's overseas investments advanced from the establishment stage to the activation stage as investment on resource development such as lumber, oil fields, and soft coal increased from 1976 to the mid-1980s. Accordingly, the Bank's Overseas Investment Credit also greatly expanded. The Bank also responded to the increased demand for funds through successful overseas financing by selling deferred notes, obtaining bank loans, and issuing foreign currency denominated export and import financial bonds.

2.1.4. Switch to Surplus in Balance of International Payments and Diversification of Support Functions of Korea Eximbank (1986 ~ 1989)

In the late 1980s, Korea experienced an economic boom. Korea was able to achieve high rates of economic growth, switch to a surplus in the current account balance, and minimize inflation to single digits due to increased competitiveness of Korea's industries and because of low dollar values, oil prices, and interest rates. During this period, economic restructuring

Table 2-1 | Shifts in the Role of Korea Eximbank and Changes in Loan Execution

(Unit: billion Won, %)

Main Role	Year	Total Amount of Loans	Rate of Change
Promotion of the Heavy Chemical Industry and Establishment of the Business Foundation of Korea Eximbank	1976	53.4	-
	1977	96	44%
	1978	127.2	25%
	1979	158.6	20%
	1980	300.2	47%
	1981	524.1	43%
	1982	701.6	25%
	1983	719.5	2%
	1984	896.1	20%
	1985	860.5	-4%

Main Role	Year	Total Amount of Loans	Rate of Change
Switch to Surplus in Balance of International Payments and Diversification of Support Functions of Korea Eximbank	1986	607.4	-42%
	1987	496.6	-22%
	1988	530	6%
	1989	580.6	9%
Globalization of the Korean Economy and Establishment of a Support System for International Trade	1990	730.5	21%
	1991	1285.4	43%
	1992	1294.5	1%
	1993	2333.8	45%
	1994	3033.8	23%
	1995	4049.4	25%
	1996	4807.3	16%
Transformation to a Core Bank for International Trade	1997	7120.3	32%
	1998	6600.9	-8%
	1999	7726.7	15%
	2000	8095.7	5%
	2001	7336.7	-10%
	2002	8375.4	12%
	2003	9289.5	10%
	2004	11540.3	20%
	2005	15071.1	23%
	2006	16811.6	10%
	2007	19462.3	14%
	2008	25269	23%
	2009	32843.9	23%
	2010	38766.9	15%

Source: The Export-Import Bank of Korea.

including rationalization of industry, promotion of small and medium-sized enterprises, and financial liberalization was accelerated. Also, an open-door policy to ease trade conflicts was adopted and economic cooperation with developing countries was promoted.

As the government's economic restructuring and open market policy began in earnest, the Korea Eximbank Act was revised for the third time, and this revision diversified the Bank's business area and functions to include import financing systems and to manage the Economic Development Cooperation Fund (EDCF) while strengthening the overseas investments credit system. Also, the stated capital increased from 500 billion won to 1 trillion won.

The features of Korea Eximbank's business activities during this period included expansion of support for overseas investments. With the switch to a surplus in the balance of international payments in 1986, liberalization of overseas investments made rapid progress and demand from Korean enterprises for overseas investments increased sharply to overcome the deterioration of the domestic business environment (such as appreciation of Korean won and rise in labor costs). The government made progress in liberalization of overseas investments by adopting active measures such as industrial restructuring and developing of overseas markets. Accordingly, Korea Eximbank switched its criteria of support for overseas investments from a positive list system to a negative system, which allowed support to all areas except restricted areas. In particular, the Bank gave incentives in terms of interest rates, loan ratios, and financing processes to small and medium-sized enterprises suffering from financial difficulties. Consequently, this led to an increase in the share of Bank support for small and medium businesses to 41% in 1989.

Also, it became possible to directly support long-term funds to Korean companies' overseas subsidiaries so as to expand Korean companies' overseas investment projects while exempting them from withholding taxes on interest payments under the double tax avoidance agreement. Additionally, it became possible to establish subsidiaries domestically and abroad to carry out Korea Eximbank's work-related research and facilitate overseas financing.

Second, Korea Eximbank reformed the import credit system. With a surplus in the balance of international payments, the pressure to adopt an open-door policy increased. To meet the government's efforts to ease trade conflicts, manage the balance of international payments, and secure main resources needed for the national economy in the long-term, Korea Eximbank expanded eligible items for import credits and thus provide credits to imports of key commodities and main resources without classifying each item as exportable or domestic.

Third, Korea Eximbank started to manage the Economic Development Cooperation Fund (EDCF) entrusted by the Korean government in June 1987. So far, the Bank contributed to efficient management and administration of the Fund by building a solid foundation and expanding support to developing countries. Although Export Credit offered by the Bank and official development assistance through EDCF are different policy instruments, the two have similarities in that both have aims to facilitate economic development of developing countries by granting Korea's capital goods. Moreover, the information needed to handle the two is quite similar, so that the accumulated experience and expertise can be utilized by the Bank. Against this backdrop, the Bank was entrusted with EDCF.

2.1.5. Globalization of Korea' s Economy and Building the Support System for International Trade (1990 ~ 1996)

In the 1990s, when the economy encountered diverse and severe environmental changes both internally and externally, Korea faced a turning point in achieving the goal of joining the group of developed economies by the early 2000s. External environments changed rapidly with the free trade movement triggered from the Uruguay Round negotiations, limitless competition in the global market, the Eastern Bloc's transfer into the market-based economy after the collapse, establishment of diplomatic relationships and enhancement of economic cooperation between Korea and former communist countries, and intensified competition in the international market due to increased industrialization of least developed countries like China and ASEAN. Internally, while the heavy chemical industry increased its share of exports and production, Korea needed to develop more technology-based and high value-added industries to survive from the growing competition with least developed countries and to gain a competitive advantage over other advanced countries.

The features of Korea Eximbank's business during this period included expanded support for high-technology industries in line with government industrial policies. Support for ship exports decreased drastically with the fall in demand for deferred-paid export credit of vessels due to low interest rates in the global market. On the other hand, as exports of industrial equipment and high-technology products such as semiconductors and computers increased, Bank support for these industries grew significantly. In addition, Korea Eximbank's support for overseas investment also increased as investment by small and medium-sized enterprises expanded to reduce production costs.

Second, the role as a government window for economic development and cooperation increased. After establishing diplomatic relations in the early 1990s with former communist countries such as the Soviet Union, China, and Vietnam, Korea Eximbank played a pivotal role in enhancing economic cooperation with these countries by increasing financial support for businesses. In addition, the Bank was entrusted with the management of the Inter-Korean Cooperation Fund in March 1991 by the government due to the Bank's accumulated know-how of reviewing international projects and fund management expertise. Since then, the Bank has contributed greatly to revitalizing exchange and cooperation between the South and North Korea.

Third, short-term export credits expanded significantly. To cope with the change in economic structure and export goods, Korea Eximbank strived to provide balanced support to various industries by lessening dependency on ship exports while expanding support for exports of equipment and short-term export credits for the high-technology industry. As a result, the Bank initiated customized financial services designed according to short-term export transaction types for high-technology goods exports including semiconductors and computers.

2.1.6. Transformation to a Core Bank for International Trade (1997 ~ present)

The Korean economy slowed down after 1996 with the emergence of insolvent enterprises due to excessive and overlapping investments. In 1997, bankruptcies of major firms continued and the foreign exchange market became unstable. With the current account recording continued large-scale deficits and foreign capital inflows decreasing, foreign exchange reserves declined and the exchange rate rose. As a result, in October 1997, Korea’s sovereign credit ratings were downgraded by major credit rating agencies and a large amount of foreign capital left the country. This resulted in a national liquidity crisis. Eventually, with 10 billion dollars in stand-by loans from the International Monetary Fund (IMF) and eight advanced countries, Korea was able to avoid a national bankruptcy crisis.

The financial crisis brought radical changes to Korea’s economic structure and the Bank’s business environment. To overcome the crisis, the government took measures such as business restructuring, export market expansion, and reinforcement of export financing support by Korea Eximbank. These policies were praised as having improved the national economic structure and strengthening the Bank’s role as an important supporter for international trade.

In line with government policies, Korea Eximbank contributed to export market expansion for Korean enterprises as the Bank aggressively took on risks to finance export transactions with developing countries and focused on providing customized financial supports for international transactions. Moreover, the Bank introduced and operated Rediscount on Trade Bills in response to the failure of the private financial market so as to execute its own function as an official Export Credit Agency (ECA).

The features of Korea Eximbank’s business during this period included active assumption of risks related to international transactions. In other words, the Bank expanded financial support for exports to countries with low credit ratings, i.e., it actively supported guarantee transactions for importing countries, especially those with low credit ratings (such as D-). In addition to this, the Bank introduced a trade promotion program for developing countries. Specifically, the Bank initiated Forfeiting through which it purchased export bills based on export L/C issued by banks in developing countries on a without-recourse basis. The Bank also introduced L/C confirmation which guarantees L/Cs issued by banks in developing countries.

Second, Korea Eximbank expanded customized financial services to meet changes in international transactions. The Bank utilized mixed credit, which is an integration of the Economic Development Cooperation Fund and Export Finance, for a project. This helped ease the shortage of financial resources and facilitated exporting companies' efforts to win more contract orders. In addition, by financing domestic shipping agents to secure ocean-going vessels, the Bank resolved the reverse discrimination problem against domestic shipping companies. The Bank revitalized Guarantee of an Obligation services to meet various client demands and it covered interest rate risks resulting from banks' fixed-rate loans when it guaranteed credits on a long-term deferred payment.

Third, Korea Eximbank expanded loans on credit. Using its own credit rating system, it provided more loans and performance guarantee services on credit. Also, it introduced the Special Program of Short-term Export Loan for SMEs, which lack securities but are highly capable of carrying out export contracts.

Fourth, to make up for failures in the private sector, Korea Eximbank introduced systems to expand the amount of corporate loans and guarantee supports during a financial crisis and global recession when private financial institutions became passive in lending funds. In other words, the Bank carried out the supplementary function for the private financial market by providing foreign currency through Rediscount on trade bills for commercial banks, by handling special import credit using funds raised from IBRD and JBIC, and by expanding Performance Guarantees for overseas construction projects.

2.2. Main Tasks

2.2.1. Outline

During the last 30 years, Korea Eximbank expanded support volumes, strengthened existing services, and developed new services in accord with the development of Korean companies' overseas transactions in order to achieve its purpose for establishment, i.e. provide financing support needed for activities such as export, import, overseas investment, and development of natural resources for the sound development of the national economy and foreign economic cooperation.

Korea Eximbank credits are classified into four categories: 1) Export Finance which supports commodities (mainly capital goods) and services exports, 2) Overseas Investment Finance which supports Korean companies' overseas expansion, 3) Import Finance which supports stable and timely supply of essential materials and major natural resources, and 4) Natural Resources Development Credit which supports development of major resources for long-term stable supplies. In addition, the Bank deals with the following operations: 1) the Economic Development Cooperation Fund which supports developing countries' industrial growth and facilitates their business transactions with Korea, 2) foreign exchange tasks such as

Forfeiting and Factoring which became major tasks of the Bank since the revision of related laws, 3) Rediscounts and Guarantees which are provided to cooperating banks to ease loans, 4) Advance Payment Bonds needed to attain export contract, and 5) Performance Bonds to assure contract fulfillment. The following describes loan services, which are the Bank's essential functions as an official Export Credit Agency According to the nature of capital, loan services can be categorized into Export Loans (Short-term Export Loan and Inclusive Export Loan are included), Inter-Bank Loans, Technical Services Credit, Import Credit, and Overseas Investment Credit. Loan services can also be categorized roughly into Export Finance, Import Finance, and Overseas Investment Finance.

2.2.2. Export Finance

2.2.2.1. Export Loans and Technical Services Credit

Export Loans support exports of all commodities including capital goods such as industrial facilities, while Technical Services Credits support exports of services including technology. However, since their direct recipients are domestic suppliers (producer or exporter), these loans are categorized under Supplier's Credit. Hence, Technical Services Credit is operated under Export Loan conditions.

Export Loans, which comprise the largest share of Korea Eximbank's workload, provide short and long-term finance to domestic exporters of capital goods and foreign buyers who purchase Korean goods and services or technical services. To maximize effects with limited policy fund resources, the Bank grants loans under specific terms to transactions which satisfy certain conditions. These conditions include the following: first, goods and services must not be prohibited for export under applicable laws and international conventions and must fulfill minimum foreign-exchange earnings ratios, second, advance receipt by the Bank of a portion of the export transaction (except for short-term export loans and inclusive export loans), third, the loan period shall not exceed a set period and proper bond preservation should be made, and lastly, export transactions should follow set repayment and settlement procedures.

To support export transactions that meet these conditions, the Bank provides financial services such as Short-term Export Loans (a system that supports short-term export loans before and after shipment for sight payment transactions in which total export proceeds are paid until the delivery of export goods, and to export transactions with deferred payment terms of less than 2 years), Inclusive Export Loans (a system that previously granted inclusive loans needed for preparations for production and export of goods according to actual export records), and Unsecured Small Loans for Prospective Small Exporters (unsecured credit for entities with low credit rating but which perform high quality export transactions).

Technical Services Credit aims to facilitate overseas technical services (including overseas construction) which contribute to expansion and development of export markets, promotion of economic cooperation, and acquisition of foreign currency. In this context, technology implies the following: first, services, investigation, design, and supervision of technology for installation and operation of industrial facilities (including ships and vehicles), related raw materials, reserve stocks, and accessories; second, overseas construction work and service; third, other services which require financial support to develop and secure export market share and improve the trade balance.

2.2.2.2. Direct Loans and Interbank Export Loans

Direct Loans and Interbank Export Loans are classified as Buyers Credit as they are provided not to domestic suppliers but to foreign buyers (importers). However, they are very useful because they also support domestic entities' export of capital goods, as Export Finance does.

Direct Loans are beneficial for domestic suppliers, foreign buyers, and also for Korea Eximbank. Domestic suppliers can prevent deterioration of balance sheet caused by deferred payment, because export proceeds are paid by cash so that suppliers do not take collection risk of export bonds. Moreover, domestic suppliers can reduce labor costs because no further management is needed as transaction ends when goods are delivered.

Foreign buyers also benefit from Direct Loans as Direct Loans are considered public in most developing countries, so, according to agreement among nations and importing country' s tax system, buyers are exempt from withholding taxes on interest expenses. Moreover, accelerated depreciation of export goods is allowed for foreign buyers and they can take advantage of price negotiation since export proceeds are paid in one sum. Since Korea Eximbank, as the provider of the loan, makes contracts directly with buyers separately from the export contracts, the Bank can recover the entire bond.

As Direct Loans become activated, it developed into Project Finance. The main sources of repayments for Project Finance are cash flows generated from the operation of projects. Project Finance bases its bond preservation on operational profit of projects, while taking business-related assets as collateral. Project Finance increased in the late 1970s and early 1980s particularly in the oil resource development industry. Since the mid 1990s, it is also used as a way of obtaining finance in the private sector to build Social Overhead Capital (SOC) during the process of privatizing government enterprises in developing countries. Recently, it is used in various industries such as crude oil and gas development, oil refining, petrochemicals, manufacturing, and real estate development.

Interbank Export Loans provide lines of credit to creditworthy banks in foreign countries to help foreign buyers obtain credit (Relending) for the purchase of goods and services of Korean origin. Under specified credit lines, foreign banks facilitate import transactions of small capital goods and durable consumer goods such as small machineries, without incurring internal costs. Foreign buyers can import Korean goods by borrowing from their domestic banks with deferred payment terms. Korean exporters are able to not only sell their goods, but also collect the total value of the export contract.

2.2.3. Overseas Investment Finance

Korea Eximbank provides Overseas Investment Credits, Overseas Business Credits, and Overseas Project Credits. First, Overseas Investment Credits are provided to Korean companies that invest abroad in the form of capital subscription, acquisition of stocks, and long-term credit. Since its foundation, the Bank, as a bank established to support overseas investment, actively helped Korean companies expand overseas, especially for the development of natural resources and manufacturing. In particular, in the late 1980s, the Bank increased support due to greater demand for market preoccupation and development through overseas direct investment, and also because high costs resulting from higher wages, high land values, and interest rates led to increased overseas investment of small businesses.

Second, Overseas Business Credits are extended directly to foreign companies, in which a Korean company has an equity share, for the purpose of purchasing equipment and/or providing working capital. In this case, borrowers of Bank loans are foreign corporations. These credits support Korean companies incorporated abroad which need funds to extend their business in foreign markets, but face difficulty in obtaining funds. As a result, these overseas affiliated companies can reduce fundraising expenses and labor costs, timely obtain funds, and benefit from the exemption of interest income tax. Moreover, since companies incorporated abroad become borrowers, domestic companies can avoid increases in debt.

Third, Overseas Project Credits are provided to Koreans (including corporations) engaged in business outside of Korea. These credits are for entities which secure most of the materials required for installment, expansion, and operation of the equipment or facilities from foreign markets, and also for facilitating economic cooperation with foreign countries. Since these credits support foreign projects operated directly by Korean entities or overseas branches, borrowers are Korean entities. Overseas Project Credits are special in that their targets are not ordinary investment projects, but large scale projects which contribute to the national economy.

2.2.4. Import Financing

Import Credits provide funds for stable and timely supply of essential materials and major resources, and for overseas development of necessary mineral resources. Since raw materials and capital goods occupy about 90% of Korea's imports, timely and smooth supply affects national competitiveness. Moreover, to make leading export industries such as high technology or new growth industries more competitive, active provision of Import Credits is needed for political and strategic purposes.

2.2.5. Natural Resources Development Financing

Natural Resources Development Credits are provided to Korean companies or foreign companies conducting overseas investments for the development of natural resources which need long-term and stable procurement. Despite high risks, these credits are provided for national interest, so conditions including repayment differ from other credits. After 2004, the prices of mineral resources including oil are increasing rapidly, thus Korean companies dealing with resource development actively are entering into overseas oilfield or mine development. These developments are increasing demand for provision of Natural Resources Development Credits.

2.2.6. Foreign Exchange Deals, Guarantees, and Rediscount on Trade Bills

Since the revision of Korea Eximbank's law in 2002, Foreign Exchange deals became one of the main tasks of the Bank. The Bank handles Forfeiting, Export Factoring, Export Bill of Exchange, Notification and Confirmation of Export L/C, Refinancing related to Inter-bank Loans, import approval for Import Credits, Import L/C, and Import Letter of Guarantee (L/G).

Financial Guarantees for non-residents have been handled by the Bank since the amendment of Korea Eximbank's law in 2002. These Guarantees include guarantees of obligations provided to lending agencies to facilitate credit provision and Performance Bonds which assure execution of export contracts. Performance Bond is a representative example covering against market failure in Korea developed after the financial crisis in the late 1990s.

Korea Eximbank issued Performance Bonds to satisfy demands for counter guarantees on ordinary guarantees issued by commercial financial institutes, reduce additional financing costs of Korean enterprises, and enhance competitiveness of domestic businesses in export markets.

By implementing Rediscounting on trade bills occurring from export loans, Export Credits for R&D, and Import Loans of other financial institutions, Korea Eximbank indirectly supports loans by providing finance to related financial institutions. This task is also established to supplement financial markets by providing foreign currency through Rediscounting on trade bills of Korean banks, as the supply of foreign loans to export businesses fell sharply after the financial crisis in late 1997. In addition, Rediscounting is used as a tool to overcome limits of direct support of the Bank because the Bank has limited branches and a relatively small number of employees.

3. Evaluating the Role of the Export-Import Bank of Korea

3.1. Contribution to the Exports

3.1.1. Contribution to the Total Amount of Export Volume

Korea Eximbank's contribution to the total export volume in 2009 is 15.7%, an increase of 0.3% points from 2008. This is due to increased financial support of the Bank for export growth during the global credit crunch. Contributions to the total export volume can be derived by calculating the ratio of Bank support to Korea's total export volume.

Table 2-2 | Korea Eximbank's Contribution to Total Export Volume

(Units: million USD, %)

	2006	2007	2008	2009	Rate of Change
Total Amount of Export(A)	325,465	371,489	422,007	363,534	△ 13.9
Korea Eximbank's Support(B)	57,238	71,793	64,779	57,166	△ 11.8
Contribution to the Total Amount of Export(B/A)	17.6	19.3	15.4	15.7	0.3p

*Note: Rate of Change is the change occurred between 2008 and 2009.

In Table 1, Korea' s total export volume and Bank support decreased because of a sharp drop in trade volume after the global financial crisis.

3.1.2. Contribution to the Export of Ships

Korea Eximbank's contribution to the export of ships in 2009 was 64.0%, an increase of 16.2% points compared to 2008. Contribution to the Export of Ships can be derived by calculating the ratio of Bank support for export of ships to Korea's total export of ships.

In 2009, Korea's volume of ship exports and Bank support for ship exports decreased significantly due to the global financial crisis. The crisis led to a recession in the real economy and sharp reductions in ship orders. Compared to 2008, the total amount of ship exports decreased by 86.7% and Korea Eximbank's support also decreased by 82.2%. Nevertheless, the Bank's contribution to the export of ships greatly increased because Bank support relatively increased compared to the fall in support from European banks.

Table 2-3 | Korea Eximbank's Contribution to the Export of Ships

(Units: million USD, %)

	2006	2007	2008	2009	Rate of Change
Total Amount of Export(A)	46,320	70,600	55,740	7,388	△ 86.7
Korea Eximbank's Support(B)	35,945	38,342	26,643	4,730	△ 82.2
Contribution to the Total Amount of Export(B/A)	77.6	54.3	47.8	64.0	16.2p

*Note: A - Values provided by the Korea Shipbuilder's Association.
B - Ship export volume supported by Korea Eximbank's financial supports including loans and guarantees.
Rate of Change is the change occurred between 2008 and 2009.

3.1.3. Contribution to the Export of Industrial Facilities

Korea Eximbank's contribution to the export of industrial facilities can be derived by calculating the ratio of Bank support for the export of industrial facilities to Korea' s total export of industrial facilities.

Table 2-4 | Korea Eximbank's Contribution to the Export of Industrial Facilities

(Units: million USD, %)

	2006	2007	2008	2009	Rate of Change
Total Amount of Industrial Facilities Export(A)	25,404	42,162	46,270	46,304	0.1
Korea Eximbank's Support(B)	10,195	21,475	22,411	28,341	26.5
Contribution to the Export of Industrial Facilities (B/A)	40.1	50.9	48.4	61.2	12.8p

*Note: A - Data provided by the Korea Plant Industry Association.
B - The export volume of industrial facilities supported by Korea Eximbank's financial supports including loans and guarantees.
Rate of Change is the change occurred between 2008 and 2009.

In 2009, the export volume of industrial facilities changed little compared to that of 2008, while the Bank's support increased by 26.5%. As a result, the Bank's contribution to export of industrial facilities in 2009 was 61.2%, which was 12.8% point greater than in 2008. The increase in Korea Eximbank's contribution is mainly due to the government's export promotion policy mixed with a decrease in other financial institutions' support due to the global financial crisis.

3.2. Evaluation of Korea Eximbank's Role in Korea's Economy

3.2.1. Contributions of Export Financing

Korea Eximbank's Export Financing has positive effects on the national economy by enabling export transactions that could not occur without the aid of an official Export Credit Agency. Export Financing is used to cover both political risks and credit risks, but its main emphasis is on covering political risks.

Export transactions are very risky because of difficulties in collecting unsettled balances from foreign buyers who operate under a different system and culture in addition to buyers' default risk common in ordinary loans. Because of this, private sectors are reluctant to provide export credit. Market failure occurs due to the characteristics of export industries that are difficult to be solved by the private sector. Without the aid from an official Export Credit Agency, export transactions are difficult due to such financing problems. Therefore, Korea Eximbank's financial support supplements this market failure of the private sectors. By providing export loans to small businesses which have relatively low capacity for obtaining equity capital, the Bank's economic effect becomes greater.

Generally, to supplement the market failure, loans, guarantees, and insurance are provided through political means and Korea Eximbank deals with loans and guarantees. The Bank's main support targets are industries dealing with capital goods and high technology industries which have positive external effects on economic development but are unable to obtain sufficient financial support from commercial finance.

Moreover, the Bank's financial support contributes to economic development by protecting Korean companies and enhancing international competitiveness of exporters. Because Korea's rival export countries actively provide export loans for export promotion, Korean companies may lose competitiveness in global market. For this reason, developed countries try their best to understand the support of other countries' ECAs and to improve competitiveness of their own support services.

3.2.2. Contribution of Overseas Investment Financing

Similar to Export Financing, Overseas Investment Financing is a type of loan, but it is distinctive because it enables stable procurement of resources and overseas manufacturing bases. Stable procurement of resources has economic effects because it allows stable production of domestic and export goods, thus preventing price increases, recessions, and unemployment. As Korea is dependent on other countries for raw materials due to limited land and resources, securing resource supplies is essential.

In addition, for overseas resource development financing, private financial institutions and public enterprises specializing in specific resource development cannot provide enough funds when projects involve high risk, are too large in scale, or have extensive long-term business periods. Therefore, Korea Eximbank's Overseas Investment Financing supplements for such areas.

Overseas investment is desirable for foreign countries as well and has positive effects on economic cooperation among nations. By securing overseas manufacturing bases, production costs are reduced and price competitiveness is improved, hence resulting in export expansion, creation of employment, and increase in national income.

3.2.3. Contribution of Guarantees

Guarantees have economic benefits by facilitating trade by covering for risks that occur during borrowing and execution of export contracts. In case of guarantees, providers are exposed to risks as soon as they decide to provide a guarantee. Guarantees are unconditional support which means cancellation is impossible. As a result, the Bank supplements market failure using guarantees, by covering risks related to borrowing and execution of the export transaction.

Compared to other financial supports, guarantees are less speedy because borrowers need to enter into contracts with both Korea Eximbank and commercial institutions. However, guarantees have benefits such as inducing private sectors to participate in the export credit market.

3.2.4. Contribution of Government Entrusted Operations

Besides Export-Import Financing and Overseas Investment Financing, Korea Eximbank manages the Economic Development Cooperation Fund and Inter-Korean Cooperation Fund for further contributions to the economy.

3.2.4.1. Contributions of the Economic Development Cooperation Fund

As developing countries become more important globally, the Economic Development Cooperation Fund (EDCF) which was established for industrial development, economic stability, and promotion of exchange of developing countries, also becomes more significant. We can attain economic and non-economic effects through EDCF because it improves the national image, secures export markets and resources by fostering cooperative relationships with developing countries, directly increases exports, and reward the international society.

First, expansion of Official Development Assistance (ODA) through EDCF improves the image of Korea, and this improvement results in enhancement of Korean goods' competitiveness and popularity. Moreover, establishment of friendly relations through EDCF also induces development of new markets and expansion of export markets.

Korea received aid from developed countries' ODA after liberation from Japan, and Korea is considered the most successful case of development among aid recipients. Due to the aid received in the past, Korea was able to succeed and join the ranks of developed countries. In fact, Korea recently ranked 12th in terms of world trade. By helping developing countries with its experience, Korea hopes to fulfill moral responsibilities by serving as a responsible and caring partner.

3.2.4.2. Contributions of the Inter-Korean Cooperation Fund

As a divided nation, desirable changes in the relationship between North and South Korea have political and economic impacts by reducing unification costs and risks and by expanding markets. Economic cooperation between North and South Korea facilitates mutual economic development by filling the economic gap and homogenizing the economic system, hence reducing unification costs. In addition, achieving a peaceful atmosphere on the Korean peninsula greatly reduces uncertainty so that foreign investors can increase direct investments and economic agents of the two Koreas can enjoy increased benefits. Economic development of North Korea will stabilize and expand its markets and trade with the country will result in positive long-term effects benefiting South Korea's national interests.

4. Knowledge Sharing with Other Countries

4.1. Overview of Korea Eximbank's Knowledge Sharing Project

Since its establishment in 1976, to advance Bank operations and management, Korea Eximbank has benchmarked U.S. Eximbank (since trade volumes with the U.S. were the largest) and Japan Eximbank (since Japan shared a similar development path). In so doing, reports of Korea Eximbank's staff, who were trained by the above mentioned Eximbanks, and lectures given by staff or board of directors from these Banks served as a foundation for the development of Korea Eximbank. After 20 years of efforts to learn advanced ECA systems, Korea Eximbank's efforts paid off and was selected as the most successful Eximbank by UN Conference on Trade and Development (UNCTAD) in 1996 and introduced to 160 developing countries as a "model for ECA." Soon after, least developed countries rushed requests to learn of Korea' s remarkable development and Korea Eximbank's dynamic role in support of such development.

Ever since Korea Eximbank welcomed China Eximbank's founding members and shared knowledge on establishment processes and management know-how in the mid 1990s, the Bank continued to provide training programs to staff of China Eximbank. In addition, as Indonesia Eximbank requested consulting on export financing for small businesses, Korea Eximbank conducted special training programs and invited managers of small firms in Indonesia as trainees. Moreover, Asian countries including India, Thailand, and Taiwan requested advice for the establishment of their own Eximbank, implying that Korea Eximbank has become a benchmark for developing countries.

Korea Eximbank began to share knowledge in earnest on establishment and management of developing countries' ECAs when Korea's Ministry of Strategy and Finance initiated the Knowledge Sharing Project (KSP) in 2004. The Ministry emphasized support for Vietnam after receiving a request from the Treasury Department of Vietnam and entrusted Korea Eximbank with the duties of establishing and managing Vietnam's ECA. Korea Eximbank gladly accepted the request and has been successfully accomplishing the KSP in Vietnam. In 2008, the Dominican Republic also requested the KSP in order to establish its own ECA. Since then, many follow-up projects were initiated and are in progress.

4.2. Knowledge Sharing for the Establishment and Management of Vietnam's ECA

In 2004, working to reform Vietnam's systems for increased competitiveness in the global trade market and to gain membership into the WTO, the Vietnamese government decided to establish its own Eximbank for implementation of export-promotion policies approved under the WTO Regime. The Treasury Department of Vietnam searched for appropriate benchmarks for this task and decided to use Korea Eximbank as a role model. The Vietnamese government requested knowledge sharing on the establishment and management of an Eximbank in March 2005. Before the request from Vietnam, the Bank had only been providing general management know-how to the countries such as China and India which were growing rapidly. Financial expertise had not been shared with these countries. However, with the firmly established economic cooperation in terms of trade and investment between Korea and Vietnam, Korea accepted request of the Treasury Department of Vietnam. Korea Eximbank decided to share almost all necessary knowledge on financial products, financing, and risk management as well as knowledge on establishing a systematic infrastructure.

To perform the KSP more thoroughly, Korea Eximbank held prior consultations with staff of the Treasury Department of Vietnam in regards to the requested area and investigated general economic conditions such as the level of Vietnam's trade structure and the process of becoming a member of the WTO. The Bank also organized a Task Force (T/F) which consisted of staff from the Overseas Economic Research Institute, Credit Policy Department, and SME Support Department. After organizing the T/F, the Bank started to establish specific action plans to set up an Eximbank suited to Vietnam. Korea Eximbank provided policy consultations in regards to Vietnam's Export-aiding financial laws and enforcement ordinances for establishment and management of Vietnam Eximbank which were to be reported to the Prime Minister of Vietnam. In addition, the Bank supported the establishment of an information management system (such as a globalized risk management system) which is essential for operating an Eximbank, as well as establishment of rules and procedures covering general tasks including loans, guarantees, risk management, and financing. To transfer practical know-how which is not easily provided through documents, Korea Eximbank provided intensive training in March and November 2005 to Vietnamese government officials in charge of establishing the Eximbank. Experts from Korea Eximbank on loans, financing, personnel, and organization management, developed programs for Vietnam to share lessons about the function or role of ECAs and describe Korea's export supporting financial systems. They also shared knowledge accumulated over a 30-year period in regards to establishment and management of various rules and structures such as Korea Eximbank's export loans and founding laws.

In late 2005, the Treasury Department of Vietnam drafted and submitted the "Vietnam Export Credit Law" which reflected the experience and knowledge gained through policy consultations and in-service training from Korea Eximbank. On May 28, 2006, after the proclamation ceremony of the law, Vietnam Development Bank (VDB) was founded as Vietnam's ECA. After the foundation of Vietnam Development Bank, the Treasury Department of Vietnam further requested comprehensive consultations about management of VDB. In response, Korea Eximbank carried out intensive in-service training centered on financial tasks such as advanced techniques including project financing and risk management with staff from the Treasury Department of Vietnam and VDB.

On November 16, 2006, Korea Eximbank signed a comprehensive MOU with VDB regarding facilitation of cooperative loans, information exchange, sharing of work experience, and personal exchange. This resulted in changing the Korea Eximbank-VDB relations from the vertical mentor & mentee to a mutually beneficial parallel relationship in which businesses in both countries are supported interactively.

Meanwhile, the Treasury Department of Vietnam appreciated the foundation of VDB through the Knowledge Sharing Project as a desirable outcome of the Korea-Vietnam cooperation project, and requested additional support from the Ministry of Strategy and Finance of Korea. Consequently, an MOU between the two Ministries was signed to perform a KSP for the financial sector. According to the agreement, the Ministry of Strategy and Finance of Korea was to aid in the operation of VDB export loans and domestic development finance, and also help establishment of a credit guarantee fund for small businesses in Vietnam in order to support construction of a financial infrastructure in Vietnam. This cooperation project was implemented over a period of 3 years starting from 2007 and can be extended for an additional 2 years under agreement.

It took much time and collaboration for stable operation of a newly established organization in Vietnam, so government officials supervising Vietnam's ECA and staff members of the ECA were in dire need of knowledge sharing on the operation of the ECA. The Treasury Department of Vietnam and Vietnam Development Bank repeatedly requested that the Ministry of Strategy and Finance of Korea and Korea Eximbank provide comprehensive consultations on management of Vietnam's ECA. As the Ministry of Strategy and Finance of Korea signed a contract with the Treasury Department of Vietnam, it requested that Korea Eximbank execute the project so the Bank is actively supporting this project as a part of extending economic cooperation between the two countries.

〈Note〉 Proceedings of KSP with Vietnam on ECA

□ Year 2005
- Invitation training program for government officials heading the establishment of Vietnam's ECA
  - First program: 2005.5.9~16, attended by 8 members of the Treasury Department of Vietnam
  - Second program: 2005.11.14~20, attended by 11 members of the key ministries of Vietnam

□ Year 2006
- Establishment of Vietnam Development Bank as Vietnam's ECA on May 28, 2006
- Invitational training program for government officials officials charged with supervision and operation of Vietnam's ECA (in September)
- Dispatch of advisory groups consisting of loan experts (in November)

□ Year 2007
- Joint survey of Vietnam's export credit system (in September)
- Invitational training program for staff charged with supervision and operation of Vietnam's ECA (in October)
- On-the-Job training for middle managers concerning VDB's export credits (in November)

□ Year 2008
- On-the-Job training for staff concerning VDB's export credits (in July)
- Joint survery on Vietnam's export credit system and in-field education (in September)

- Invitational training program for government officials dealing with export credits (in November)
- 2008 Annual Review Meeting (ARM) (in December)

□ Year 2009
- In-field education about Vietnam's export credit system (in September)
- Seminar on financial system during KOREA WEEK in Vietnam (in October)
- Invitational training program for government officials dealing with export credits (in December)
- 2009 Annual Review Meeting (ARM) (in January 2011)

□ Year 2010
- In-field education about Vietnam's export credit system (in October)
- Invitational training program for government officials heading export credits (in November)
- Invitational training program for delegation of the Treasury Department of Vietnam (in May, December)
- 2010 Annual Review Meeting (ARM) (in January 2011)

4.3. Knowledge Sharing for the Establishment of Dominican Republic's ECA

In June 2006, when President Fernandez of the Dominican Republic visited Korea, he made an official request to Korea for consultations on economic policies. The Ministry of Strategy and Finance of Korea responded to this request by processing the export promotion and reinforcement project as the first KSP with Dominican Republic in 2008. Among topics of the project, Korea Eximbank was in charge of studying methods to facilitate export credits, and so the Bank investigated the current situation of export credits in the Dominican Republic and provided consultations on establishing an ECA.

The growth rate of exports in the Dominican Republic is the lowest among countries in Central America and the Caribbean. It was previously considered that external factors such as the US economy was the most influential factor to Dominical Republic's exports, but after analysis based on research of the actual conditions, it was pointed out that the lack of systemic export promotion policy, especially the absence of financial supports for exporters, hindered exports of the Dominical Republic. Moreover, an organization such as an ECA did not exist to exclusively help exporters while very little amount of financial support was provided by state-owned development banks and few commercial banks in the form of trade finance. Most of this finance was based on collateral, so the evaluation of export contracts and credit rating of exporters were not reflected in this finance. As a result, exporters could not obtain enough finance despite the high interest rate of over 20%.

Recognizing this, researchers of KSP proposed short and long-term policies for revitalizing export finance of the Dominican Republic. In the short-term, since there would be few tasks regarding long-term financing with the current level of heavy chemical industry and exporting firms, it was proposed that Dominica's National Housing Bank (Banco Nacional de la Vivienda; BNV) which is a government-operated development bank providing some trade finance, become fully responsible for export financing. To do this, the Dominican government was to expand its funding to secure capable workers, try its best to advance the financial supporting system by constructing a credit-rating system, and form a 30~50 million dollar scale of export credit so that the government could financially support export-related organizations and main industries or commodities selected. Funds for this operation was obtained by setting up credit lines with ECAs of main trade partners, by utilizing budget support from major donor countries' ODA, and by issuing bonds. If the BNV's export credits are successfully operated and concrete heavy chemical industry promotion strategies which require deferred financing are established, the Dominican government agreed to positively consider creating a Dominica Eximbank under the Korean model.

Korea Eximbank continues to support Dominican Republic's foundation of Eximbank, an invitational training seminar for staff dealing with the foundation, and plans to perform in-field education on Dominican Republic's export credit system and operation. Internal procedures are in progress for budget allocations and Korea Eximbank is actively working to establish Dominica Eximbank in early 2011 by organizing an establishment-propelling task force.

5. Implications

5.1. Considerations for the Establishment of an Eximbank

5.1.1. Utilizing Export Financing as an Export Promotion Policy under the WTO Regime

So far, most developing countries achieved successful economic development through export expansion, and Korea was not an exception. Before the WTO regime, there were many cases where some developing countries provided export subsidies to protect their domestic exporters. However, under the WTO regime, government subsidies such as export subsidies are prohibited. Therefore, for developing countries, export promotion policies can be implemented more directly and effectively through export financing. In the case of Vietnam, which was supported by Korea Eximbank, there was no export financing system except a short-term export loan funded by Vietnam' s Development Assistance Fund (DAF). However, since this system was prohibited by the WTO, it was abandoned when Vietnam joined the WTO. When Vietnam tries to introduce a new export supporting system, it should not violate WTO' s rules, especially the Agreement on Subsidies and Countervailing Measures (ASCM). Article 1 of ASCM defines financial contributions by a government or any public body as a subsidy if such contribution creates benefits. Considering this regulation concerning subsidies, the Vietnamese government carried forward establishing an official ECA to facilitate export.

5.1.2. Focusing on Trade Finance at an Early Stage

During early stages of economic development, developing countries do not have trade financing systems through appropriate commercial banks. In Vietnam, a trade L/C was widely used, but Pre-Shipment Loans were not actively used. Moreover, although state-run companies and their joint companies can easily obtain funds using their special relationship with state banks, individual enterprises face difficulties in securing financing through financial institutions. Therefore, it is necessary to introduce a trade financing system which can be used easily by all export businesses and to adopt an export insurance which allows exporters to cope with insolvency in transactions without L/C.

5.1.3. Raising Export Funds

It is not easy for developing countries to finance funds for establishing and expanding a government-run financial institution. The Dominican Republic, for example, is aiming to expand its industrial structure from clothing to medical, bio, and IT industries to increase exports. In addition to this, the country reinforced policy aid to its development bank to strengthen export finance. However, the current loan system, which pays margins to commercial banks based on clients' deposits, is not helpful for export businesses and guarantees or other loans operated under a collateral system also make little contribution to exporters' competitiveness because of high interest rates and their complex procedures. Accordingly, raising export funds which focus on key industries or commodities through government financial aid will effectively revitalize export finance.

5.2. Development Strategy of Eximbank

5.2.1. Introducing Diversified Trade Finance Instruments

As developing countries come out of the initial development stage, they face diverse demands for trade-related finance resulting from the increase in trade volumes. Since the export finance systems of Vietnam and the Dominican Republic concentrate on short-term export loans, they cannot meet the various financial demands of export businesses. Therefore, these countries need export financial products which do not limit the use of funds to specific export transactions, but which set extensive credit lines in consideration of past export records and future expected exports. Moreover, for recommended exporting goods which rely highly on imported raw materials, financial supports such as import finance are essential for stable supply of these raw materials.

5.2.2. Introducing the Credit Rating System

Most developing countries do not have a credit rating system because of their poor financial structure. Under their practice in which loans are mostly secured by collateral due to distrustful financial statements, it may take some time for the credit rating system to become established. However, it is desirable to introduce the quantity-based evaluation system which makes use of simple quality evaluation and estimates of financial statements as soon as possible. Introduction of the credit rating system is important in that it facilitates credit finance while moving away from current collateral-based loans. Once the system is established, credit lines can be set differently according to each firm' s credit rating: firms with higher ratings can use bank funds under more favorable conditions, and this induces export businesses to improve their financial structure in order to raise their rating.

5.2.3. Extending Credit Line and Offering Favorable Lending Conditions

Due to underdeveloped credit rating systems of developing countries' financial institutions, lending conditions (such as credit lines, terms and interests of loans) do not vary according to a firm's credit ratings. To expand exports, however, it is essential to provide more favorable lending conditions to promising export businesses with higher growth rates of exports, firms with better credit ratings, and exporters in industries which need government planned aid.

5.2.4. Obtaining Funds

When developing countries establish Eximbanks, government contributions are a major source for stable initial operation. However, it is necessary to consider other funding sources such as borrowing from domestic or foreign financial markets, signing loan contracts with major developed countries' ECAs, and issuing bonds.

1. Proposed Points for Vietnam Eximbank Establishment

1.1. Form of Eximbank

Although trade loans or insurance were provided in Vietnam, there was no long-term loan or insurance similar to what ECAs offer. Considering Vietnam's current economic conditions and development stage of its financial system, the time is not yet ripe for an Eximbank that mainly deals with long-term deferred finance as Korea Eximbank does. However, establishing an Eximbank will be beneficial for building a community of trade experts or an information center.

Since both banking and insurance are managed by the Treasury Department of Vietnam, separate operating system for export finance will be easy in modifying tasks as much as integrated system. Also, instead of using current measures such as Development Assistance Fund (DAF), having an independent Eximbank is desirable.

1.2. Types of Financial Services

1.2.1. Export Insurance and Guarantees

As an Export Credit Agency (ECA), the Eximbank provides export financing such as export insurance to support export businesses. In addition to credit guarantees, it offers project financing to aid Vietnamese enterprises to expand overseas.

1.2.2. Mid-to-long term Loans

In the short run, it seems that there would be little demand for mid-to-long term loans resulting from the export of industrial plants or machinery, but maintaining these loans will make future adjustment easier.

1.2.3. Short-term Trade Finance

As an official organization which is in charge of trade, the Eximbank provides short-term trade finance. It does this by offering trade loans and discounts on trade bills.

1.2.4. Rediscounts

Trade bills are rarely used in Vietnam. Introducing a system of trade bills and their rediscounts will provide more liquidity to new trade finance, and also contribute to facilitating the use of trade bills.

1.2.5. Supporting Working Capital for Small Businesses

As a policy organization, the Eximbank needs to maintain a special loan program for small businesses.

1.2.6. Other Services

To support export firms, the Eximbank aids firm participation in overseas exhibitions and market surveys. Moreover, the Bank needs to reinforce research on trade and provide related information.

1.3. Structure of the Eximbank

As a newly established organization, the Eximbank needs an Operations Committee, Board of Directors, and Executing Departments. Executing Departments consist of the Planning and Administration Group (including Human Resources and General Affairs Department), the Export Credit Group (which provides export insurance, long-term loans, and short-term trade finance), Country Research & Risk Evaluation Office, Risk Management Department, Treasury Department, Legal Office, and Auditing Department.

1.4. Risk Management

The financial market of Vietnam was estimated to have a very low level of risk management, so it was proposed to improve project evaluating capabilities by hiring experts, and to evaluate and diversify various risks. To do this, the whole organization needs to be aware of the importance of managing risk, and possess an appropriate risk management system. For more efficient risk management, independence in the managing process should be secured, while making clear the endurance level and responsibility or authority of related organizations. Constructing the infrastructure of risk management is also needed. Moreover, a rational credit limit management system is the most basic and essential part of risk management.

2. Proposed Points at time of Dominica's Eximbank Establishment

2.1. Form of the Eximbank

If Dominican Republic's export fund, managed by BNV, is successfully operated, then the government needs to consider extending the fund to establish its own Eximbank which is actually the ECA of the Dominican Republic. For other less developed countries, export finance was mostly short-term loans and direct export loans. Because of this, developing countries without an ECA decrease competitiveness of domestic businesses.

2.2. Types of Financial Services

2.2.1. Export Insurance and Guarantees

At present, 70% of Dominica's exports are directed to the US, so the importance of country risk and credit risk is low. However, as Dominica's exports expand into Central and South America and the Caribbean, demand for export insurance will grow.

2.2.2. Long-term Loans

Although the Dominican Republic establishes its own Eximbank, the Bank will provide mainly short-term export finance. However, if the country grows into a mecca for IT, clothing, and the bio industry, then demand for long-term loans will grow. Hence, investigating and analyzing operations for long-term loans provided by ECAs of developed countries will be necessary.

2.3. Structure of the Eximbank

As the role of BNV becomes more important and the introduction of a credit rating system is visualized, the Bank will need a risk management department and market research & risk evaluation office to investigate main export markets. In addition, the Bank should operate overseas branches to expand provision of various loans and research of overseas markets.

Chapter 02-2

Establishment of Korea Trade Insurance Corporation (K-sure)[1]

Pil-Joon Kim(Korea Trade Insurance Corporation)

<Summary>

Because of the long-term economic plans for the bold export-oriented growth strategy, exports increasingly were transacted via non-credit based payment methods such as D/A and T/T while Korea diversified into high-risk emerging markets. This inevitably led to an increased risk of export loans being uncollectable.

To mitigate this risk, Korea introduced and implemented a formal export insurance scheme early in 1969, which continues to provide an excellent platform for expanding exports after some 40 years. Initially run by Korea Reinsurance Corporation, and then the Export-Import Bank of Korea, Korea Export Insurance Corporation (KEIC) was established in 1992 for the specific purpose of operating this scheme, which subsequently assumed the new name, Korea Trade Insurance Corporation (K-sure) in July 2010 to better meet the demands of exporters.

The establishment of KEIC as the primary governmental organization responsible for export insurance in the early 1990s coincided with rapid changes in regulations related with international trade such as the creation of the WTO and the growing trend towards financial globalization and liberalization. While such changes served to indirectly promote exports, they also helped to draw much attention to export insurance, which provides financial support in a market-friendly way.

1. Korea Export Insurance Corporation assumed its new name, Korea Trade Insurance Corporation on July 7, 2010.

Export insurance helps domestic exporters to aggressively pursue their business by removing much of the uncertainty surrounding export transactions. Additionally, it supports financial intermediaries to increase export financing offered to both exporters and importers and concentrate their support to promising industries. In other words, it can be a powerful industry-promotion policy tool.

For example, export insurance was successfully mobilized to foster strong small and medium enterprises (SMEs) by providing SMEs with various preferential treatments and to increase trade with eastern European countries in the 1990s. Moreover, it was utilized as an effective policy tool to promote the heavy industry such as engineering, procurement and construction (EPC), chemical and shipbuilding when Korea shifted its focus to the secondary sector of the economy from the light industry.

In particular, export insurance played a pivotal role in bringing about economic recovery in the wake of the 1997 Asian financial crisis and the 2008 global financial crisis by urgently providing much needed liquidity to SMEs and by increasing opportunities for exporters to enter the global market.

1. Background on the Foundation of Korea Trade Insurance Corporation

1.1. Background

1.1.1. Drive to Increase Exports to High-risk Markets

At the start of economic development, Korea had to take a two-pronged approach to continue its expansion of exports to cope with fierce global competition brought on by the emergence of developing countries. First, the country needed to pursue bold export promotion by diversifying export payment methods, i.e., focusing on safe L/C based payments while utilizing D/A and D/P contracts on a deferred payment basis. Second, it needed to tap into diverse export markets including developing and non-hostile socialist countries despite the high political risks they posed.

At the time, Korea sought to increase exports to not only major export markets including the U.S. and Europe but also the Middle East, former communist countries, and Latin America. Furthermore, entry was made into major construction markets including Iran, Iraq, Libya, etc., by diverting its energy from Saudi Arabia under full diplomatic support of the Korean government.

Unavoidably, this bold export promotion policy brought an increased risk of non-payment of export proceeds. This risk increased as Korea focused on more heavy, chemical, and EPC (engineering, procurement and construction) industries and less light industry exports. Expensive and high quantities of heavy and chemical products requiring longer settlement periods replaced inexpensive and low quantities of light industry products requiring shorter settlement periods. Consequently, insurance claims meant higher payouts, much more due to higher political risks as more importers were in developing countries.

Table 2-5 | Changing Landscape of Korea's Industrial Base

(Unit: %)

	Agriculture	Textile	Wood/ Paper	Chemical	Metal	Machinery	Other (Electronics, etc)
1960's	15.7	35.4	13.4	12.1	8.6	12.5	2.3
1970's	13.6	31.1	11.0	11.8	9.5	17.4	5.6
1980's	9.0	30.9	7.8	13.2	9.2	26.5	3.4
1990's	7.1	22.1	7.4	14.4	8.3	37.7	3.0
1998's	7.5	16.6	5.5	11.6	3.6	46.6	8.6

Source: National Statistical Office Year Book.

Furthermore, a shift in export markets toward developing countries in Latin America and Africa meant increased commercial risk as well because L/Cs would come from domestic financial institutions in these regions since global banks would be hesitant to deal with these countries because of their low foreign reserves and poor credit ratings. In other words, Korea had to deal with an increased risk of larger losses, and therefore, it had to urgently provide policy support at the government level to minimize the uncertainty faced by exporters and financial institutions. Thus, the role and functions of export insurance became more important as a system to support the Korean government's export promotion policy.

1.1.2. Changes in the International Trade Environment

The severely distorted global economy marked by deepening imbalances in the early 1990's saw conflicts arising in every corner of the world as each region claimed economic autonomy. The underlying causes included the globalization of economic activities and markets, structural changes in industry driven by fast technical innovations, the mounting US trade deficit and national debt pressing the world, etc. Nonetheless, a consensus had been reached that the world should maintain international economic order based on free trade while avoiding extreme trade conflicts because each country has become deeply interdependent with one another.

Amid this confusion, negotiations began in the Uruguay Round, which once concluded, brought about a new order of free trade through the strengthening of standards in a wide range of areas such as banning tax/financial regulations as tools of protectionism. In other words, stronger international regulations meant that Korea urgently had to find ways for indirectly supporting exporters, while gradually phasing out direct support including public financing and tax benefits.

The Agreement on Subsidies and Countervailing Measures under Item 1-1 of Article 1 states that “a subsidy is deemed to exist if there is a financial contribution by a government or a public body”. Item (j) under Annex I (Illustrative list of export subsidies) specifies that “the provision by governments (or special institutions controlled by governments) of export credit guarantee or insurance programs, of insurance or guarantee programs against increases in the cost of exported products or of exchange risk programs, at premium rates which are inadequate to cover the long-term operating costs and losses of the programs” are prohibited subsidies.

Export insurance that sought to maintain long-term account balance would not be considered as a subsidy, whether it is run by the government, an independent government agency or a private company. Thus, export insurance is the only policy tool permitted to promote exports under the WTO system.

Unlike export finance, which could be viewed as a direct form of government subsidy by other countries, export insurance maximizes the effect of the government’s export promotion policy. Externally, it can be used to avoid trade conflicts with other nations while indirectly supporting the government’s effort. Domestically, it minimizes the drawbacks of providing direct financing via export finance such as unfair distribution of financial resources and higher prices, while supplementing export finance with limited financial resources.

Thus, the Korean government actively sought to introduce an export insurance scheme that could support its export promotion policy.

1.2. Introduction of Trade Insurance - Purpose

Trade insurance was introduced for the first time in Korea in 1969 with the purpose of expanding exports, thereby contributing to the national economy. The introduction of this trade insurance scheme and the purpose behind the establishment of the agency that was in charge of this scheme have continued to remain the same despite several amendments to the Export Insurance Act, the legal basis of the scheme. And this fact reflects the government’s initial industrial development strategy of pursing economic development through export expansion.

However, the term “export expansion” can bring about trade conflicts with other nations. There has been a growing support to foreign direct investments of Korean companies as they expand their international operations and set up overseas subsidiaries. And the linkage between exports and imports has become tighter over the years. Thus, the existing trade insurance scheme had to be changed with measures such as the introduction of import insurance. Consequently, the mandate of the agency in charge of the scheme also had to be changed.

Therefore, the purpose of the agency was defined to cover a wider scope when the “Export Insurance Act” was amended to the “Trade Insurance Act” in 2010. As such, the mandate of K-sure is now “to effectively operate the trade insurance scheme for the goal of promoting trade and overseas investment, thereby strengthening national competitiveness and contributing to the national economy of Korea”.

2. Introduction of Korea Trade Insurance Corporation (K-sure)

2.1. K-sure as an Institution

2.1.1. K-sure as an Institution and Statute

Korea Export Insurance Corporation (KEIC), the predecessor of K-sure, was established in July 1992 as a non-capital special legal entity. Although the agency was the main entity that conducted all trade insurance-related business activities including the management and operation of the Export Fund that was already established, it was a “special entity” because it did not have separate funds of its own.

KEIC was considered unique because 1) the management and operation of the Trade Insurance Fund (the former Export Insurance Fund) were commissioned to various agencies (Korea Reinsurance Corporation, the Export-Import Bank of Korea) from the beginning and 2) historically Korea used to establish agencies that had the same legal basis as other institutions such as the Korea Credit Guarantee Fund and Korea Technology Finance Corporation.

This legal entity format enables a stable operation of trade insurance but has in some drawbacks. The agency needs to submit and obtain approval from the Administration and the National Assembly each year and has to manage the Fund accordingly. This makes a flexible management of the trade insurance scheme impossible because of the procedural matters involved when modifying annual plans under special circumstances.

2.1.2. K-sure's Organization and Personnel

At the time of its founding, KEIC was set up with five departments, after which new departments branched off from the existing ones. The initial five departments included the 1) business department responsible for marketing and underwriting, 2) claims and recovery department responsible for the evaluation of claims, calculation of insurance payouts, and handling of bonds, 3) credit risk department in charge of the evaluation of buyer and country credit risk, 4) planning department with three business teams, and 5) administration department with two support teams.

Although the agency has expanded its size and organization, totaling 22 teams at the end of 2010, it continues to operate under the same organizational structure of five department scheme. The current five departments include the 1) business development in charge of handling customer relations, marketing, etc, 2) trade promotion responsible for short-term underwriting, 3) structured finance in charge of handling medium and long-term underwriting, 4) claims and recovery in charge of handling claims and receivables, and 5) strategic management responsible for providing management support including planning and handling of general affairs. The number of employees jumped from 169 at the time of KEIC's establishment to 430 at the end of 2010.

2.1.3. K-sure's Asset Composition

K-sure has four sources of income for the operation of the trade insurance scheme: 1) premiums collected from its customers, 2) recoveries collected from defaulted receivables, 3) returns on the investment of the Trade Insurance Fund, and 4) contributions from the government for the purpose of expanding the Fund. The major portion of K-sure's income comes from premiums and recoveries collected from defaulted receivables, which amounted to KRW 621.8 billion as of 2010.

Nonetheless, Article 36 of the Trade Insurance Act (Disposition of Gain and Loss) stipulates that any profits obtained after settlement of the Fund shall be reserved in full; any losses incurred after settlement of the Fund shall be indemnified using the reserve amount, and when such reserve amount is insufficient to cover the losses, the government shall be ultimately responsible for the settlement of the remainder of such losses. In other words, the Trade Insurance Act provides the basis for K-sure to have the same credit rating as the Korean government.

2.2. Major Functions and Roles of K-sure

2.2.1. Roles of K-sure

2.2.1.1. A Safety Net for Export Transactions

One of the major functions of export insurance is to create an environment conducive to export trade, in which export insurance would hedge the export-related risks of exporters by facilitating export transactions for exporters as if they were domestic transactions.

In other words, it indemnifies exporters and financial institutions from losses arising from the political and commercial risks associated with the promotion of export activities, which in turn would increase investment and employment to boost the real economy.

2.2.1.2. Support toward Securing Financing

Export insurance helps exporters secure export finance from financial institutions through non-payment guarantees, at the same time it facilitates export finance from financial institutions to exporters while easing the collateral provision clause. In other words, a virtuous cycle of developing the domestic financial industry can be achieved where more credit can be available with private funds introduced to export finance.

2.2.1.3. Policy Tool for Export Promotion

Trade insurance makes it possible to set insurance premiums as low as possible as long as a long-term balance is achieved for the agency since the system is operated under government support. On the other hand, insured exporters can obtain maximum coverage. In other words, it can be an effective policy to promote exports and strengthen the export competitiveness of a nation.

Thus, the role of trade insurance, which is the only policy support allowed under the international financial regulatory system, is bound to become more important as countries around the world are competing to provide better export support and face tougher regulations on providing direct support such as export finance and tax benefits.

2.2.1.4. Credit Evaluation of Importers and Importing Countries

Trade insurance needs active research on foreign importers/buyers and importing countries taking into account their political and economic conditions from various aspects to effectively underwrite and manage export insurance and to prevent claims beforehand. This credit information on buyers and importing countries leads to constructive export transactions for exporters when seeking new buyers and increasing export volumes.

2.3. K-sure Programs Supporting Trade

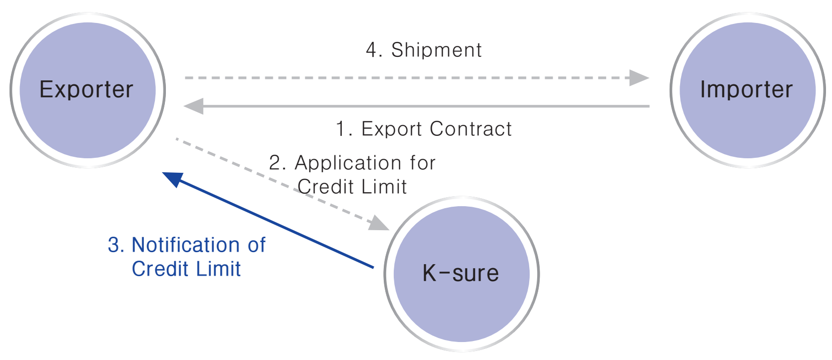
2.3.1. Programs Supporting Short-term Transactions including Consumption Goods Exports

K-sure offers Short-Term Export Insurance, Cultural Export Insurance, Agro-Fisheries Export Insurance, Overseas Marketing Insurance and Reliability Insurance to protect clients from the political and commercial risks associated with short-term transactions (those transactions where the credit period between shipment and settlement is less than 2 years).

Protecting the short-term products of K-sure, Short-Term Export Insurance is extended to those transactions less than two years to insure the policyholders from losses arising from defaults on export receivables after shipment. This product covers the political risks (such as restrictions on foreign exchange transactions by the importing country, the event of war in the importing country, etc.) and commercials risks (such as the importer's refusal or inability to accept the imported goods, refusal of payment, etc).

The following diagram is a schematic illustration of how Short-Term Export Insurance works. Once an importer and an exporter concludes an export transaction based on credit, K-sure sets a credit limit and informs the exporter of the limit. Then, the exporter ships the export goods on the contract and at the same time, pays an insurance premium to K-sure. When the

Figure 2-1 | How Short-term Export Insurance Works



exporter cannot collect the export receivables by the settlement date on the contract, K-sure pays out the insurance proceeds to the exporter and collects the amount from the importer. This product protects exporters from the risk of non-payment of export proceeds and enables active global market penetration.

Cultural Export Insurance protects the policyholders from losses arising from investments or loans made for the production of movies, games, dramas, performances, etc. where their export contracts have been concluded or they are to be exported. Agro-Fisheries Export Insurance covers exporters from the political and commercial risks related to export transactions of agricultural and fishery goods.

Overseas Marketing Insurance indemnifies losses related with overseas marketing activities by Korean exporters. Reliability Insurance covers losses resulting from defective parts/materials exported by Korean exporters.

2.3.2. Programs Supporting Medium and Long-term Transactions including Capital Goods Exports

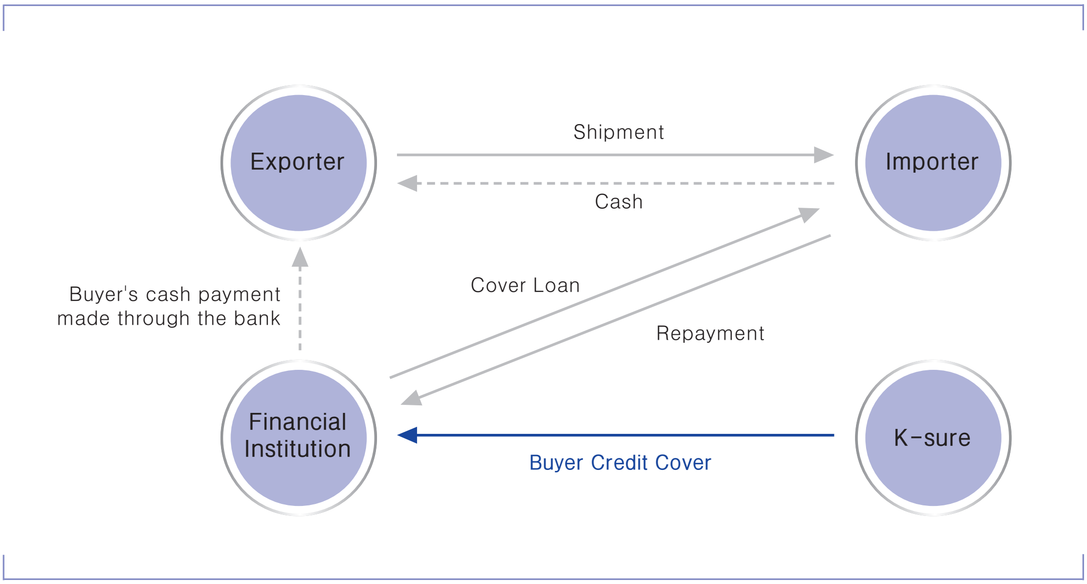
K-sure offers two lines of medium and long term products, the financial products to facilitate financing (Medium- and Long-Term export insurance, Interest Rate Risk Insurance, Overseas Business Credit Insurance and Export Bond Insurance) and the insurance products to cover the risk of non-payment of Korean businesses' export receivables and overseas investments (Overseas Construction Works Insurance, Service Insurance and Overseas Investment Insurance).

Medium- and Long-Term export insurance covers the risk of non-payment on credit used to finance the export of Korean capital goods. Overseas Business Credit Insurance protects the risk of non-payment on credit used to finance Korean business' overseas investment. And both insurance products are applied only to those financial contracts with a tenor exceeding two years.

K-sure utilizes these two programs to facilitate financing, and thus, the boosting of exports and overseas investments by Korean enterprises in global financial markets. The role of these medium- and long-term products is expected to become more important with the increasing demand for ECA-backed loans seen in the past couple of years due to the global economic crisis.

The following diagram shows how Medium- and Long-Term export insurance (Buyer Credit) works. Most medium- and long-term transactions are mostly related with capital-driven projects that involve a huge amount of capital and long periods. Thus, the buyer (contractor/importer) borrows a huge amount of capital from financial institutions to pay the exporter over a long period (actually, the financial institution pays the importer). At this time, K-sure provides insurance that it will pay the capital borrowed by the importer in case the importer defaults on the loan. This scheme is called “Medium- and Long-Term export insurance” (Buyer Credit). The eventual goal of export insurance is to facilitate financing to promote the export of capital goods since importers would not be able to secure long-term financing from financial institutions without K-sure’s insurance.

Figure 2-2 | How Medium and Long-term Credit Insurance Works



2.3.3. Products supporting SMEs’ Securing of Finance

Export Credit Guarantee (Pre-Shipment) is a program where the exporter secures a loan or L/C issued by a foreign bank or export finance institution with K-sure’s guarantee to secure funds to manufacture or process goods to be exported out of Korea.

This scheme is operated directly and indirectly in which K-sure may directly issue a guarantee to the exporter upon review or consign a bank to review and issue a guarantee. The latter system was devised to favor the exporter who can receive a guarantee from its bank without going through K-sure. As of late 2010, K-sure has concluded MOUs with 14 financial institutions to consign the issuance of Export Credit Guarantee issuance.

Export Credit Guarantee (Post-Shipment) supports exporters by allowing the exporter to receive export proceeds after the shipment of goods on credit before the settlement date from a foreign financial institution that had purchased export receivables based on shipment documents.

Foreign Exchange Risk Insurance is a scheme to protect the exporter from FX fluctuations where K-sure indemnifies FX losses or the exporter returns FX gains to K-sure. In other words, the exporter can use this scheme for FX hedging purposes. The exporter transacts in Korean Won, including export proceeds, to protect profits and avoid risks from FX fluctuations.

2.4. Changing Hands over the Years before the Establishment of KEIC

2.4.1. Korean Reinsurance Corporation (Korean Re)

In June 1968, the economic ministers of Korea agreed in principle to let the Ministry of Finance to oversee the export insurance system as it had supervisory authority over insurance activities and the special nature of insurance, over the Ministry of Commerce and Industry responsible for trade. And the Korean Non-Life Reinsurance Corporation (Korean Re), the only government-invested agency handling insurance activities at the time, was commissioned with the daily operation of trade insurance on behalf of the Korean government. And the supervisory authority was given to the Fiscal Policies Bureau at the Ministry of Finance (then it became the Policy and Insurance Bureau after March 1973).

Korean Re offered five different insurance programs including general export insurance, export finance insurance, export insurance, deferred-payment export insurance, and consignment sale export insurance. Premium rates were set as low as possible to minimize policyholders' burden since, unlike property insurance, export insurance is characterized as having the government's policy support in nature. At the same time, they also reflected the balance sheet of Korean Re in an effort not to incur losses to the "Export Insurance Fund," enabling the independent operation of Korean Re without dependence on government funding. Furthermore, the government allowed the "Export Insurance Review Council" to decide whether to provide comprehensive insurance based on the product, exporter, or cooperative to prevent policyholders from taking too much risk and also to level premiums.

In February 1969, when trade insurance was offered for the first time in Korea, Korean Re had only three departments to handle the trade insurance business including the business department that operated the trade insurance business; the buyer credit research department that was responsible for credit research; and the management department that was responsible for back-office affairs including management, general affairs and finance. And there were only 20 personnel who directly handled the trade insurance business. The trade insurance business barely managed to stay afloat until 1974 when the number of personnel was increased and the size of the organization was expanded with the opening of the Busan office.

Aside from its Board of Directors, Korean Re had set up the "Export Insurance Review Council" to deal with major issues arising during the course of operating the export insurance. The Council was established to resolve conflicts of interest at Korean Re as a proxy of the government and maintain expertise in export insurance. The Council reviewed and decided on coverage rates, general terms and conditions of various insurance policies, limits in insurance relationships, limits of liable periods for various policies, implementation of comprehensive insurance, underwriting limits for each insurance program, operating guidelines for the Export Insurance Fund, budgeting and settlement of accounts with the Export Insurance Fund, etc.

The Council was composed of a chairman and up to 15 members, with the CEO of Korean Re taking the chairmanship. The members included a Director of Finance of the Ministry of Finance; Director of Trade of the Ministry of Foreign Affairs; Director of Commerce of the Ministry of Commerce; and Industry Director of Agricultural Affairs of the Ministry of Agriculture; and one board member each from the Bank of Korea, KEXIM and KOTRA; Secretary General of the Korea Chamber of Commerce and Industry Executive; Vice President of Korea International Trade Association; and individuals with expertise in export insurance.

2.4.2. The Export-Import Bank of Korea (KEXIM)

The government shifted its policy focus from the light to heavy industry in the mid 1970's as heavy and chemical exports increased in the 1970s. And on July 1, 1976, the government spun-off the Medium/Long-term Credit group of Korea Exchange Bank (KEB) to set up the Export-Import Bank of Bank (KEXIM) as a way to boost the export of ships, overseas investments, and overseas EPC contracts.

With the establishment of KEXIM, the government amended the Export Insurance Act on December 31, 1976 to strengthen trade insurance to insure financing of medium and long-term and overseas investments. And the trade insurance business was assigned to KEXIM from Korean Re effective on January 1, 1977; subsequently, additional personnel were added and the organization expanded. And the consensus was that the Ministry of Commerce and Industry would be better suited to handle the operation of trade insurance because the trade insurance scheme is closely related with trade. From a functional point of view, it made more sense because it removes uncertainties related with export, supplements finance, works as a trade management system, and promotes exports.

Thus, the operation of export insurance was handed over to the Ministry of Commerce and Industry from the Ministry of Finance, where the "Export Insurance Division" was set up specifically to handle export insurance related affairs. And in November 1981, the “Second Division of Export Insurance” responsible for exports based on medium- & long-term deferred payment contracts, foreign investments and international bidding, assumed the responsibility for trade insurance. As a result, effective policy support was mobilized for the export of the heavy industry including EPC and heavy and chemical goods on a medium- & long-term deferred payment basis, which had steadily increased in line with the government’s heavy industry export promotion policy in the mid 1970’s.

Trade Insurance drew much attention with the progress of the Uruguay Round negotiations in the 1990’s as countries around the world felt the limitations of direct export support including subsidies. The “Second Division of Export Insurance” changed its name to the “Trade Insurance Division” in November 1991 to recognize the importance of the role of trade insurance in supporting exports. This name change from “Export Insurance Division” as initially planned reflected the intention of the government to minimize the risks from not only exports but also imports as well.

The number of personnel handling trade insurance was also augmented; consequently, the “general affairs department” and “claims department” were established to research and improve the overall system and to effectively handle claims. In the following year in August, the Los Angeles office was set up to handle importer credit and claim investigations and the Hong Kong office was established in the following month to oversee Southeast Asia.

Even after KEXIM took over the trade insurance business from Korean Re, the “Export Insurance Review Council” at Korea Re made decisions on major items related with the business, rather than the Board of Directors of the KEXIM. Furthermore, the Council was also assigned to review those cases of export insurance contracts where the KEXIM would be the beneficiary as the bank providing both trade insurance and deferred export finance.

3. Establishment of K-sure

3.1. Background

The Korean government recognized that trade insurance was an effective policy tool to support the entry of Korean businesses into the global market in line with the emergence of a new international trade regulatory environment in the 1990s which changed drastically during the Uruguay Round negotiations, as shown with the 5th amendment of the Export Insurance Act where an article was adopted to establish an agency handling trade insurance exclusively.

Even under this global trade environment where trade insurance could be an excellent policy tool, only about 3% (the amount of export insurance underwritten/total exports amount) of Korean businesses utilized trade insurance in the early 1990's. Despite the fact that the utilization ratio shot up to a level of 3 to 4 % at one time or another with the implementation of a comprehensive insurance program for shipbuilding and EPC exports, the average ratio remained at the 1% level during 1969 up to the late 1980's.

Compared to advanced countries with a relatively stable export pattern that resulted in a utilization rate of 20~30%, this ratio was very low. For example, 50% of Japanese exporters used trade insurance in the late 1970's when the country's total exports volume was between U$ 50 to 100 billion.

Although there were several factors that inhibited the utilization of trade insurance, the major obstacle in the way of a higher utilization rate was the fact that the operation of trade insurance was commissioned to agencies that did not specialize in trade insurance, namely Korean Re and KEXIM.

The Korea Reinsurance Corporation, the predecessor of Korean Re, offered reinsurance programs for life and non-life insurance, and thus, its purpose was totally different from what trade insurance was adopted for, namely policy support. On the other hand, although KEXIM has a similar policy support function, its major scope of operation lies in financial, not insurance products.

Furthermore, trade insurance is a special form of insurance with the purpose of providing protection against political and commercial risks. The risks would be assessed based on analysis and the insurance to cover these risks were provided without collateral. The focus is different from banks which provide loans placing priority on returns.

Other than the problems associated with administering trade insurance through a commissioned system, the number of policies underwritten increased from about 2,000 to more than 20,000 a year with the implementation of the comprehensive export bill insurance. And with the number expected to increase continuously with the changing international trade environment, the government saw the limitations of a commissioned basis system.

3.2. Policy Decision-making Process

The Ministry of Commerce and Industry revised the Export Insurance Act again in 1981 as the legal basis for establishing Korea Export Insurance Corporation, with the sole responsibility of administering export insurance in Korea, benchmarking 27 out of 33 Berne Union member countries operating independent export credit agencies (ECAs).

The Berne Union (The International Union of Credit & Investment Insurers) facilitates world-wide cross-border trade and investments by fostering international acceptance of sound principles in facilitating the credit of export and insurance of investments for the purpose of promoting international trade. There were 50 members from 40 countries as of 2010. The Berne Union Intranet offers underwriting statistics for each member and other information useful for actual underwriting cases. K-sure as KEIC hosted the annual general meeting (AGM) of the Berne Union in 2009 to boost its international standing and recognition.

However, the biggest obstacle in establishing the agency was securing funds. Although there was no debate about having to establish an effective independent agency solely responsible for trade insurance at the government, with the trade insurance fund being only KRW 26.6 billion in the early 1990s, the Ministry of Finance and the Ministry of Strategy and Planning in charge of the national budget continued to raise questions about the agency's substantiality even after a steering committee was set up for the agency and insisted that KEXIM keep running the operation for at least several more years.

The Ministry of Commerce and Industry negotiated with the Ministry of Strategy and Planning for two more years to secure more funds. In the mean time, Korea International Trade Association (KITA) contributed KRW 5 billion and the government promised to expand the Fund during the next two years. Thus, the bill to establish "Korea Export Insurance Corporation (KEIC)" was passed during the economic meeting of ministers at the Blue House.

3.3. Steering Committee

A steering committee, with its secretariat, for the establishment of "KEIC" was formed in May 18, 1992. The committee was composed of five members including the appointed president of KEIC, deputy minister of Economic Finance Board, deputy minister of Finance, deputy minister of the Ministry of Commerce and Industry, and vice president of KEXIM. They prepared and reported the "comprehensive progress report" to the Minister of Commerce and Industry, containing the article of incorporation, budget and balancing of accounts statements, international regulations and the projected number of employees, and operational procedures. And the steering committee convened temporarily for two months until the establishment of KEIC on July 7, 1992.

All the major decisions related with KEIC's establishment were made once a consensus was reached among various government stakeholders since the steering committee was composed of high-ranking government officials with respective expertise in budgeting, finance, and industry.

The secretariat was comprised of three teams with 25 member staff to assist the committee. The three included the planning (the article of incorporation of KEIC, registration for the establishment of KEIC, transfer of power, etc), legal (overall regulations related with trade insurance, adoption and amendment of general terms and conditions for insurance products, etc) and general affairs (budget proposal, office rentals, etc) teams. Most of them were from KEXIM that were responsible for insurance activities at the bank.

KEIC took over all trade insurance related activities from KEXIM effective July 7, 1992, ending the chapter in history where trade insurance was run on a commission-basis for 23 years and 6 months.

3.4. Adoption and Amendment of Acts

3.4.1. Background behind the Adoption of the Export Insurance Act

The need for trade insurance emerged when the government expanded financial and tax support for businesses after the introduction of the first "Five-year Plan for National Economic Development" in 1962. Specifics on the introduction and operation of export insurance were discussed starting in 1968, the year when the second "Five-year Plan for National Economic Development" was introduced, after the Ministry of Commerce and Industry (the current Ministry of Knowledge Economy) surveyed traders, bankers, scholars and business organizations on the need for export insurance in early 1968.

The Trade Insurance Act (initially the Export Insurance Act) was adopted on December 31, 1968, modeled after Japan's "Export Insurance Act" which contributed to the export promotion policy as part of the post-WWII reconstruction efforts. The Trade Insurance Act is composed of a total of nine chapters with 45 articles. The major contents include the purpose of adopting the Act, types of insurance products, premiums, total ceilings, etc. It even contains practical information on items related with the conclusion and termination of insurance contracts, the scope of coverage, payment of insurance payouts, etc.

3.4.2. Amendments to the Trade Insurance Act

The Trade Insurance Act was amended 18 times until 2010 due to changes in regulations related with the Act, trade insurance system, operational and organizational changes, etc. Recognizing that the Export Insurance Act adopted in 1968 could not deal with changes in commercial practices and practical financial issues in a flexible way because it contained too much specific information on standard operating procedures related with the operation of export insurance, several amendments were made under the Trade Insurance Act including the "Trade

Insurance Enforcement Decree", "Trade Insurance Enforcement Regulation", "Trade Insurance Business Process Rules", etc.

The latest amendment was made on April 5, 2010 when the "Export Insurance Act" was amended to the "Trade Insurance Act", expanding the scope of coverage to include import insurance and granting K-sure the power to issue bonds to secure funding directly from the market.

3.4.3. Major Contents of the Trade Insurance Act

The Trade Insurance Act is the very foundation for the operation of trade insurance programs in Korea. From a legal perspective, it is a special statute that covers trading companies and acts as the legal basis for the operation of business insurance where exporters or banks are the policyholders.

The major contents include the establishment of the Trade Insurance Fund and the Korea Trade Insurance Corporation, the mandate of the trade insurance, the organizational structure and composition including the composition of the board of directors and appointment of its president and the adoption of standard operating procedures for the operation of specific programs.

The Act ensures an effective operation of the trade insurance system, which protects exporters, importers and financial institutions that facilitate trade from the risks related to the exporting of goods and services. It also insures other forms of international transactions for the purposes of promoting exports and developing the national economy. When the Export Insurance Act was amended to the Trade Insurance Act in April 2010,the scope of coverage was expanded to include risks related with not only export transactions and overseas investments but also import transactions to reflect the closer ties between export and import transactions and the fast convergence of trade and investment seen in recent years. Under the act, import transactions of vital commodities including oil, natural gas, minerals, etc., and domestic transactions that contribute to export promotion can be insured.

Furthermore, flexible operation of the trade insurance system became possible by subjugating practical issues related to trade insurance such as insurance types, premiums, comprehensive insurance, etc down to subordinating regulations.

However, the Ministers in charge are still responsible for setting the maximum underwriting limit of K-sure with the approval of the National Assembly each year. Also, the underwriting limit for medium and long term transactions exceeding two years are set within the total limit for risk management. Furthermore, small and medium-sized exporters are given benefits such as discounts on premiums, increased coverage, special programs for SMEs, shortened period for granting insurance proceeds, etc. Thus, the Trade Insurance Act has been amended to maximize its role in the development of growth engines in the future.

3.5. Funding

Funding of the Trade Insurance Fund is a major issue to its operation. The Fund was started with KRW 300 million after the Export Insurance Act was adopted on December 31, 1968. The Fund was set up to specifically administer trade insurance, and K-sure (including those organizations commissioned to operate export insurance) is a special purpose non-capital entity that operates and manages this Fund.

In the event of loss occurring as a result of the Trade Insurance Act, the government shall cover the loss. However, this special-purpose Fund was created to boost credibility on payment and indemnify exporters from non-payment. Almost all of the funding for the Fund came from profits of operating the trade insurance business and government contributions. Although organizations other than the government can contribute toward the Fund, the first and the last of such a contribution came from KITA which contributed KRW 5 billion before K-sure was established.

Table 2-6 | Recent Five-year Changes in the Trade Insurance Fund

(Unit: KRW 100 mil)

Category	'06	'07	'08	'09	'10
Gov't contribution	500	250	250	5,100	1,500
Total fund (B)	18,310	19,823	15,290	17,287	11,505

Although external funding sources such as the issuance of bonds and loans from financial institutions had been strictly prohibited, the 18th amendment of the Act in April 2010 provided K-sure with the legal basis to issue bonds to secure funding. However, up until now, no external funding has been used for the operation of the trade insurance system in Korea.

3.6. Launching of Korea Trade Insurance Corporation

Korea Export Insurance Corporation (KEIC) assumed the new name, Korea Trade Insurance Corporation (K-sure) on its 18th anniversary of its founding on July 7, 2010. This change was brought about to reflect the growing interdependency between exports and imports in recent years when financial support for imports became more urgent to boost the country's export capabilities amid rapid technical development and expanding global outsourcing. Insurance support is now possible for the import of commodities vital to the national economy and for parts/materials needed to be processed domestically and exported to earn foreign currencies. K-sure will strive to promote international trade and boost international competitiveness of Korean businesses and of Korea as a nation, while proactively dealing with changing trends in global trade.

4. Evaluation

4.1. Quantitative Achievements

A model was developed to examine the extent of contribution of the trade insurance on exports and GDP for the purposes of scientifically analyzing the effects of trade insurance and of reflecting the results to its operation. In addition, K-sure actively utilizes the model in many areas of its operation including the establishment of management goals, etc.

This model showed that trade insurance contributed 7% to Korea's total export amount of KRW 363.5 billion. In terms of GDP, it accounted for 2.3% of the total GDP of KRW 25 trillion. From the perspective of employment, trade insurance contributed to the creation of 1.9% of the total employment of 300,000.

Table 2-7 | Contribution of Trade Insurance to the National Economy

(Unit: KRW tril, 10,000)

Category	2000	2005	2008	2009	Average('97~'09)
Promotion of exports (vs. total export volume)	11 (5.7%)	20 (6.9%)	54 (11.6%)	38 (8.1%)	20 (7.0%)
Addition to value-addedness(vs GDP)	9 (1.4%)	14 (1.6%)	32 (3.2%)	25 (2.3%)	14 (1.7%)
Employment creation (vs. total employment)	15 (1.1%)	18 (1.2%)	38 (2.3%)	30 (1.9%)	17 (1.1%)

Source: KIEP, 2010.

The results of the analysis show that trade insurance can be an effective tool to promote trade and create employment, especially considering the fact that the Trade Insurance Fund was about US$ 1 billion as of the end of 2010.

4.2. Qualitative Achievements

4.2.1. Support Trade Expansion with Other Nations(Including Regime-changed Economies)

Eastern European countries pursued democracy after escaping the grip of the Soviet Union after Mikhail Gorbachev as General Secretary of the Communist Party adopted “Perestroika,” the political and economic reforms. The Soviet Union collapsed in late 1991 and the countries of the former Soviet bloc quickly transformed themselves into market-based economies from planned economies. The former Soviet Union characterized as a command economy with a nationalized manufacturing base, quickly adopted policies for price liberalization, privatization of state-owned enterprises, and other market-oriented measures including taxation and stock and financial markets. It became more integrated with the global economic order through their membership into the GATT and the IMF.

Korea, in turn, expanded economic cooperation with the former communist countries that had undergone a regime change. These once socialist countries that had adopted the principles of a market economy posed economic and political uncertainties, despite being endowed with rich natural resources and advanced technologies. Thus, Korea focused on expanding the framework for economic cooperation by concluding agreements related to trade, investment protection, elimination of double-taxation, etc. through summits and ministerial meetings.

Korea also established official ties with each of the CIS (Commonwealth of Independent States) countries, after establishing official ties with the Soviet Union in December 1991; subsequently, all the agreements signed with the former Soviet Union were transferred to Russia. In 1992, Korea and Russia concluded several agreements including an MOU on energy cooperation, MOU for industrial cooperation, and an agreement to prevent double taxation. In the same year, the Korea-Russia Fishery Conference was held in January and December and the Korea-Russia Summit Meeting in June with both nations agreeing to expand bilateral economic cooperation through the expansion of investments, exchange of technologies and development of natural resources. Furthermore, Korea held private-public joint meetings with Czechoslovakia, Hungary and other Eastern European countries to discuss economic issues such as trade expansion.

This expanded framework of economic cooperation significantly expanded trade and investment in the private sector, despite the short period of exchange with these former socialist countries.

K-sure has been gathering information on importers from Czechoslovakia and Hungary since 1992 after concluding MOUs with credit research institutions from these two countries.

And effective 1993, the agency eased the underwriting terms for these two countries by providing export insurance even for non-L/C-backed export transactions.

In 1994, the Eastern European region entered a full growth cycle after Poland achieved 4% growth in both 1993 and 1994, while Czechoslovakia finally escaped the turmoil of the Soviet Union's collapse. In 1995, K-sure finally removed all underwriting provisions on Czechoslovakia, Hungary and Poland to promote trade with the regions.

A valid contract limit was set in July 1994 for Russia to resume underwriting for the country that had stopped since the collapse of the Soviet Union as trade expanded in 1993, and the underwriting limit was increased for the country in 1995. Around this time, the underwriting terms were also changed for Slovenia and Kazakhstan.

K-sure resumed underwriting for Russia in 1999 but only for L/C-based transactions after trade insurance was stopped in August 1998 when the country defaulted on some of its sovereign debt in the wake of the financial crisis in Latin America. Currently, the agency is gradually expanding the number of banks dealing with Russian exporters under its portfolio.

In short, export insurance is an effective policy tool to penetrate emerging markets. And the importance of export insurance has grown greater as a tool to mitigate the risk of non-payment of receivables, especially with the recent increase in non-L/C-based T/T and T/A transactions over safe L/C-based transactions. K-sure expects this increasing trend to continue for developing countries, which accounted for 29.2% of the total underwriting volume going to these countries as of 2009, compared to 11.6% in 2006.

4.2.2. Support toward the Export of Capital Goods

The EPC industry related overseas projects contracted out to Korean companies include the exports of machinery, equipment, etc. as well as the designing, engineering, construction, and maintenance/repair of plant facilities. In other words, it involves various industries including manufacturing, engineering, consulting, financing and others; many benefits spill-over before and after the project completion. This, in turn, results in the advancement of domestic industries, creation of value, exports of parts/machinery and human resources, etc.

Fluctuations in global markets for certain export goods can significantly affect Korea because the country relies heavily on the export of these few items. Thus, the EPC industry can be another important export driver and help diversify its export base and break its dependency on a few export goods. The industry also can contribute to the development of new industries and the promotion of trade with other countries that import. This could be not only a source of much needed foreign dollars but also a way to address trade conflicts and import restrictions.

Along with the value-added and knowledge-based sectors of the EPC industry that has a huge potential to lead Korean exports, the shipbuilding and machinery exporting sectors significantly contribute to the national economy by advancing technologies, creating jobs and promoting related industries.

Nonetheless, developing countries that import capital goods, where the cost of capital is high, must resort to payment of exports on a deferred-payment basis, over a payable-at-sight basis, because they lack liquidity. Hence, the competitiveness of exporting capital goods depends heavily on financial market competitiveness, aside from cost and technological competitiveness. As a result, financing conditions become more important as competition becomes more intense. As such, project finance is implemented frequently where cash flows from a specific project are used as collateral without (bank) guarantees. The export of capital goods usually involves projects that require a medium to long term time horizon to complete, and thus, they come with not only commercial risks but also country and foreign exchange risks.

K-sure mitigates the risks associated with project finance to support the export of plants and industrial facilities produced by Korean companies. The Agency became interested in project finance in 1995, as the method of financing based on the securing of future cash flows and assets/rights generated by plant facilities as collateral. K-sure, formerly as KEIC, hosted a seminar on project finance for the first time in October 1995 and then again another in April 1996, to share knowledge on the methods of supporting project finance transactions. In July 1997, the Agency hosted a seminar titled “the infrastructure markets in developing Asian countries and strategies to penetrate these markets” and published a report on “Current trends in project financing” to provide information on regions where Korean companies can secure EPC contracts.

Since 2000, it has launched a series of new products including overseas investment insurance (on investment financing to support the export of capital goods, overseas investments and overseas resources development projects), overseas business financing insurance, overseas resource development comprehensive insurance, etc. The Agency also focused on boosting its international footprint by participating in the “Global Export Finance Conference” and by hosting seminars with major buyers such as Brazil’s Petrobras, etc. With the first meeting on January 1, 2008, K-sure hosts the “Kwangwhamun Forum” annually to build a cooperative network for capital goods export. The Forum participants include capital goods exporters, domestic and international financial institutions, law firms, members of the Korean Plant Industry Association and Korean Shipbuilding Association, etc.

These efforts have paid off, as shown by the increasing trend in the total underwriting volume for MLT insurance products. The volume, which stood only at KRW 199.4 billion in

1992, rose to KRW 13.1841 trillion in 2009 even with the global financial crisis, contributing to a total of USD 46.3 billion of overseas plant contracts in 2009.

Table 2-8 | Underwriting Amount for MLT Products

(Unit: KRW 100 mil)

Category	1992	1997	2000	2007	2009
Support Amount	1,994	17,900	30,522	82,298	131,841

MLT products covered include: MLT export insurance, overseas business financing insurance, overseas construction works insurance, overseas investment insurance, Export bond insurance, Interest rate risk insurance, Service export insurance (earned value method on a deferred payment basis).

Table 2-9 | Korea's Overseas Plant Contract Volume

(Unit: USD 100 mil)

Category	1992	1997	2000	2007	2009
Support Amount	33	65	84	300	63

Source: The Ministry of Knowledge Economy and Korean Plant Industry Association.

4.2.3. Contribution toward Fostering SMEs

K-sure has been implementing the SME preferential treatment policy since its establishment in 1992. Unlike the medium/long-term deferred payment export insurance scheme devised mainly for large companies, the short-term insurance scheme (for both large enterprises and SMEs) has been modified for SMEs. It incorporates provisions to specifically support SMEs in line with the government's SMEs promotion policy.

The export credit guarantee program epitomizes the measures set up to support SMEs. At the time of its introduction, both large and SME exporters were allowed to use the program with SMEs receiving a 30% discount on premiums. However, the program was revised in November 1994 to allow only SMEs.

SMEs can benefit in two ways: being insured as well as receiving premium discounts. Compared to 95% of large enterprises being covered under the insurance scheme, 100% of SMEs receive insurance and a 15% discount on premiums. They are also given benefits on country-based underwriting and a grace period for claiming insurance proceeds, exempted from K-sure's evaluation process in case of small claims. Although a separate set of underwriting limits were specified for SMEs for countries where underwriting is limited, this benefit became no longer applicable since the country-based short-term underwriting policy has been simplified. SMEs are also granted an extra 10%~20% discount on premiums for outstanding SMEs chosen by the government or other K-sure related agencies.

As a result, K-sure's support for SMEs based on the amount and ratio out of total underwriting has steadily increased. In 2009, the underwriting amount for SMEs was USD 52.7 billion, which amounted to 45% of total export volume of USD 117.3 billion achieved by SMEs. These SMEs made up the majority (96%) of K-sure's clients. Indeed, K-sure contributes to the dynamism of the national economy by promoting SMEs under K-sure's export insurance system to drive the export-driven industrialization.

Table 2-10 | Trade Insurance Underwriting Volume for SMEs

(Unit: USD 100 mil)

Category	1992	2006	2007	2008	2009
SMEs' export volume	306	1,042	1,135	1,305	1,173
Export insurance support amount for SMEs	8	361	487	543	527
Export insurance usage by SMEs(%)	2.7%	34.6%	42.9%	41.6%	44.9%

4.3. Overcoming Challenging Times through Trade Insurance

4.3.1. Asian Financial Crisis of 1997 and Role of Trade Insurance in Korea

Korea faced its worst financial challenge in 1997 since the start of rapid economic development in the 1960's. In the wake of the Asian financial crisis, the Korean Won lost half of its value, interest rates rose over 30% and the country's foreign reserves were all but depleted.

The government not only had to deal with the short-term foreign currency crisis but also correct long-term structural problems in the financial markets as well as the corporate, labor and public sectors. Thus, it resorted to a complete overhaul of the entire economy to overcome the financial crisis under broad public support. In the mean time, K-sure also duly carried out its functions as an ECA and was actively engaged in the process of overcoming the crisis as a component of the Korean society.

While fully realizing the fact that the risk profile of its portfolio could increase by insuring more risky transactions from a short-term perspective, the Agency aggressively provided export support to resuscitate the Korean economy by recognizing the economic crisis as a state of national emergency, with the belief that there would be no ground to stand on without a strong Korean economy.

K-sure concentrated its efforts toward its main lines of business, i.e., insurance and guarantees, while focusing on the following two areas to better support exporters in time of crisis.

4.3.1.1. Export Promotion as a Source of Supplying Foreign Currency

First, the main culprit of the financial crisis, the short-term foreign currency shortage, had to be resolved to improve the national credibility of Korea in the eyes of the global financial market and prevent possible future crises.

The agency determined that the promotion of exports was the first and most important way to secure much needed foreign dollars as Korea was (and still is) a heavily export-dependent nation and that a severely marred export trade would delay economic recovery. Thus, the agency concluded that it could contribute to Korea's overcoming of the financial crisis through stronger export support.

4.3.1.2. Promotion of Trade Finance

Second, the agency focused on export finance to fill the gap between creditors and lenders. Financial health is one of the most important aspects to recover from a financial crisis. As such, K-sure reviewed the overall financial sector in detail.

At the time, the capital adequacy ratio of 8% based on BIS (Bank of International Settlements) was the decisive factor in determining the condition of financial institutions. This ratio was strictly observed to the point that banks used the ratio as internal guidelines when lending, completely changing lending practices in Korea and making it difficult even for exporters with sound credit to secure bank loans.

Against this background, K-sure played an important role in filling the creditor-lender gap in that K-sure could lessen a creditor's risk exposure and increase a lender's financial safety by providing insurance. And this especially helped SMEs that usually had many transactions but lacked liquidity.

4.3.2. The Global Financial Crisis and Trade Insurance

The global financial crisis following the bankruptcy of Lehman's Brother's Holdings Inc. in September 2008 led to a world recession as many banks defaulted, housing markets crashed, global trade plummeted, etc. Not only major markets including the U.S., Japan and the EU but also most of the countries in the world recorded negative growth rates.

These changes brought about a severe financial crunch, where exporters were in dire need of export insurance support more than before since commercial banks decreased lending, etc. as banks were worried about the health of their assets worsening further.

K-sure changed gears by operating the insurance business on a contingency basis where an emergency plan focusing on the following three areas was established to promote trade during the financial crisis.

4.3.2.1. Increase Total Underwriting Volume of Trade Insurance

As global economic growth and international trade plummeted in the wake of the global financial crisis, the agency concluded that the recession consequent to the global financial crisis was much worse than preceding recessions. The export slowdown significantly affected the export-led economy of Korea. As such, the agency decided to drastically expand the volume of export insurance to overcome the financial crisis via export promotion. As a result, the total underwriting volume increased by 27% to KRW 165 trillion in 2009, compared to 2008. Thanks to this effort, Korea witnessed only a 13.8% drop in total exports, compared to 30% for Japan, Canada and the U.K.

4.3.2.2. Emergency Liquidity Support for SMEs

The global financial crisis affected SMEs more severely compared to large companies: SMEs were faced with severe liquidity shortage as more lenders recovered loans and increased interest rates on loans. Globally, they faced decreased sales as markets declined sharply. Concluding that proactive support was in order, the agency introduced an emergency guarantee program to provide SME exporters more export insurance and trade bill guarantees for export transactions. As a result, a total of KRW 6 trillion of liquidity was supplied to SMEs in 2009, which was a 281% increase compared to 2008.

4.3.2.3. Increase in Global Market Share

The agency offered export credit guarantees (pre-shipment) in conjunction with overseas marketing insurance to help top manufacturers and promised SMEs to penetrate new global markets even during the crisis. Consequently, the underwriting volume for the IT industry, a major export driver of Korea, saw a 108% year-on-year increase in 2009, for a total of KRW 84 trillion. Korea’s global share of wireless communication devices increased to 32.5% (as of March 2009) from 25.3% (2008).

4.4. Knowledge Sharing with Other Countries

4.4.1. Knowledge Sharing with Vietnam

As part of its Knowledge Sharing Program (KSP) designed to share Korea's development experience with developing countries, the Ministry of Strategy and Finance (MOSF) launched the KSP with Vietnam in 2005. The Ministry concluded an MOU with the Vietnamese Ministry of Finance in September 2006 to support the Vietnamese government in building its financial infrastructure for three years starting in 2007. And in late 2009, both parties agreed to extend this project for two more years until the end of 2011.

Although the export insurance business was not included when this project first started, the Vietnamese government requested the Korean government to include this area in 2008 in light of Vietnam's desire to continue on with the KSP. Upon accepting Vietnam's proposal, the MOSF commissioned the KSP project on export insurance to K-sure, which has since helped the country establish an export insurance system.

K-sure has provided training and has held seminars/lectures for officials and employees of the Vietnamese Finance Ministry and the Vietnamese Development Bank since 2008 in Korea and Vietnam. Upon much deliberation on how to run an ECA in Vietnam, the Vietnamese government declared through a prime minister's decree that a private insurer will be selected to operate the ECA between 2011 and 2013.

During the Annual Research Meeting (ARM) held in January 2011, the Vietnamese government announced that it would decide on which insurer to run the ECA. It also made a request to Korea. First, it asked that a joint survey be conducted to assess the need of export insurance in the country. Second, it sought to utilize K-sure's long-term experiences in designing insurance and guarantee products, building the IT system needed to run the export insurance system, and training personnel in export insurance. In turn, K-sure agreed to help Vietnam during the introduction phase, with the hope of introducing the system and seeing the actual results in 2011.

〈Note〉 K-sure support toward Vietnam for the introduction of the export insurance system within the country

□ Year 2008

- Hosted a seminar on export insurance by inviting personnel from the banking bureau of the Vietnamese Finance Ministry (Nov)
- Hosted a seminar on export insurance in Vietnam for officials of the Ministry of Finance (Dec)
- Attended the 2008 ARM (Dec)

□ Year 2009

- Hosted a seminar on export insurance in Vietnam for officials of the Ministry of Finance (Nov)
- Hosted a seminar on export insurance by inviting personnel from the banking bureau of the Vietnamese Finance Ministry (Dec)
- Attended the 2009 ARM (Oct.1)

□ Year 2010

- Hosted a seminar on export insurance in Vietnam for officials of the Ministry of Finance in October
- Hosted a seminar on export insurance by inviting personnel from the banking bureau of the Vietnamese Finance Ministry in November
- Attended the 2010 ARM in November

4.4.2. Knowledge Sharing with BAEZ of Bulgaria

Upon receiving request from the Bulgaria Export Insurance Agency (BAEZ), which was established in October 1998, to assist Bulgaria in the introduction of the export insurance system, the Korea International Cooperation Agency (KOICA) sought K-sure's assistance. Thus, K-sure took the initiative and dispatched its personnel for about 30 days every year for three years between 1999 and 2001 to help the country launch its own system.

The training conducted by K-sure in 1999 was geared toward laying the foundation for the system including: 1) establishing an operational platform for the system, 2) setting up a system for underwriting limits for each exporter and 3) constructing a system for country credit ratings. Furthermore, K-sure recommended that BAEZ initially introduce a pre-shipment export credit guarantee product. In 2000, based on a survey conducted by K-sure in 1999, the government of Bulgaria adopted the Export Insurance Act for the introduction of the export insurance system and asked for K-sure's help in building the operational platform for export insurance.

The focus of K-sure's training in 2000 was two-pronged: 1) constructing the institutional foundation for the introduction of the export insurance system in Bulgaria and 2) promoting understanding between BAEZ and related government agencies. The specifics of the training emphasized the point that the restructuring and development of the financial sector in the country needed to occur at the same time for an effective introduction and operation of the system. This was despite the fact that vulnerable exporters and financial institutions could complement the supply and demand function of the pre-shipment trade finance, if the pre-shipment export credit guarantee product were to be introduced.

Furthermore, K-sure's training of personnel from the Bulgarian government and related agencies in 2001 emphasized the fact that the legislation of future Bulgarian export policies and early settlement of the export insurance system were important. The contents of the training included: 1) successful cases of Korea's export-led economic growth, 2) importance of export and export insurance, and 3) the Korean government's export support polices.

The technical consultations held by K-sure in three sessions for BAEZ between 1991 and 2001 not only boosted K-sure's status as an advanced export insurance agency but also contributed toward promoting understanding and cooperation between Korea and Bulgaria and between K-sure and BAEZ.

At the same time, this knowledge sharing experience transferred Korea's export insurance system to an Eastern European country for the first time, and thereby, established a stepping stone to boost cooperation with ECAs of other countries in the region.

5. Lessons and Ramifications

5.1. Factors to Be Considered for the Development of an Official ECA

5.1.1. A Small Agency Focusing on Core Functions

As mentioned earlier, the "value chain" of export insurance lies in three functions, i.e., buyer credit research, underwriting and indemnification (including debt management). Additionally, the fourth function may be the "administrative management function", which deals with the supervision of administrative resources to help management's decision-making process. In the early stages of establishing an ECA, it would be ideal to set up the agency focusing only on these four functions. The export insurance business does not require a large number of employees at the beginning since direct lending is not involved in underwriting insurance but rather functions such as paying out insurance proceeds when the client files for a claim. Furthermore, there are many ways to mitigate the risks and maximize the benefits from underwriting such as the introduction of comprehensive insurance, standardization of risk, etc. However, it is necessary to flexibly increase/decrease personnel and organization size in line with market demand and export insurance environment.

5.1.2. An Independent Agency Specializing in Trade Insurance

The most effective way to maximize the effects of the government's policy on export promotion is to establish an independent agency that handles the export insurance business only. But for developing countries, a commissioned agency such as Korea's KEXIM could conduct trade insurance activities due to lack of experience in trade insurance and large financial burden on the nation. In such a scheme, where an export-import bank handles the export insurance business, measures are needed to prevent the inherent and unavoidable moral hazard of having the bank underwrite loans and insurance.

5.1.3. A window to build an international network and acquire know-how from advanced ECAs

Building international networks to obtain information on buyer credit, to conduct claims related investigations, and to recover payments on claims already paid out, is one of the most important tasks of establishing an ECA. Despite the availability of hundreds of credit rating agencies targeting global, regional or specific markets, it is time-consuming to find out which credit rating agencies are credible and to establish the foundation to effectively utilize them.

As such, it is important for ECAs in developing countries to form ties with advanced ECAs by holding regular meetings, joining the Berne Union (The International Union of Credit & Investment Insurers) or the Prague Club (a 33-member international club of emerging, development country ECAs and credit and investment insurers), and actively participating in meetings and seminars hosted by these organizations. There are many cases where BU members amongst themselves successfully form closer ties by concluding MOUs for comprehensive cooperation, reinsurance agreements, etc. to exchange information and personnel.

5.2. Operation and Future Development

5.2.1. Principle of Non-competition with Private Financial Institutions

Once growth of a country's domestic financial markets is in line with its economic growth, the official export insurance agencies (such as ECAs and export-import banks) need to stay away from competing in the domestic financial sector in order not to retard the growth of private financial institutions. To this end, it is important to foster domestic commercial banks and insurers that can compete in the international arena.

5.2.2. One Trade Insurer Responsible for All Risks Coming from Trade

Developing countries also need to decide whether to establish one institution to handle both trade insurance and export finance or two separate agencies. Korea, for example, had two agencies, the Korean Re and KEXIM, with their authority to operate trade insurance activities. Then, it established KEIC in 1992 to exclusively handle trade insurance. Advanced countries such as the U.S., the U.K., and Canada operate one agency whereas Japan, Sweden and Norway operate two separate agencies. Thus, it is important to establish a system that best suits the country.

5.2.3. Flexible Operation and Introduction of New Programs

ECAs also need to develop new products/programs in line with the country's industrial development stage. K-sure, for example, offered general export insurance products such as export insurance for SMEs to support the export of consumer goods in the early stages of its establishment. The agency then focused on MLT export insurance, export bond insurance, and insurance for foreign construction works as Korean companies in the heavy and chemical industries entered global markets. In recent years, K-sure has introduced new products including: cultural export insurance to support the entertainment industry to penetrate global markets; overseas investment insurance to promote foreign investments by Korean companies; overseas business financing insurance; and overseas natural resources development fund insurance.

Chapter 03

Establishment of a Trade Promotion Organization (TPO)

Chapter 03

Establishment of a Trade Promotion Organization (TPO)

Youn-Soo Rah(KOTRA)

<Summary>

This research report covers a wide range of activities carried out by KOTRA (Korea Trade-Investment Promotion Agency), and explains the numerous changes it has undergone since its establishment in 1962 as a Korean state-run trade promotion organization (TPO). This report also introduces trade strategies to countries which intend not only to establish a TPO but also to build-up capacity for an already existing organization.

Section 1 provides background information on the establishment of KOTRA and the state of the South Korean economy at the time of its founding. When it was established, KOTRA used JETRO (Japan External Trade Organization) as a model in view of its success in promoting Japan's business. With a mission to improve the country's international balance of payments by promoting the growth of exports, KOTRA is now engaged in the following activities: surveying and exploring overseas markets; promoting Korean industries and domestically-made goods; serving as a channel between foreign entities interested in trading with the country and domestic exporters; operating trade centers in foreign countries; and participating in international trade fairs and exhibitions.

At present, KOTRA is also engaged in activities aimed at attracting foreign direct investment (FDI) amid changes in the environment and Korea's economic growth. Indeed, KOTRA has been appraised as an exemplary agency among the world's many trade promotion organizations as a result of its innovative efforts.

* Notice: Data and Figures are collected in 2010.

Section 2 deals with KOTRA's organizational structure and budget. As of 2010, KOTRA had 2,025 employees (625 employees at the KOTRA Headquarters plus 1,400 locally hired staff) working at its Korea Business Centers (KBCs) in 99 cities around the world. KOTRA plans to increase the number of KBCs, including those in Africa, by 12 in 2011 to assist domestic businesses with their forays into world markets.

KOTRA's annual budget currently amounts to $290 million, most of which is provided by the government. The diverse activities carried out by KOTRA include active indirect(cf. p.1)participation in the management of KINTEX in Goyang near Seoul and BEXCO in Busan.

Section 3 discusses the activities carried out by KOTRA in detail. Since its establishment, KOTRA has been engaged in a wide variety of activities designed to help the overseas marketing efforts of domestic businesses. In addition, it now assumes the function of attracting FDI and providing support for domestic businesses looking for investment opportunities in foreign countries. More recently, KOTRA has even become involved in globalizing the knowledge-based service industry, fostering the medical service industry, and helping domestic businesses participate in the overseas procurement market.

Essentially, the collection and distribution of information on overseas markets forms part of KOTRA's functions. KOTRA distributes market information collected through its overseas network to customers on a real-time basis and holds different seminars to help domestic businesses carry out their operations based on solid information.

In connection with the need to provide support for overseas marketing efforts, KOTRA dispatches trade delegations to more than 200 sites annually, and helps businesses take part in exhibitions held in foreign countries. KBCs serve as branch offices for small-sized domestic exporters, assisting their efforts to explore overseas markets. KOTRA also operates logistical centers in major cities around the world to help SMEs reduce their logistics expenses.

Under the Foreign Investment Promotion Act, KOTRA was designated as a leading agency for supporting efforts on attracting FDI. In fact, it attracts more than $11 billion worth of FDI annually and operates an "ombudsman system" to settle difficulties experienced by foreign businesses in the country. KOTRA also provides assistance on matters pertaining to local laws, accounting systems and labor-management relations to South Korean businesses operating in foreign countries through the Korean Investor Support Centers based in China, Vietnam, Indonesia and Cambodia.

With the expansion of the country's trade volume, KOTRA's mission has become more diverse. At the time of its establishment, the provision of trade-related support for domestic businesses constituted the full extent of its duties. Now, its role has been broadened dramatically to include efforts on globalization of knowledge-based industries, recruitment of talented professionals, and brand marketing and PR.

Section 4 sheds more light on KOTRA's successful accomplishments. It is important to note that KOTRA is by law an independent agency, and is managed accordingly. KOTRA explores relevant business ideas on its own, although it also carries out programs under the foreign economic policies of the government.

It is also important to note that KOTRA does what it can to enhance the expertise of its employees in their specialty areas through diverse programs. KOTRA encourages its employees to enhance their professional knowledge in business management and industrial operation as well as proficiency in foreign languages such as English and other foreign languages.

Every year, KOTRA's performance results undergo both an internal and external management appraisal. The customer satisfaction, which is often appraised when customers participate in its projects, is considered as such an important factor in KOTRA's incentive structure.

Keeping in mind that its operation should be carried out with the help of an efficient information-based system as a body with an expansive network, KOTRA operates WINK, an internal infrastructure system that facilitates communication between employees, as well as portal sites that provide customers with information and services, and KBCs' websites, which enable prompt and efficient operation.

Finally, Section 5 evaluates KOTRA's achievements to date. No one will dispute the fact that the agency has made great contributions to South Korea's rise as the 13th largest economy in the world from being one of the poorest just 50 years ago. This was made possible by the establishment of an advanced operational platform that is able to manage worldwide operations systematically; the training of talented professionals with expertise; the adoption of a service-oriented mindset that puts the interest of customers first; and the network of solid partnerships with relevant institutions both in and out of the country.

As evidenced by KOTRA's achievements, a state-run TPO can succeed only when it possesses the following: a systematic apparatus to enable autonomous operation; service-minded employees that put the interest of customers first; talented professionals with expertise; efficient management of the internal functions of the organization; and the ability to play a leading role in carrying out the government's policies with foresightedness.

1. Background to Establishment

1.1. The Economic State of South Korea in the Early Days

A KOTRA employee recollects Korea's weak export economy in 1962, the year in which the agency was established:

> In 1962, Korea recorded exports of just US$54.81 million, as follows: foodstuffs including pork worth $1.47 million, fish worth $3.45 million, dried fish worth $2.49 million, shell fish worth $1.81 million; live animals worth $2.85 million; and raw silk worth $3.96 million; natural resources worth $19.37 million, including China clay and graphite deposits worth $2.69 million, iron ore worth $3.85 million, and coal worth $2.74 million. As such, production of the primary industry accounted for 75 percent of Korea's total exports at the time KOTRA was established.[1]

The following was written by Swedish journalist Haken Hedberg immediately after his visit to South Korea in the early 1960s:

> In the summer of 1963, I closed my own private door to South Korea behind me with a bang. I would not visit the place again. This country had no future. In the countryside people ate bark from the trees, and new university graduates went straight into the unemployment queues.[2]

The homepage of the U.S. State Department had the following to say about the remarkable economic development of South Korea.

> Since the 1960s, South Korea has achieved an incredible record of growth and global integration to become a high-tech industrialized economy. Four decades ago, GDP per capita was comparable with levels in the poorer countries of Africa and Asia.[3]

1. Source: KOTRA, Chronicle of KOTRA's 40 Years, 2002
2. Source: Haken Hedberg, The New Challenge; South Korea, 1978
3. Source: Website of the U.S. Central Intelligence Agency (www.cia.gov)

1.2. Background to KOTRA's Establishment

In 1962, the first year of the First Five-Year (1962~1967) Economic Development Plan, the value of South Korea's exports stood at a mere US $55 million. The country's foreign reserve, which stood at US$168 million, decreased to $114 million by the middle of 1963, although the country managed to attain its export target of $100 million at the end of November 1964. Under such circumstances, KOTRA was established in 1962, with the mandate of of export promotion.

At the time, the Ministry of Commerce and Industry (MOCI)[4] intended to establish a trade promotion organization under the plan to achieve the export target of $100 million by 1961. In connection with these plans, the MOCI sent a team of working-level employees from the ministry to Japan in December 1961 to assess the role of JETRO.

The South Korean government laid the legal basis for the establishment of a TPO with the enactment of the Korea Trade Promotion Agency Act on April 24, 1962, followed by its Enforcement Decree on May 7 of the same year.

Thus, KOTRA was established on June 2, 1962, with the inauguration of Mr. Kim Gi-yeop as its first president. Mr. Kim Gi-yeop had served as a vice president of the Bank of Korea, a vice chairman of the Korea International Trade Association (KITA), and a member of the committee for the establishment of KOTRA. The agency took its first step forward by opening trade centers in New York, Los Angeles, Hong Kong and Bangkok in the fall of that year.

1.3. Purpose of Establishment and Major Functions

In May 1962, the Minister of MOCI declared that KOTRA would be established as a government institution, with a paid-in capital of two billion hwan (the currency of South Korea during 1953~1962). He added that the agency's main functions would be to survey and explore overseas markets; promote Korean industries and domestically-made goods; act as a go-between for foreigners interested in trading with the country and domestic exporters; operate trade centers in foreign countries; participate in international trade fairs and exhibitions; make efforts to improve the packaging and designing of exported goods; and display samples of the country's export goods in cooperation with Korean embassies in foreign countries.

Thus, KOTRA carried out its task to assist the country in earning foreign currencies by promoting exports and improving the country's export structure, which was heavily dependent on the production of primary products.

4. Now the name has been changed to the Ministry of Knowledge Economy.

At the beginning, KOTRA's major activities consisted of carrying out market surveys/explorations and exhibition/PR. Its market survey activities consisted of collecting import/export-related materials and information; surveying the demand for specific Korean-made goods in foreign markets and the supply capability of domestic exporters; measuring the rate of increase in exports; checking trade-related systems and policies; and analyzing the cost of and reasons for the poor performance of exported goods. Its market exploration activities were focused on providing a channel of communication between foreigners interested in trading with the country and domestic exporters; analyzing market trends; and searching for potential buyers of Korean-made goods. Its exhibition/PR activities comprised of a variety of activities, including the production of PR films and brochures. KOREA TRADE[5], which served as a leading PR brochure for SME exporters for a long time, was launched at that time. As its market survey/exploration and exhibition/PR activities started to reap substantial results, KOTRA opened the Export Academy in March 1965, followed by the Information Center for Exporting Industries towards the end of 1969.

KOTRA also implemented diverse programs designed to help exporters cultivate their commodity-related knowledge. First of all, a research body was launched in connection with the need to develop goods that would satisfy the needs of foreign customers. This research body, reporting directly to KOTRA's president, applied itself to research aimed at improving the quality, packaging and design of exported goods. The activities carried out to provide support for the improvement of export packaging included the following: recommendations for setting export packaging standards; the dispatch of delegations to industrialized countries to acquire knowledge on packaging methods; lectures on packaging; and conferences with relevant institutions and businesses. The export goods packaging exhibition (1962~1969) was one of the leading programs carried out as a means of improving the way in which exported goods were packed. Goods developed through the exhibition were showcased in trade centers in foreign countries for potential foreign buyers.

1.4. Changes after the Establishment of KOTRA

KOTRA, which led the growth of the country's economy through the expansion of foreign trade, was assigned new functions in line with the changing environment. Toward the end of the 1980s, it played a leading role in opening new markets for exports in the transitioning economies of the Eastern Europe. Liaison offices were established in Budapest, Hungary and Seoul in 1987, even before the establishment of diplomatic relations between the two countries. Also, South Korean trade representative offices were opened in Moscow, Russia and Beijing,

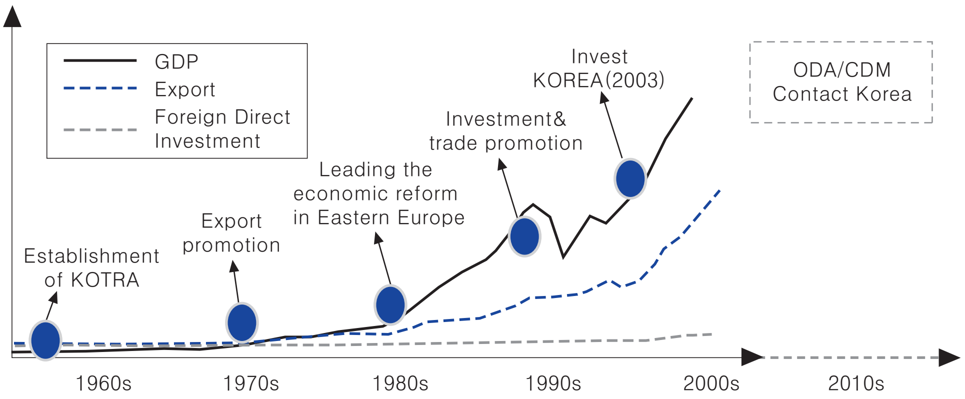
5. KOREA TRADE was a PR brochure that compiled a catalogue of Korean export products. It is no longer published.

China in 1989 as footholds in leading socialist countries.

In August 1995, the organization's name was changed from the Korea Trade Promotion Corporation to the Korea Trade-Investment Promotion Agency, to signify the undertaking of additional functions, i.e., inducing foreign direct investment (FDI) and collaborating in the industrial sector. The Korea Investment Service Center (KISC) was newly launched as a KOTRA-affiliated organization dedicated to providing foreign investment-related service. With the enactment of the Foreign Investment Promotion Act, following the foreign exchange crisis that hit the country in 1997, KOTRA's functions of inducing foreign direct investments were further reinforced. In 2003, KISC was changed to Invest Korea (Invest Korea), as the organization was dramatically increased to become a one-stop service for FDI.

In 2007, KOTRA also assumed the role of providing support to South Korean businesses looking for opportunities in foreign countries. At present, there are total of 13 Korean Business Support Centers, including one in Beijing.

Figure 3-1 | Changes in the Functions and Roles of KOTRA



Source: by KOTRA[6]

In 2008, Contact Korea was launched to recruit relevant experts from foreign countries

Towards the end of 2009, South Korea became a member of the OECD Development Assistance Committee (DAC). Thus, KOTRA assumed an additional function related to foreign aid and PR in regards to Korea's ODA efforts.

6. A table or figure with no source shall be considered as materials owned or researched by KOTRA.

As noted, KOTRA has taken on new roles in step with the country's economic growth with the mandate of pursuing the South Korean Government's trade/FDI-related policies. Now, KOTRA has become one of the leading TPOs in the world as a result of its constant efforts in innovation.

2. KOTRA - Its Organizational Structure and Budget

2.1. Organization and Staff

The number of KOTRA's employees has increased from 181 since its establishment in 1962 to 1,400 at present (2010), including 650 locally hired people at KBCs in 99 cities and 72 countries.

KOTRA is a global organization on which the sun never sets. The number of KBCs in foreign countries increased from four since its establishment to 99 by 2010, and is expected to increase to 111 by the end of 2011 with the addition of 12 more in the future.

Table 3-1 | Brief History of KOTRA

Year	Event
1962	• Establishment of KOTRA (Korea Trade Promotion Corporation).
1970	• Establishment of the Information Center for Exporting Industries.
1985	• Establishment of a Budapest KBC in Hungary, the first one set up in the former Socialist Bloc.
1995	• Name changed to the Korea Trade-Investment Promotion Agency. • Establishment of the Korea Investment Service Center (KISC).
2003	• Establishment of Invest Korea.
2004	• Awarded the World Trade Promotion Organization Award from the WTO/ITC. • Started providing support to Korean businesses looking for overseas investment opportunities.
2008	• Establishment of Contact KOREA, a service dedicated to recruiting top professionals.
2009	• Establishment of the Support Center for Overseas Investment.

Figure 3-2 | KOTRA Organizational Chart

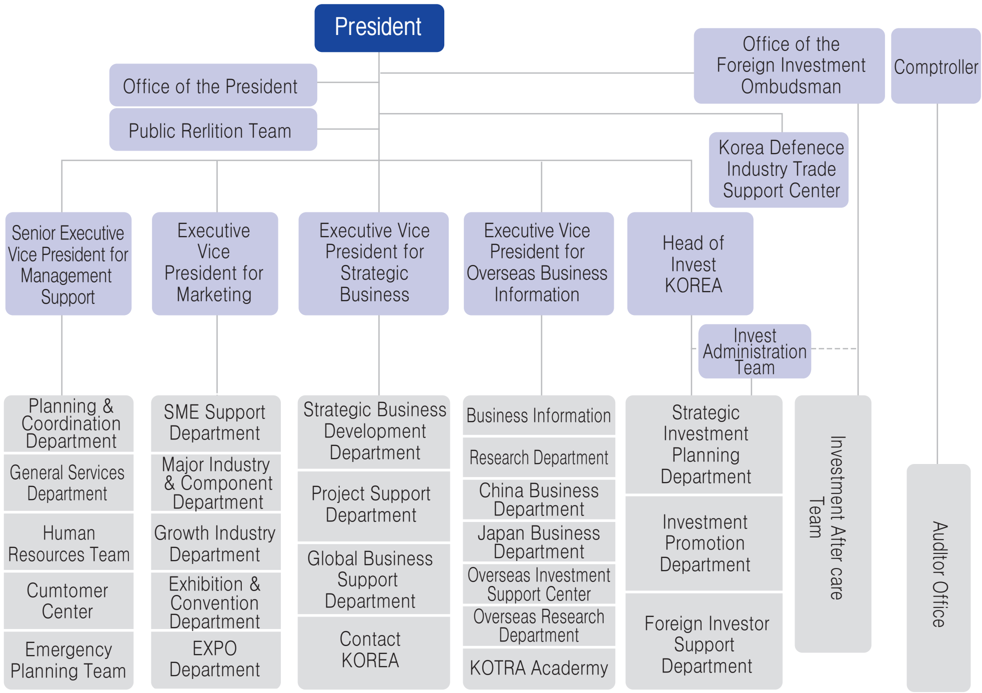


Figure 3-3 | KOTRA's Overseas Network

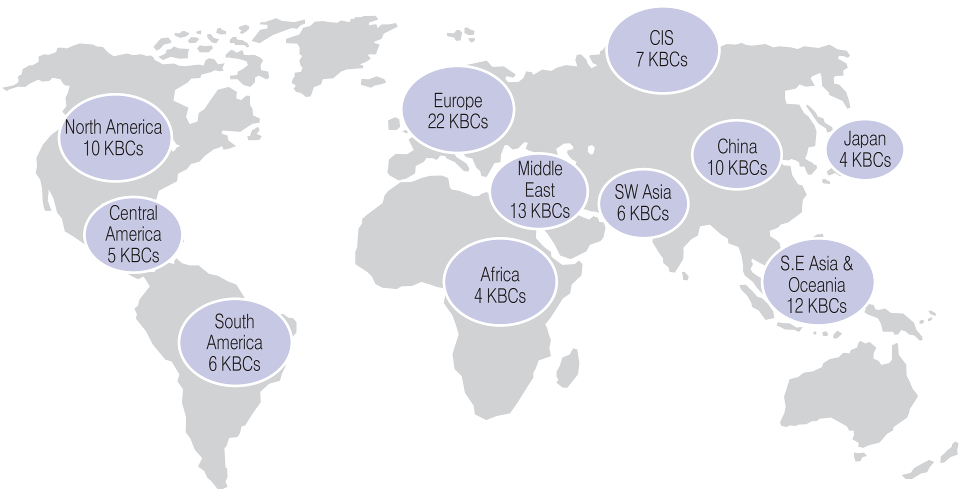


Table 3-2 | Expansion of KOTRA's Overseas Network

Year	1960s	1970s	1980s	1990s	2010
Number of overseas offices	4	40	78	81	99

Table 3-3 | Overseas Offices of KOTRA: Korea Business Center (KBC)

Region	Number of KBCs	Number of Employees	Region	Number of KBCs	Number of Employees
Europe	22	67	China	10	53
North America	10	45	Middle East	13	32
Central & South America	11	31	South-East Asia and Oceania	12	45
CIS	7	20	South-West Asia	6	16
Africa	4	9	Japan	4	26

2.2. Budget

KOTRA's annual budget, which stood at $354,000 in 1962, jumped to $5,965,000 ten years later. Now, its annual budget has risen to $289 million (as of 2010) as a result of the continued expansion of the organization and its functions.[7]

KOTRA's funding is mainly comprised of government subsidies and revenue earned from programs carried out in collaboration with local administrative units and other relevant institutions. The fees earned from businesses that use KOTRA's service account for less than 15% of total revenues. In terms of cost, the lion's share of expenditures is used to fund the operation of overseas network of offices, including employees dispatched to offices in foreign countries. It is noteworthy that the budget for the Shanghai Expo and the operation of KINTEX (Korea International Exhibition Center),[8] situated in Goyang, was separately set aside in the 2010 budget.

7. The annual budget is set in Korean won. Foreign exchange rate applied: US$1=130 won in 1962, 399 won in 1972, and 1,156 won in 2010.
8. KOTRA invested in KINTEX with budgetary support for expansion of the exhibition center from the Government. KOTRA indirectly takes part in the management of the exhibition center as a large shareholder, staying away from direct operation. Further information can be found at: http://www.kintex.com

Table 3-4 | Composition of KOTRA's Annual Budget for 2010

	Item	Amount [9](mil. USD)	Share (%)
Revenue	Ordinary subsidy from the National Treasury	159	55
	Special project subsidy	95	33
	Internal revenue	35	12
Total		**289**	**100**
Expenditure	Labor expenses	59	21
	Operational expenses of overseas network	52	18
	Project expenses	122	42
	Expenses for the Shanghai Expo	25	8
	Expenses for KINTEX operation	31	11

3. Business Spectrum of KOTRA

3.1. Introduction

South Korea's foreign trade is expected to surpass the $1 trillion mark in 2011. KOTRA is doing all it can to contribute as a body engaged in comprehensive economic promotion, including FDI, in step with the country's economic growth.

KOTRA carries out the following programs: surveys and the distribution of trade-related information; support of domestic businesses' overseas marketing campaigns and investment in foreign countries; and inducement of investment from world-famous businesses. KOTRA is also pushing ahead with strategic programs in high-tech sectors as part of the overall effort to secure new growth engines.

The KOTRA's vast network both in and out of the country enables it to carry out programs successfully. Information on hundreds of thousands of domestic exporters and foreign buyers gathered by KOTRA is stored in its Customer Relationship Management System. The database on customers is maintained with real-time input/output based on information gathered from

9. Foreign exchange rate applied: US$1=1,156 won

businesses both in Seoul and in foreign countries. KOTRA dedicates considerable effort to maintain solid collaborative relationships with relevant institutions, including the Ministry of Knowledge & Economy, which acts as the main supervisory institution over KOTRA's operation. KOTRA also carries out various programs in collaboration with government ministries, local administrative units, FDI-related public institutions, economic ministries of foreign governments, and international organizations, including the UN.

3.2. Collection and Distribution of Information of Trade/Investment

3.2.1. Methods of Collecting and Distributing Information

The most important function of a TPO is to collect and distribute information on overseas markets. KOTRA collects useful economic/trade/industrial information through its worldwide network and provides it to government institutions and businesses, which they use when setting up their export strategies. In the rapidly changing trade environment, including the signing of FTAs, KOTRA fulfills its role as a repository of information on overseas markets. KOTRA publishes booklets on market trends based on in-depth surveys of the export environment, holds seminars segmented according to regions and sectors, and updates the relevant information online.

KOTRA also publishes information booklets on the business situations of different countries, including their general state, local economic trends and investment environment. It also answers inquiries about the export/import of specific items, provides information on local buyers and conducts surveys on local market trends at the request of customers.

KOTRA distributes the information both on-line and off-line. Seeing an increase in the number of on-line customers, KOTRA provides ordinary information through its website, while operating a separate website that provides comprehensive information on specific areas. Its trade-related data office helps customers find in-depth information themselves.

3.2.2. Two Kinds of Information Services

The trade-related free information offered on KOTRA's homepages, i.e., Digital KOTRA and Global Window, include the following: brief, general information on foreign trade and investment; information on Korean businesses in foreign countries; country profiles; and information on exhibitions.

The overseas market survey is a typical consulting service that KOTRA provides on a fee-paid basis. At the request of customers (mostly exporters), KOTRA conducts a survey on market trends or looks for potential buyers. KOTRA posts such information (initially provided to customers on a fee-paid basis) on portal sites after a certain period of time has passed.

Table 3-5 | KOTRA's Overseas Market Survey Service

	2005	2006	2007	2008	2009
Number of cases of support provided	22,942	18,531	15,619	16,186	9,850
Number of companies using the service	4,283	4,006	3,338	3,217	2,517

Table 3-6 | KOTRA's Overseas Market Survey Service by Types

	2005	2006	2007	2008	2009
Survey for exploration of potential buyers	13,929	11,082	9,874	8,378	4,726
Customized market survey	8,027	6,385	5,038	5,980	3,314
Credit rating survey	758	661	450	717	762
Check of potential buyers	228	36	-	618	939
Total	22,942	18,531	15,619	16,186	9,850

3.2.3. Seminars and Forums

Prior to the widespread use of the Internet, KOTRA-held seminars constituted the only available means for domestic businesses to obtain information on overseas markets. The seminars still remain a crucial channel despite the emergence of the Internet and diverse media outlets in the 1990s and thereafter.

Every January, KOTRA holds a forum at which its analysis of the world market trends is presented.[10] Managerial-level participants from businesses engaged in trade-related activities in foreign countries present on the market trends about their respective countries. This event attracts more interest on the part of those concerned every year. KOTRA also holds seminars on the investment environment in foreign countries targeted by domestic businesses, as well as sessions on business issues and trends such as the protection of intellectual property rights or information on project biddings carried out by international organizations.

10. The forum is held every January in Seoul, attracting more than 600 participants as audience members.

Table 3-7 | Trade and Investment-related Seminars in November 2010

Date	Event	Contents
October 29	Online Distribution in North America and Eupore	-
November 2	Korea Private Equity & Venture Capital Fund	Inducement of FDI
November 8	Global Mobile Vision 2010	Recent trends in mobile technologies and products
November 23	How to invest in unexplored strategic markets	Presentation on the local markets of Mozambique, Papua New Guinea and Laos by Korean trader(s) based in those countries
November 26	Investment in Vietnam and China	-
November 29	Strategy for success in the Chinese market	Analysis of recent market trends in China, currently emerging as the world's No.1 economy

3.2.4. Publication of Materials

The publication of booklets may sound like a very outdated way of disseminating trade-related materials, but businesses still find them very useful. KOTRA provides a number of such booklets containing materials presented at seminars, reports on specific subjects, and introductions to the prevailing situation of foreign countries.

Most of these publications are sold at KOTRA's Trade Information Library, although some of them are available at bookstores.

Table 3-8 | KOTRA's Major Publications and Newly Published Books in 2010

Date	Material	Contents
Sold at KOTRA's Trade Information Library	Country facts (by country)	Recent information on trade, investment, business related to a specific country
	Korean business directory on those in foreign countries	List of Korean businesses by countries and regions
	Working-level guide to investment (by country)	Information on investment environments, incentives offered, and business operations in countries

Date	Material	Contents
Available at bookstores	For those on a business trip to a foreign country (by region)	A guide book for a business trip to a foreign country
	Cross market - 7 ways proposed by experts in 22 countries	Successful marketing strategies
	2010 Blu-sumer -12 golden markets that will dominate the future	Analysis of emerging markets
Free periodicals	Invest Korea Journal	PR of the economy, industry and culture of South Korea for the attraction of FDI
	Green Report	Information on the green movement, including green technologies, green policy trends, and updated news on the environment

3.3. Supporting Overseas Marketing of Korean Businesses

KOTRA conducts a range of activities designed to help domestic businesses with their overseas marketing efforts, such as sending market exploratory teams to foreign countries, organizing consultation meetings for domestic exporters, supporting overseas exhibitions, and so forth. Domestic businesses may also apply KOTRA's knowledge, which is based on the information collected in individual countries, to facilitate their employees' business trips to foreign countries.

Table 3-9 | KOTRA's Efforts on Supporting Overseas Marketing by Year

Supporting Activities		2005	2007	2009
KBCs serving as Branch Offices for SMEs	Number of relevant offices	1,636	1,671	2,070
	Amount of contracts signed (Million Dollars)	305	412	743
Dispatch of Trade Delegations	Number of times dispatched	265	156	212
	Number of participating businesses	2,419	1,940	2,243
Overseas sales visits	Number of visits	985	419	395
Overseas Market Survey	Number of surveys conducted	22,942	15,619	9,850
	Number of requesting businesses	4,286	3,217	2,517

Supporting Activities		2005	2007	2009
Response to Trade/Investment-related Inquiries	Number of cases of exploration	-	8,733	11,906
One-on-One Business Meetings with foreign buyers	Number of meetings	105	70	32
	Number of participating foreign buyers	2,495	1,599	3,489
	Number of participating domestic exporters	5,811	3,407	8,192
Overseas exhibitions	Number of exhibitions held	69	119	162
	Number of participating businesses	1,532	2,839	3,462

3.3.1. Responding to Business Inquiries on Trade and Investment

In the beginning, one of KOTRA's most important tasks was to search and deliver the inquiries on Korean-made products from foreign buyers to domestic exporters, and provide support to ensure successful transactions. Until the 1980s, the majority of small-sized domestic exporters could not afford to establish representative offices in foreign countries and channels of communication had not fully developed. Thus, KOTRA was an important source of trade inquiries, which became to be relied on heavily.

At present, KOTRA receives more than 10,000 trade inquiries per year. KOTRA makes it a rule to disclose the general information which it obtains in connection with such inquiries to the general public via its Internet potal sites and through emails, rather than giving out directly to export companies.

3.3.2. Dispatch of Trade Delegations

KOTRA has long regarded the responsibility of sending trade delegations to foreign countries to explore overseas markets as one of its crucial activities. Now, KOTRA dispatches trade delegations to more than 200 places around the world every year, where they conduct trade meetings with buyers. KOTRA's KBC also provide support for delegations dispatched by local administrative units and economic organizations.

Table 3-10 | Achievements of KOTRA Trade Missions by Regions

Region	2003	2005	2007	2008	2009
Europe	41	50	25	42	41
North America	18	29	23	26	25
Asia and Oceania	47	68	34	38	48
Japan	11	16	12	11	11
China	18	37	20	22	25
Latin America	20	25	17	19	21
Middle East /Africa	20	20	13	23	27
CIS	23	20	12	12	14
Total	**198**	**265**	**156**	**193**	**212**

3.3.3. KBCs Serving as Branch Offices for SMEs

In 1999, KOTRA's KBCs started to act as representative offices of small-sized domestic exporters on a fee-paid basis. KOTRA's one-on-one services for SMEs looking for overseas markets covered almost every steps of trade process; from market surveys, information on potential importers, and until support for trade contract. Once a deal has been accomplished, the relevant KBC continues to provide services free of cost to the business for six months, covering all matters included in the deal.

Each KBC hires local employees for this service, with each employee managing seven to eight businesses. There have been many successful cases so far.

Table 3-11 | Results of KBC Efforts to Support SMEs by Year

Year	Budget (in bil. KRW)	Number of customer businesses	Amount of deals (in mil. USD)	Number of employees dedicated to the service	Per-employee business
2000	3.8	543	50	62	8.7
2003	25.9	1,555	104	130	11.9
2006	39.4	1,609	352	169	9.5
2008	99.0	1,677	467	198	8.4
2009	139.0	2,070	743	275	7.5
2010	142.6	2,100	970	283	7.4

3.3.4. Operation of Logistics Centers

KOTRA-operated logistics centers go a long way in helping businesses enhance their competitiveness. The service helps Korean exporters reduce their logistical costs and makes it possible for buyers in each country to place small orders.

The first logistics center was opened in 2004 in Amsterdam, Netherlands, the largest port in Europe. At present, KOTRA operates 25 logistical centers in 25 cities around the world.

Figure 3-4 | Procedure for Establishment of a Logistics Center

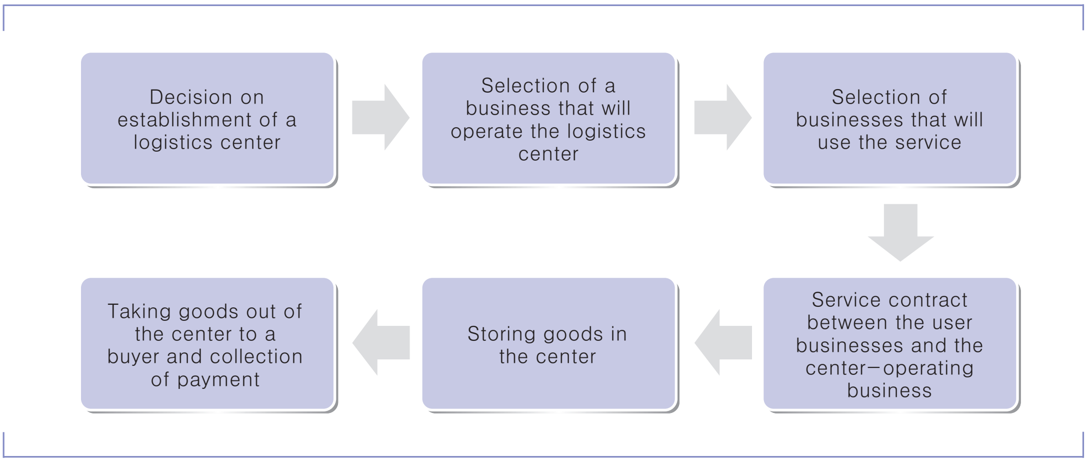


Table 3-12 | KOTRA Logistics Centers(in 25 Cities in 14 Countries)

Year	Number of User Businesses	Location of KOTRA Logistics Centers(City)	Total Number of Centers	Amount of Exports via the Centers (in mil. USD)
2004	11	Rotterdam	1	7.3
2005	33	New York, Toronto, Dubai and Qingdao	5	12.5
2006	70	Los Angeles, Panama, Budapest and Novosibirsk	9	24.5
2007	111	- Chicago, Detroit, Qingdao and Wuhan - The one in Dubai has been closed.	12	51.0
2008	141	London and Vladivostok	14	78.7
2009	308	- Antwerp, Singapore, Tokyo, Tianjin, Shanghai, Buenos Aires and Melbourne -The one in Budapest has been closed.	20	159.0
2010	320	Moscow, Ho Chi Minh, Guangzhou, Dalian and Frankfurt	25	170.0
Total		25 cities in 14 Countries	25 centers	

3.3.5. Supporting Business Trips to Foreign Countries

For business trips to foreign markets to gauge the investment environment, KBCs provide the following services on a fee-paid basis: arranging meetings and travel accommodations; arranging interpreters and transportation; visa applications, etc. The fee is charged on an as-incurred basis plus commission.

3.3.6. One-on-One Meetings with Foreign Buyers

KOTRA arranges one-on-one meetings for domestic exporters with foreign buyers interested in importing Korean-made goods. Leading examples include Buy Korea, a large-scale annual event started in 2009; Korea Auto Parts Plaza; Global Power Tech, which concerns power supply devices and materials; and Green Hub Korea, which is designed to help domestic businesses in the green industry, make forays into world markets.

Table 3-13 | Number of KOTRA-held Export Consultation Sessions

	2005	2006	2007	2008	2009	2010*
Number of sessions held	105	94	70	61	32	23
Number of participating Korean businesses	5,811	4,826	3,407	3,274	8,192	2,824
Number of participating foreign buyers	2,495	2,109	1,624	2,890	3,489	1,570

* September Year-To-Date for 2010.

Table 3-14 | Number of One-on-One Business Meetings Organized by KOTRA

	2005	2006	2007	2008	2009	2010*
Machines and industrial plants	19	14	11	10	3	2
Auto parts	12	10	5	5	2	2
Textiles	5	9	3	4	2	1
Medical supplies	1	5	6	4	2	1
Electro-electric	5	6	4	-	4	0
Information technology	9	15	12	9	6	4
Combined items	31	22	10	7	3	7
Green industry	23	13	19	24	10	6
Total	**105**	**94**	**70**	**63**	**32**	**23**

* September Year-To-Date for 2010.

3.3.7. E-trade Overseas Marketing Service

With its e-Trade overseas marketing service, KOTRA helps businesses facilitate their foreign trade transactions (i.e. business meetings, orders, contracts, payment and shipping) safely online, including online trade meetings. In particular, the KOTRA Online Payment Service (KOPS) makes it possible for domestic exporters to receive payment for samples or small orders via the foreign importer's credit card instead of the usual Telegraphic Transfer (T/T), thus facilitating transactions safely and conveniently.

3.3.8. Organizing Trade Fairs and Exhibitions

In 1963, KOTRA took over responsibility of organizing trade exhibitions from the Ministry of Foreign Affairs. It has since carried it out proactively. In 2009 alone, KOTRA took part in more than 150 international trade exhibitions through the Korean pavilion.

In addition, KOTRA holds trade exhibitions exclusively for Korean goods in major trading partner countries. In 2009, KOTRA held the World Class Korean Product Show seven times in major world cities, including Bangkok and Beijing. In May 2010, KOTRA held the show in Moscow, Russia in cooperation with more than 100 Korean businesses.

Table 3-15 | Overseas Exhibitions Held by KOTRA

	2008년	2009년
Provision of support from the National Treasury (in bil. KRW)	107	220
Number of exhibitions held	117	150
Number of participating businesses	2,263	2,645

Table 3-16 | Results of 2009 World Class Korean Product Show

	Number of participating businesses	Number of visiting foreign buyers	Number of business consultations
Bangkok	64	2,288	1,417
Beijing	112	2,977	1,612
Warsaw	55	764	1,089
Chicago	72	693	1,296
Birmingham	20	3,100	917
Qingdao	76	1,525	1,525
Mexico City	80	1,116	1,443
Total	**479**	**12,463**	**9,299**

3.3.9. Participation in the World EXPO

KOTRA took over the responsibility of managing Korea's World Expos from the government and has taken part in all of them since the one held in New York in 1964, including the one held recently in Shanghai.[11]

Expos serve as an important opportunity to enhance country's brand value and export goods, in addition to promoting trade by leaving a strong impression on visitors. KOTRA's experience of participating in trade exhibitions and the know-how in foreign trade it has accumulated over a long period of time are critical in its management of Korea's expos in a more efficient and systematic manner.

3.3.10. Hosting Trade Fairs and Exhibitions in Korea

In 1968, KOTRA hosted the Korea Trade Fair, the country's first modern expo. In 1982, it held the Seoul International Trade Fair (SITRA).[12] Now, only SEOUL FOOD, an annual international food industry exhibition, is still hosted by KOTRA, as most of the other domestic trade exhibitions have been handed over to associations in individual industrial sectors. KOTRA now concentrates on attracting foreign buyers to the exhibitions held by the domestic industry organizations.

In the 2000s, many international exhibition centers were opened in large cities across the country, including KINTEX (opened in 2005) in Goyang near Seoul. KOTRA provides support for hundreds of exhibitions held annually in KINTEX, the largest exhibition center in the country.

11. In 2010, the World Expo was held in Shanghai - an economic hub of China, a country which has transformed itself from the world's factory into the world's market - between May 1 and October 31. The Korean pavilion was built using shapes modeled on the letters of the Korean alphabet. It won a favorable reception from Expo visitors for being "very creative." The Korean pavilion became the focus of attention, attracting an average of 39,000 visitors a day. More than 7.2 million people visited it, waiting in line an average of 5 hours for admission.
12. SITRA was held for the last time in 1994 and has not been held since then.

Table 3-17 | Major International Trade Exhibition Centers in Korea

Exhibition centers	Total floor space(㎡)	Year of Opening	Number of exhibitions held in 2009	Running agency
KINTEX	53,976	2005	49	KOTRA and the Gyeonggi-do Office
COEX	36,027	2000	134	KITA
BEXCO	26,508	2001	48	The City of Busan and KOTRA
EXCO	11,616	2001	33	The City of Daegu
SETEC	7,948	1999	42	The City of Seoul
Kim Dae Jung Convention Center	9,072	2005	28	The City of Gwangju
KOTREX	4,200	1995	13	KOTRA

Source: research by KOTRA.

3.4. FDI Attraction

3.4.1. Background

When its name was changed from the Korea Trade Promotion Corporation to the Korea Trade-Investment Promotion Agency in 1995, the importance of inducing foreign direct investment (FDI) was not emphasized as strongly as it is now. However, this changed abruptly with the foreign exchange crisis that hit the country in 1997. The South Korean government sought to expand FDI as one of its crucial economic policies. The Foreign Investment Promotion Act, enacted in September 1998, put the Korea Investment Service Center (KISC) under KOTRA and designated KOTRA as an institution in charge of FDI inducement.

In 2003, KOTRA changed KISC's name to Invest Korea, and significantly expanded the organization and refocused it to FDI. The designation of Allan Timblick, a British citizen, as the first CEO of Invest Korea was an exceptional step taken to win over foreign investors. At present, officials dispatched from the central government, local administrative units and the relevant public institutions are working along with KOTRA employees at Invest Korea to provide a one-stop service to foreign investors.

Invest Korea fulfills its roles as a body dedicated to inducing FDI, attracting more than 60% of the entire FDI amount.

3.4.2. Invest Korea - Its Organization and Facilities

Unlike the other internal organizations of KOTRA, the employees of Invest Korea KOTRA consist of officials dispatched from the central government, local administrative units and relevant public institutions as well as experts from the private sector, all of whom work together to help maximize the value of the one-stop service to foreign investors. Invest Korea offers a menu of services to foreign investors including investment/tax-related consulting, FDI report, visa extension, and so forth. In an effort to maintain a favorable atmosphere for foreign investors, KOTRA took the extraordinary step of appointing a British citizen and a Korean-American as the first and second CEOs of Invest Korea, respectively.

Invest Korea has also adopted an ombudsman system to help foreign investors with their management-related problems. The ombudsman, directly appointed by the President, concurrently serves as the co-chairman of the Regulatory Reform Committee, which produces synergistic effects, as the problems experienced by foreign investors can be submitted to the committee for its deliberation.

KOTRA also provides foreign investors with office spaces at reasonable rates in the early stages of their operation in the country following submittal of the FDI report. Such office spaces (40 rooms) are available at the Invest Korea Plaza (IKP), situated next to KOTRA's Headquarters, along with round-the-clock video conferencing facilities and English-speaking secretaries.

Table 3-18 | Invest Korea - Major Functions

Teams	Major assignments
Investment Planning Team	- Establishes strategies and plans for inducing FDI; handles general business of Invest Korea
Investment PR Team	- Promotes the advantages of investing in Korea - Produces PR materials on Korea's business environment
Investment Information Team	- Compiles FDI statistics, and manages and analyses them - Maintains a database of foreign-invested businesses - Analyzes the effects of FDI policies and conducts research on improvement methods
Main Industry Investment Promotion Team	- Responsible for FDI in main industries and the parts/materials sector
Service Industry Investment Promotion Team	- Responsible for FDI in the service sector, such as logistics and distributions, the social overhead capital sector, and the alternative energy sector - Responsible for FDI concerning the country's objective of becoming a financial hub in Northeast Asia

Teams	Major assignments
Hi-tech Industry Investment Promotion Team	- Responsible for FDI in new industries, such as IT (information technology) and BT (biotechnology), and R&D centers
Financial Industry Investment Promotion Team	- Responsible for FDI in domestically available financial products
Investment Administration Team	- Manages the investment-related approvals and authorization procedure on behalf of foreign investors; receives investment reports
Investment Consulting Center	- Investment consulting provided by the industrial sector (e.g. manufacturing, finance, tourism, leisure, etc) and by requirement (e.g. accounting, tax, legal matters, etc.) - Provides education, advice and consulting designed to enhance the expertise of the employees of FDI-related institutions, organizations and businesses
Investment Service Team	- Implements improvements of the investment service - Operates the Invest Korea Plaza (IKP)
Investment Aftercare Team	- Works on improving the experience of foreign investors

3.4.3. Economic Ripple Effects of FDI

FDI has wide ranging ripple effects, bringing positive growth in the country's industry and society. Examples of FDI's positive ripple effects include: increased investment in production facilities and the creation of jobs; increase in effective demand and exports; transfer of high-end technologies from more advanced countries; and promotion of industrial clusters; improvement of corporate structures through increased effective competition; and positive effect on management conditions. Business watchers say that KOTRA has gone a long way towards creating such ripple effects through its proactive efforts to attract FDI.

Table 3-19 | FDI Reports KOTRA's Contribution

(Unit: in mil. USD)

	1998	1999	2000	2001	2005	2008	2009
KOTRA's contribution	2,170	5,251	5,411	6,419	5,009	4,929	7,489
FDI report	8,852	15,541	15,690	11,870	11,566	11,704	11,483
KOTRA's contribution	24.5%	33.8%	34.5%	53.7%	43.3%	42.1%	65.2%

3.5. Supporting the Foreign Investment Activities of Korean Businesses

3.5.1. Background

Korean businesses started investing in foreign countries in the 1980s. In the beginning, their investment was mostly concentrated in Southeast Asia, including Indonesia and some industrialized countries (e.g. the U.S. and the U.K.). In the 1990s, they started expanding the scope of their overseas investment even to China and CIS countries. The country's foreign exchange crisis in 1997 led domestic businesses to downsize activities, along with an overseas investment funds crunch.

In 1995, the organization's name was changed from the Korea Trade Promotion Corporation to the Korea Trade-Investment Promotion Agency in light of its additional functions, namely inducing FDI and promoting collaboration in the industrial/technology sector. Korean businesses found it inevitable to make overseas investment to enhance their international competitiveness, amid the deepening of technology protectionism on the part of industrialized countries and the growing trend towards a more globalized economy and the consequent blurring of national borders. However, there was a limit to what the government could do to encourage overseas investment at the time due to criticisms over the possibility of Korea's industries being hollowed-out.

As it happened, the country's foreign exchange situation improved in the 2000s and China emerged as a very attractive investment target. Domestic businesses pushed forward with their investment in foreign countries, including China. The demand for KOTRA's support service concerning forays into foreign countries increased. In 2006, the South Korean government announced a policy aimed at encouraging overseas investments by Korean businesses, thereby lending additional strength to KOTRA's programs. In 2009, KOTRA was officially assigned the duty of providing support to domestic businesses engaged in overseas investment with the enactment of the Act on Formation of the Basis for Foreign Trade Transactions.

3.5.2. Support Centers for Overseas Investment

KOTRA's provision of support to domestic businesses engaged in overseas investment starts with the collection of information. KOTRA collects information on the investment environment of each country on behalf of interested businesses through its worldwide network. It also provides a consulting service to businesses interested in overseas investment. Korean businesses in foreign countries can obtain support for their business operations from the Korean Business Support Centers at 13 KBCs.

Table 3-20 | Korean Business Support Centers

Country	Cities
India	New Delhi
Philippines	Manila
Indonesia	Jakarta
Cambodia	Phnom Penh
Vietnam	Ho Chi Minh and Hanoi
Russia	Moscow
China	Beijing, Shanghai, Qingdao, Guangzhou and Dalian
Poland	Warsaw

3.5.3. KOTRA's Supporting Activities

KOTRA supports overseas investment efforts of Korean businesses in diverse ways, primarily by 1) drafting in-depth reports on areas in which Korean businesses are interested; 2) arranging business meetings with local businesses and making accommodation arrangements for employees of Korean companies; 3) organizing seminars on investment environments and procedures for businesses seeking to make a foray into a local market; 4) presenting successful case studies in cooperation with Korean businesses that have an established foothold in foreign countries; and 5) sending business delegations to observe industrial parks and the operation of Korean businesses in foreign countries.

In regards to securing overseas contracts, KOTRA helps Korean businesses by conducting a first-hand check of the site, arranging meetings with the client, collecting information on the relevant local businesses and the local bidding system as well as making follow-ups for on their behalf. Also, promoting the protection of intellectual property rights of Korean businesses in foreign countries is also one of KOTRA's activities. Indeed, KOTRA's IP-China offices in Beijing, Shanghai, Qingdao and Guangzhou carry out activities related to protecting intellectual property rights.

As seen in the Table 3-21 below, the Overseas Premium Service (OPS) is a premium customized service provided by KOTRA for businesses engaged in overseas investment. Many businesses have spoken highly of the service, which is provided to meet customers' specific requirements, including winning large-scale contracts, establishing local corporations and factories, general consulting on overseas investment and franchise business opportunities, etc.

Table 3-21 | KOTRA's Premium Service for Overseas Investment

Type of service provided	Details of service
Support for securing large-scale overseas projects	- Provision of information on potential projects and the project owner on the construction/supply of industrial plants and resource development, and local agents and bidding system; arrangement of meetings with prospective clients; provision of information on local agents and bidding system; and making follow-ups on behalf of customers. - Provision of project-related support, such as following the prequalification procedure, drawing up bidding documents, etc.
Support for establishment of local corporations	- (In the case of establishment of a local sales corporation): introduction to the procedure for local investment; application for approval of investment; information on proper locations; on-the-spot check of sites; information on living environment for employees working overseas, etc. - (In the case of establishment of a local factory): information on available sites; customs/logistics-related information; land use/building permits, etc.
General consulting on overseas investment	- In-depth feasibility survey concerning investment/business environment and candidate sites.
Support for franchise business opportunities	- Basic survey concerning investment/business environment and candidate sites. - Provision of support for participation in the relevant events, such as franchise expos.
Fostering businesses taking in part in the U.S. government's procurement programs	- Establishment of a strategy for individual participation; appraisal of marketability; search for prime vendors and clients; preparation of the bidding document and hosting of relevant seminars.

3.5.4. Overseas Investment Information System

KOTRA's integrated IT system helps businesses interested in making forays into foreign countries. For example, its Overseas Investment Information System (OIS) provides information on overseas investment opportunities offered by total of 31 government ministries, institutions and organizations.

Businesses can seek updated news/information on overseas investment, a list of Korean businesses in a given country, overseas investment-related statistics, expert opinions and other relevant data via the portal site operated by the system. KOTRA's experts also provide consulting on tax or legal related matters of specific countries.

Figure 3-5 | KOTRA's Overseas Investment Information System (OIS)

Source: http://www. ois.go.kr.

3.6. Strategic Projects in Search for New Growth Engines

3.6.1. Background

KOTRA has continued to expand the scope of activities in supporting the overseas marketing efforts of businesses in industries such as computer games and software. It also supports businesses' efforts to secure construction projects and supply industrial plants as well as ordinary commodities. KOTRA strives to help businesses by dispatching trade delegations, organizing and coordinating overseas exhibitions, and holding export consulting sessions; and by designating new growth strategic sectors that are expected to create high added value, such as cultural content, medical supplies, green industries, and the government procurement market.

Other programs provided by KOTRA include Contact Korea, which helps domestic businesses find talented professionals, and the national brand PR program, as well as providing support for the South Korean government's Official Development Assistance (ODA) program (starting 2011).

3.6.2. Promotion of Strategic Programs

3.6.2.1. Globalization of Knowledge-based Service Industry

Korea's economic policy used to be focused on manufacturing. Now, in contrast, KOTRA has been playing a leading role in promoting the government's policy of encouraging the service industry to make forays into world markets in connection with the need to create more jobs and enhance domestic businesses' competitiveness. Thus, KOTRA provides support to the cultural content, franchise, and e-Learning industries to make forays into foreign countries, thus contributing to the growth of Korea's knowledge-based service industry throughout the world.

3.6.2.2. Entering into International Procurement Markets

KOTRA, jointly with international organizations, holds regular seminars on the overseas procurement market in an effort to help Korean businesses take part in the bidding of procurement contracts for commodities and services held by international organizations, including the UN, or foreign governments. At present, such activities are confined to the supply of goods, but will be expanded to other areas, including large-scale construction projects.

3.6.2.3. Promotion of the Medical/Bio Industry

Following the South Korean government's policy of upgrading the medical industry in 1995, KOTRA launched the Support Center for Overseas Marketing for the Medical Industry. Among its various activities, the center hosts medical industry international conferences, conducts marketing campaigns aimed at attracting foreign patients to Korea, and dispatches trade delegations to foreign countries to explore world pharmaceutical markets.

3.6.2.4. Overseas Investment of Domestic Green Industries

In step with the South Korean government's adoption of the low-carbon green growth policy in 2008, KOTRA helps domestic green businesses specializing in development of new/renewable energy, more efficient and clean ways to use energy, and environmental products, to make forays into foreign countries. KOTRA also assists in the introduction of new cutting-edge green technologies in Korea and invites foreign institutions involved in green projects or foreign buyers to Korea or dispatches domestic trade delegations to foreign countries in an effort to secure overseas business. KOTRA tackles environmental issues like climate change directly by having KBCs explore promising projects and present their findings to domestic businesses.

3.6.2.5. Promotion of Information and Communication Technology (ICT)

KOTRA holds exhibitions and consulting sessions in major export markets, which offer Korean businesses that have sophisticated ICT technologies but little experience in foreign markets, great opportunities to introduce their export products. In 2010, KOTRA's efforts led to business discussions worth about $380 million in terms of the value of goods.

Table 3-22 | Performance Results of KOTRA's ICT Road Shows in 2010

Country (City)	Number of participating businesses	Outcome of discussions in monetary value (in mil. USD)
EU (Frankfurt)	38 Korean + 148 foreign businesses	25.5
Japan	50 Korean + 636 foreign businesses	61.1
Latin America (Mexico City)	34 Korean + 182 foreign businesses	148.1
China (Shanghai)	45 Korean + 630 foreign businesses	153.8

3.6.2.6. KOTRA's Seal of Approval

For Korean exporting businesses that possess high-end technologies but experience difficulties due to a low level of recognition, KOTRA provides the "KOTRA Seal of Excellence," which is a seal of approval of a Korean business's financial soundness, competitiveness and product's quality. Such an assurance is expected to increase the country's exports and help domestic businesses enjoy an advantageous position in terms of price negotiations.

3.6.2.7. Attraction of Talented Foreigners

KOTRA's Contact Korea is a program designed to help domestic SMEs, research institutes, and government institutions to recruit talented workers from abroad. Its portal site (www.contactkorea.go.kr) provides the following services: information on talented foreign workers collected by KBCs; verification of their academic background and experience; and online video interviews.

3.6.2.8. Activities in International Development Cooperation

As Korea's international aid activities is expected to expand with its accession to the OECD

DAC (Development Assistance Committee) in 2009, KOTRA will step up its activities related to Official Development Assistance (ODA) and put more emphasis on Public-Private Partnership (PPP) programs, starting in 2011. So far, its activities have been confined to the KDI-sponsored Knowledge Sharing Programs (KSP).

4. KOTRA's Management

4.1. Independent Operation and Members' Expertise

KOTRA has carried out its assignments successfully due to its status as a corporation whose independence is ensured by law. KOTRA consults with the Ministry of Knowledge and Economy (MKE), its supervisory institution, in carrying out the government's economic policies. However, KOTRA is allowed to make important decisions on its own in principle.

The appointment of KOTRA's CEO is made through open competition, and seeks candidates with a background in trade and investment, with final approval from the Korean President. During the 3-year tenure, which is guaranteed under the law, the KOTRA CEO can carry out creative management based on his/her expertise. The agency enjoys the great advantage of being able to recruit talented people as required annually. KOTRA employees have to follow a program that requires them to build their proficiency in a second foreign language in addition to English, attend diverse training courses on trade and investment, and accumulate experience in overseas markets, all of which is designed to transform them into experts in the economies of foreign countries.

KOTRA employees are required to build their competence and dedication in the following areas:

1) Proficiency in English and a second foreign language[13]
2) Knowledge about the international economy and business management
3) Professional knowledge about foreign trade transactions and overseas investment
4) Professional knowledge about working-level trade promotional events, such as exhibitions
5) Ability to utilize the information system

13. Major foreign languages spoken by KOTRA employees include: Chinese, Japanese, Russian, Spanish, French, German, Arabic, Italian, and Portuguese.

Table 3-23 | KOTRA's Employees by Specialties

Major	Bachelor's degree	Master's degree	Ph.D.
Economics	42	17	5
Business administration (including international trade)	72	154	6
Law (including public administration)	26	8	5
Information/computer (IT)	12	4	1
Other science/engineering majors	70	45	2
Foreign languages	129	18	-
Total	**351**	**246**	**19**

4.2. Evaluation System

4.2.1. External Management Evaluation

All the public institutions of South Korea are required to have their annual management results evaluated by a group of experts with focus on whether they have met the management target for the year and whether they have carried out their assignments efficiently. KOTRA's performance ranking among all the other public institutions is announced to the public. Details of the evaluation are disclosed in an evaluation report and interviews submitted by KOTRA. KOTRA's CEO and members strive to achieve the management target set at the beginning of each year. The higher the score they are given in the management evaluation, the wider the range of incentives offered to them.

4.2.2. Internal Evaluation

KOTRA employees also have their performance results evaluated under the internal evaluation system, which is designed to encourage them to compete with each other constructively and to carry out their assignments successfully. The most important evaluation index is the customer satisfaction evaluation. The degree of satisfaction felt by businesses, public officials and individuals who use KOTRA's service is translated into a score and reflected in the evaluation of the relevant teams.

4.3. Customer Management

KOTRA's customers include domestic and foreign businesses, the central government, local administrative units and public institutions. KOTRA does everything in its power to ensure the complete satisfaction of customers. It has adopted the Customer Service Charter and encourages employees to develop a service-minded attitude, which includes receiving incoming phone calls in a polite and pleasant manner. In addition, KOTRA has a professional survey institution conduct a survey on customer satisfaction, targeting customers who have used KOTRA's service for many years.

Table 3-24 | Customer's Satisfaction Rating of KOTRA's Service

	2005	2006	2007	2008	2009
Customers' satisfaction	85.0	84.0	86.5	83.0	93.9

*on the basis of 100 points

Figure 3-6 | KOTRA's Customer Service Charter

We shall provide our customers with a world-class trade/investment service, attain sustainable growth, contribute to the development of the national economy, and do our best to help the country join the ranks of the first-rate countries through the following:
- We shall do what we can to provide a service that gives our customers ultimate satisfaction.
- We shall remember that time is a matter of essence in the provision of a service.
- We shall ensure that our customers always receive the most up-to-date information.
- We shall regard our customers' success as our highest value.
- We shall be an organization that faithfully carries out social contribution activities.
- We shall immediately take steps to remedy any inconvenience or dissatisfaction caused by erroneous service on our part and make up for any damages and/or losses caused by it.

4.4. Management Information System(MIS)

4.4.1. Internal Information/Communication System

KOTRA employees at the headquarters and at KBCs stay connected, exchange information and views with each other, using WINK, an intranet system.[14] The system enables employees to draw up documents, obtain approvals from their supervisors, send and receive e-mails, carry out customer relationship management (CRM), accounting management, personnel management,

14. The WINK system, opened in 1999 as the first system to be adopted by a domestic public institution, made it possible for KOTRA's employees to obtain approvals from their supervisors online and carry out electronic accounting, thereby contributing to the establishment of a "Paperless KOTRA."

education/training sessions, and information technology-related operation, and share knowledge with each other.

Figure 3-7 | KOTRA's Intranet, WINK

Table 3-25 | KOTRA's WINK-supported Internal Information Systems

Name of system	Service content
Budget management system	Preparation, allocation and management of the agency's entire budget
Accounting management system	Management of expenses and revenues of the entire organization which links KOTRA with financial institutions in Korea
Operational control system	Management of the annual goals and performance results of the entire organization
Personnel management system	Management of regular employees' personnel information, including their background and holiday entitlement
Wage management system	Management of monthly wages of employees in Korea and automatic processing of payroll through financial institutions
Nemo system	System for managing office spaces, assets, and local employees(including their housing and welfare) for network of 99 overseas offices
Knowledge management	A program designed to help employees share any knowledge they acquire in the process of handling their assignments

Name of system	Service content
Suggestion management	A program that helps employees submit constructive and creative suggestions to improve existing work processes and procedures
Project management	Management of construction, supply of industrial plant, ODA/CDM, ICT projects which Korean businesses can carry out in foreign countries
In-house cyber training center	Online tool for education and training of employees
Book summary service	Provides information on newly published books and other publications related to the agency's business
Video phone	Online video conferencing
Remote support	Remote IT Support
Community	Provision of support for in-house club activities
Download Center	Center helps users to download useful software
Help Desk	IT support

4.4.2. Customer Service Website

It is difficult to expect KOTRA to carry out its business successfully without the support of an efficient information system, as its operations are based on a vast network. KOTRA operates a total of nine portal sites, in addition to a website for each KBC, to provide its service promptly to customers.

Figure 3-8 | KOTRA's Main Homepage

Table 3-26 | KOTRA's Major Portal Sites

System	URL & Service provided	Year of opening	Daily visitors
Digital KOTRA	www.kotra.or.kr - KOTRA's main homepage	1997	10,300
Buy KOREA	www.buykorea.or.org - Trade-related inquiry service	2004	7,157
Global Window	www.globalwindow.org - A trade/investment information portal that provides information on the general status of a country, goods,trade, and overseas investment.	2006	5,845
Global Exhibition Portal (GEP)	www.gep.or.kr - Processing exhibition-related information and business	2004	3,473
Overseas Investment Support (OIS)	www.ois.go.kr - Information on overseas investment and relevant businesses	2007	347
Invest KOREA	www.investkorea.org - Website dedicated to FDI related information including information on the investment environment and promising industries, online investment consulting, an investor's guide, business management, and everyday life in Korea.	1999	338
KOTRA Academy	www.kotraacademy.com - Portal for online education and training, which can introduce courses and accept online applications for the course.	2004	118
Contact KOREA	www.contactkorea.go.kr - A portal for recruiting professionals from abroad	2008	117
KOBIO	www.kobio.org - A portal that supports the overseas marketing efforts of the medical industry	2008	54
Invest Korea Plaza	www.ikp.or.kr - An investment incubation center	-	-
Ombudsman	www.i-ombudsman.or.kr - Foreign investment ombudsman	-	-
KOPS	kops.buykorea.org - A system for credit-based payment of exports	-	-

5. Evaluation

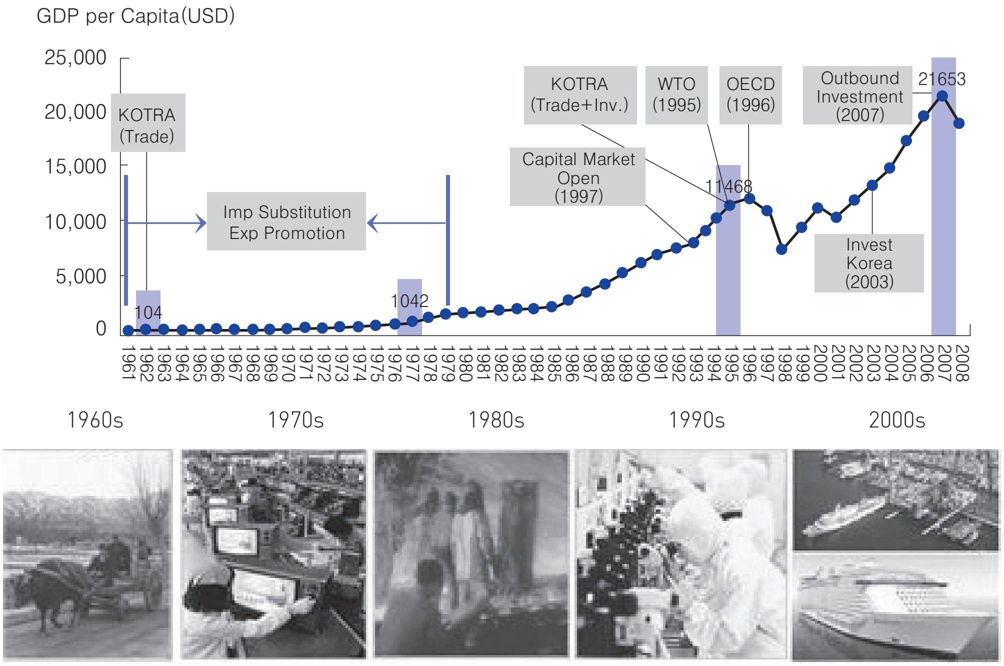
5.1. Performance Results

KOTRA has contributed to the country's economic growth during a period in which Korea has enjoyed phenomenal growth, rising from one of the poorest to one of the richest (13th in terms of GDP) countries in the world.

KOTRA's export promotion activities helped the country escape poverty in the 1960s, just a few years after the Korean War, and ultimately join the ranks of the wealthiest countries of the world. KOTRA has helped the country's exporters by collecting information on the markets of major industrialized countries, finding buyers for Korean-made goods, and providing multi-directional support for export deals with foreign buyers. No one would dispute the fact that KOTRA with the support from a number of Korean corporations has played a decisive role in the growth of the country's export volume from a mere US $55 million in 1962 to US $100 million in 1964, US $1 billion in 1970, US $10 billion in 1977, and US $423.4 billion in 2010 (as of the end of November).

Figure 3-9 | South Korea's Economic Growth and the Role of KOTRA

(Unit: GDP per capita(USD))



Source: World Bank, World Development Indicators, www.worldbank.org.

KOTRA's very successful activities have been recognized worldwide. The International Trade Center (ITC), an affiliate body of GATT/UNCTAD, presented KOTRA as a success model for developing countries engaged in export promotion in 1970. Hakan Hedberg, a renowned Swedish journalist, spoke highly of KOTRA's efficient operation, comparing it favorably with its Japanese counterpart JETRO. KOTRA has taken it upon itself to explore markets around the world and present findings and recommendations to the country's exporters. It is noteworthy that such an effort bore fruit with the opening of the country's trade centers in what used to be socialist countries even prior to the establishment of diplomatic relations.

Table 3-27 | South Korea's Major Export Items(based on Export Amount)

Year	Major export items
1960s	Bamboo handicrafts, cotton cloth, dried laver, salted Pollack roe
1970s	Textiles, cement, iron/steel, electronic goods, military equipment
1980s	Cars, ships, TVs, train carriages, steel shipping containers
1990s	Semiconductors, ships, petrochemical goods, cars, fiber optical goods
2000s	Semiconductors, textiles, computers, cars, cellular phones, petrochemical goods
2010s	Semiconductors, ships, machinery, petrochemical goods, cars, cellular phones

Within little more than ten years of its designation as an agency dedicated to the attraction of FDI, KOTRA's role has become so crucial that it is responsible for attracting more than half of the country's entire FDI amount. KOTRA has newly assumed the role of inducing FDI in connection with the need to upgrade the country's economic system, keeping in mind that it is difficult for a country to achieve rapid economic growth through export promotion once it reaches a certain level.

KOTRA's proactive activities in inducing FDI have gone a long way towards building and strengthening the country's economic structure as a result of bringing about positive effects in terms of production factors and market demands, development of the relevant industries, and improvement of management conditions.

At present, KOTRA's four strategic objectives consist of helping the country's businesses to occupy markets ahead of the competition; achieving substantial performance results; maintaining win-win relationships with customers; and reinforcing the agency's competitiveness. Based on these objectives, KOTRA aims to continue growing, while bringing in changes where necessary. In doing so, it will focus on the following: supporting the development of new industrial sectors, such as knowledge-based services, the green industry, and the medical/bio industry; exploring promising construction projects in foreign countries; expanding the scope of activities in the information procurement market; and large-scale projects with high added value, such as ODA projects.

Table 3-28 | KOTRA's Performance Results over the Past 5 Years

Type of service provided	Major content
Contribution to the country's export and FDI attraction	• Assisting SMEs' efforts to find more export opportunities • Entrance into four major markets (i.e. China, the public sector procurement market, the service industry and the parts/materials market) ahead of the competition • Establishing a comprehensive support system via the addition of new functions • Enhancing the national economy by inducing investment • Strengthening its monitoring of changes in the world market • Enhancing Korea's brand as a global leader in the new G-20 era
Enhancement of customer satisfaction	• Standardization of service through customer management system (CRM) and ISO 9001 certification • Analysis of customer needs and voice of customers (VOC) • Operation of a customer service organization that puts emphasis on where actions are carried out
Efficient operation	• Enhancement of the efficiency of team-based operation • Enhancement of financial stability and productivity • Adoption of the best evaluation/personnel affairs system among public institutions
Enhancement of influence in the international community	• (Aiming for) recognition by the WTO and the World Association of Investment Promotion Agencies (WAIPA) • A number of cases indicate that KOTRA has become a benchmark for its counterparts in such countries as Japan, Indonesia and Iran.

5.2. KOTRA's Success Factors

5.2.1. KOTRA's Core Competitiveness

KOTRA's core competitiveness lies in the gathering of trade/investment-related information through its vast worldwide network. KOTRA distributes it after processing it in a user-friendly format. As such, KOTRA employees must be able to identify useful information and process it for customers, in addition to cultivating a mindset that enables them to adapt to changes in connection with their duty to explore markets and provide support for trade/investment.

KOTRA stresses the ability for their employees, above all else, to make an accurate assessment of the market. Such a talent should be accompanied by the ability to gain access to reliable information sources and to conduct comparative analyses and surveys. KOTRA employees should also have the perspicacity with which to distinguish reliable information from that which is not. They should also be able to compare and analyze the information collected from different sources and process it into eminently useful information.

The main duty of KBC employees in foreign countries is to provide support to businesses in Korea and the foreign countries in which they operate to facilitate trade transactions between them. KBC employees need to be well-versed about the local trade/investment policies and Korea's business environment as well as its trading partners to be of service to foreign businesses seeking to trade with and invest in Korea.

5.2.2. KOTRA's Success Factors

5.2.2.1. Efficient and Well-knit Operational System

KOTRA has built an operational system that provides support in a way that helps the headquarters in Seoul and the 99 KBCs in 72 countries to work as one. In addition, each of the following factors has proved indispensable in helping KOTRA carry out its activities successfully: KOTRA's status as an independent agency guaranteed under the law; establishment of a clear-cut objective, namely that of developing the national economy through trade promotion and investment attraction; discretion to hire talented people; establishment of the internal information/communication network WINK; strong leadership on the part of the management; setting of proper indices for the evaluation of results; performance-based compensation; and customer management.

5.2.2.2. Operation of Overseas Network

The basic role of a TPO is to evaluate the overseas market conditions and export market trends and to identify potential foreign buyers. KOTRA's KBCs provide businesses looking for opportunities for export and investment with reliable, up-to-date information by producing real-time reports on the market situation and publishing in-depth reports. The KOTRA's worldwide network is valuable in organizing exhibitions and consultation meetings either in Korea or in foreign countries, and dispatching trade delegations to foreign countries.

5.2.2.3. Commitment to Provision of a Good-quality Service to Customers

Most importantly, the customer's views and needs are reflected in KOTRA's operation. Customer evaluations are used to benchmark relevant teams, and to incentivize employees based on a performance-based compensation scheme. Thus, the following virtuous cycle is formed: Customer-centered operation → Continued improvement of service quality → Higher score in customer satisfaction evaluation → Higher score in team evaluation → Incentive compensation → Higher degree of satisfaction on the part of employees → Customer-centered operation.

5.2.2.4. Good-quality Employees

A TPO is supposed to carry out service activities, leveraging KOTRA's knowledge and expertise as well as worldwide network. In this respect, it is distinguishable from other state-run corporations, such as KEPCO (Korea Electric Power Corporation) or KOGAS (Korea Gas Corporation) or KNOC (Korea National Oil Corporation), which operate vast tangible assets for the supply of power, gas or oil to the people. Thus, a TPO should be a well-knit and highly professional organization, which in turn means that the professional candidates who are hired to fill these positions must be subject to highly stringent requirements. KOTRA employees are required to attend an array of educational sessions designed to train them as trade/investment experts considering the need to promptly address changes in the business environment by securing new growth engines.

5.2.2.5. Partnerships

KOTRA carries out its programs jointly with the MKE, its supervisory institution, and other relevant government ministries. Promotion of its programs requires close partnerships with local administrative units and public institutions. KOTRA's worldwide network includes the economic ministries, trade/investment promotion agencies, chambers of commerce, financial institutions, research institutes and universities of the countries in which the KBCs are located. It goes without saying that the close partnerships maintained with them have a vital synergistic effect on KOTRA's operation.

5.3. Analysis of KOTRA's Strengths and Weaknesses and Challenges Ahead

In 2010, the world economy appeared to be recovering from the shock of the global financial crisis which erupted in 2008. Nonetheless, threatening factors, such as the rise in energy prices, deepening conflicts over exchange rates, and decreased demand in industrialized countries, still remain. Amidst a situation in which economic growth is led by emerging countries, including China, rather than industrialized countries, such as the U.S., KOTRA has assumed the assignment of conducting overseas marketing with a view to occupying markets ahead of the competition, particularly in new growth industries and as yet unexplored markets. Its assignment includes transforming 17 government-designated new growth engines into export industries and turning small businesses into larger and globalized ones. It means that KOTRA should carry out more sophisticated and complex tasks than in the past. KOTRA should also overhaul its internal organization, encourage its employees to build their expertise to cope with changes in the new economic paradigm, and foster an organizational culture characterized by determination to serve the nation and a readiness to meet new challenges.

Table 3-29 | Strengths and Weaknesses on KOTRA

Strengths		Weaknesses
• Diversification and expansion of the scope of business • Creation of new markets in technological or industrial convergence	Business	• Lack of customer-oriented and thorough supporting activities • Lack of synergistic opportunities between activities
• Vast network in and out of Korea • Accumulated database on diverse types of customers	Infrastructure	• Decrease in KOTRA's influence on related institutions since they are seeking expansion to foreign countries on their own initiative • Diminishing the use of information system for its overload
• Employees of competency • Internal consensus on the need for changes and the CEO's firm will	Organization	• Insufficient internal communication and operational efficiency • Higher demand for expertise in step with diversification of functions
• Increase in revenue from KOTRA-originated businesses	Finance	• Weakness of the capital structure compared to other public institutions

Table 3-30 | Opportunities and Threats on KOTRA

Opportunities		Threats
• Strengthened governmental support for industries expected to serve as new growth engines • Reinforcement of national branding and competitiveness	Government policy	• Decrease of budget earmarked for trade/investment promotion programs • Pressure on restructuring of public institutions
• Emergence of new consumers amid trends towards globalization and FTAs • Expectation on Korean economy under the G20 system	Economy	• Deepening synchronization under the global economic system • Uncertainty lingering over the world financial market and real economy
• Worldwide recognition of the importance of corporate social responsibility (CSR)	Society	• Increase in investment in CSR-related programs
• Spread of the practice of outsourcing and the worldwide division-of-labor system	Trend	• Expand of foreign TPOs spectrum of business and activities • More and more institutions seeking forays into foreign countries on their own
• Increase in the demand for customized investment services • Increase in new demands, including businesses making their first forays into foreign countries	Customers	• Diversification and segmentation of demands • Invention of new company business model to converge functions among its subsidiaries

The year 2012 marks the 50th anniversary of KOTRA's founding. It would not be an exaggeration to say that the efforts of KOTRA to increase the country's foreign trade volume and promote FDI in South Korea over the past half-century have contributed greatly to making Korea what it is today: that is, the 13th largest economy in the world. Now, KOTRA is mulling over how it should carry out its activities over the next half-century in order to remain the world's No.1 TPO amid rapid changes in the world economy.

5.4. Lessons Learned and Matters to Think over

The role of a state-run TPO is to contribute to the development of the national economy by promoting trade, attracting investment, and providing support for industrial/technological collaboration between domestic companies and foreign businesses. Under the globalized economic system, no country can operate its economy without engaging in transactions with foreign countries. As such, a country's trade policy should be focused on fostering an environment that is conducive to transactions between domestic and foreign businesses. It should also be remembered that SMEs should be important beneficiaries of any support activities carried out by TPO. A globalized business, such as Hyundai Motor or Samsung Electronics, can carry out their own overseas marketing activities without external help, but SMEs need state-led support in administrative services.

Operation of a state-run TPO does not guarantee the growth of the economy or trade. All individuals participating in the activities to explore new overseas markets should have a firm commitment to the development of the national economy. It is important to note that most of the 24 factors[15] which Hakan Hedberg singled out as contributors to the rapid growth of South Korea's economy and trade in the 1960s and 1970s were placing the national economy in the mindset of every individual.

As shown by the changes in KOTRA's functions and roles, a TPO should be able to anticipate changes and to adapt to the new environment by reflecting the changes in the full range of activities with the aim of developing the national economy and domestic businesses. It should also keep abreast of changes in the world economy based on the information provided by its worldwide network and help the government set up the right policies.

Finally, a TPO can successfully meet its objectives only when it is equipped with an institutional apparatus that ensures its independence, and when its members possess both the necessary expertise and an iron-cast commitment to work for the country. In addition, it should have an efficient management system and make concerted efforts to play a leading role in carrying out the government's policies with foresightedness.

Table 3-31 below contains the basic questions and answers that can be raised in establishing and operating a state-run TPO.

15. The 24 factors are as follows: strategy, decision-making process, high levels of education, diligence, growth tools, low wages, amount of information available, hierarchy, short-cut philosophy, pressure from North Korea, geographical advantage, flexible bureaucratic system, investors, competition, use of foreign technologies, urbanites' way of life, readiness to learn from other people's errors, people's complex characteristics, political stability, creditworthiness, readiness to adopt diverse opinions, competitive mindset, and young people full of energy.

Table 3-31 | Q's and A's Concerning the Establishment and Operation of TPOs

| Question | A government institution like the Department of Commerce can carry out the business of trade promotion. What, then, is the reason for establishing a separate, state-run TPO?

| Answer | In an advanced country, the central government's main functions are focused on providing authorizations and approvals. The function of policy execution is entrusted to affiliated institutions or to the private sector. This is intended to ensure that the government's functions are carried out more professionally and efficiently, in addition to following the trend toward a small government, i.e. separation of the function of policy execution from that of policy establishment. In addition, it will prevent some government officials from making shady attempts to gain personal profit by forecasting the outcome of the policies they formulate.

| Question | Developing countries should operate on a tight budget. Is the operation of a TPO justified for these countries?

| Answer | A country's policy direction will be the most crucial factor when deciding whether there is a need to establish a TPO in the country or not. Taking Korea as an example, the firm commitment of the country's leader led to the establishment of KOTRA in 1962, and that organization has played a key role in the dramatic increase of the country's foreign trade volume. Most countries the world over operate state-run TPOs to help domestic businesses make forays into foreign markets.

| Question | Suppose a country sees a need for an independent TPO. Won't the relevant government ministries be opposed to it in the belief that it will reduce their influence or power?

| Answer | Korea had such a problem at the time of the establishment of KOTRA in 1962. The leader of the country should be firmly committed to establishing one and should foster a favorable environment so that the members of such an organization will be motivated to work hard for the country.

| Question | The operation of a TPO will require considerable funding. How should one be organized?

| Answer | It is advisable to start with a small number of people and to increase the number gradually in accordance with increases in the trade volume, opening its representative offices in the major cities of export destination countries first. Young and capable employees should be dispatched to the representative offices to harvest good results on relatively low expenses. It is also a good idea to apply for ODA loans to meet the needs of the operational budgets of such representative offices.

| Question | Concerning the TPO operational budget, which is better, having the government provide it or collecting dues from the relevant businesses?

| Answer | Mostly, a TPO is included in private sector, but it is also a semi-governmental institution that provides a public service on behalf of the government. It should also be a non-profit institution. A TPO's service should be a public service provided evenly to the county's businesses. Financially, the service helps the country's trading businesses to reduce their expenses when developing foreign markets. Thus, it is desirable for the government to provide the TPO's operational budget in full in the beginning and to consider having businesses bear the burden partially as their financial situation improves.

| Question | ow should the employees be provided at the time of establishing a TPO?

| Answer | When part of the government's function is transferred to the private sector in the form of a split-off, some public officials who have experience of handling the relevant function may be moved to the newly established organization. However, to ensure the optimum efficiency of the new business, it is recommended that employees be newly recruited from among those with good foreign language proficiency and expertise in international economy and foreign trade.

| Question | What is the most important duty that a newly established TPO should assume?

| Answer | First of all, it should inform domestic businesses of the norms of international trade organizations and the contents of inter-country trade agreements as well as the market situations of export destination countries. Next, it should locate promising export items and foreign buyers to work with, and check the improvements to be made in the country's exports for domestic businesses.

| Question | Should the functions of trade promotion and FDI attraction be carried out by one institution?

| Answer | It depends on a country's policy. In the case of a developing country, the answer is "yes." That is because it may accomplish its policy objective of improving the trade environment and expanding the trade volume within a short period of time by attracting foreign businesses with expertise in international trade. In the current world economy, foreign trade and FDI are very closely associated with each other.

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