Korea’s Need for a New Economic Paradigm

(Abstract)

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During the disastrous Korean War of 1950-53, the already poor agrarian economy of South Korea was utterly devastated and its infrastructure severely degraded. However, the Korean economy has achieved a truly miraculous growth since then, becoming the world’s 15th largest economy today. Korea’s per capita income grew from just $80 in 1961 to over $22,000. This so-called *Miracle on the Han River* was achieved by the deliberate government policy of export-promoting open economy accompanied by rapid development of the manufacturing sector aimed at export markets. Korea today has become the 8th largest trading nation of the world, with its annual trade volume now exceeding $1.1 trillion, from only $500 million in 1962.

The early years of Korea’s economic development were full of trials and challenges, but the Korean people overcame those difficulties by exploiting the country’s geological and historical situations. Korean entrepreneurs initially took advantage of the advanced technical and marketing skills in the neighboring Japan through joint ventures and other cooperative arrangements with Japanese firms. Having obtained their initial access to the Western markets with the assistance of Japanese joint venture partners, Korean businesses have then chosen to compete directly with their former mentors in Japan in international markets. As the Korean economy has achieved its initial success, its unique brand image has also advanced and broadened from the economic field to cultural arenas as well, such as the so-called *Hallyu* (Korean Wave) in music, film, drama, sports and other entertainment areas. The Korean economic progress and the *Hallyu* have reinforced each other in enhancing the Korean brand image both economically and culturally, achieving a virtuous circle.

In recent years, however, the Korean economic growth rate has notably slowed down, with huge youth unemployment and even bigger under-employment. Many of the big Korean industrial giants such as Samsung and Hyundai have increasingly moved their new investments abroad to low-cost regions such as South Asia and Eastern Europe. Consequently, many experts have recently raised their voice urging a fundamental paradigm change in the Korean economic development policy towards a greater emphasis on the service sector of the economy where the job growth can be far more rapid. However, Korea’s service sector is relatively under-developed compared to other advanced countries. Korea’s service sector value added as a share of GDP is well below that of advanced countries. The same is true for its share in the total employment. Furthermore, productivity of the Korean service sector is estimated at 1/3 of Switzerland and ½ of the United States. Such a poor state is due to the fact that the Korean service sector is concentrated in low-value *infrastructure services* such as wholesale and retail sales, lodging, and food services. Korea’s service sector is painfully under-developed in the high-value *knowledge service industries* such as banking, finance, insurance, engineering, telecommunications, research and development. The urgent challenge facing the Korean economy in the coming years is how to develop world-class *knowledge service industries* comparable to Korea’s manufacturing giants such as Samsung Electronics and Hyundai Motor Company.