



Retrospect and Prospect of Korea-Japan Economic Relations



Gyu-Pan Kim

Ph.D., Senior Research Fellow, Japan and East Asia Team
Korea Institute for International Economic Policy

Since normalization of diplomatic relations in 1965, Korea-Japan economic relations can be summed up as a trade imbalance, that is, Korea's continuing trade deficit with Japan. While Korea-Japan trade volume expanded to about \$200 million in 1965, \$20 billion in 1987, \$50 billion in 2000, and \$100 billion in 2011, Korea's trade deficit with Japan started at about \$100 million in 1965, and expanded to about \$5.2 billion in 1987, about \$11.3 billion in 2000, and about \$2.86 billion in 2011. Since 2010, Korea's trade deficit with Japan has fluctuated from a minimum of \$19 billion in 2019 to a maximum of \$36 billion in 2010. Korea's trade structure with Japan shows that Korea has accumulated national wealth by achieving a current account surplus across the country by importing high-quality parts and materials from Japan and processing and exporting them during the course of Korea's high economic growth. Nevertheless, some within Korea interpret Korea's trade deficit with Japan as a form of technical and economic subordination to Japan starting from the past experience of Japanese colonial rule. This perception was most evident in the breakdown of the 2004 Korea-Japan FTA negotiations, and it has not been dispelled by Korea's pending decision to participate in the CPTPP. The fact

that the Korea-Japan currency swap deals have not resumed, ever since the Japanese government announced the suspension of negotiations to resume the currency swap in 2017, is also the result of failing to clear up the historical issues between Korea and Japan, including the military comfort women issue in the Japanese colonial era.

In July 2019, the Japanese government entered into measures to restrict the country's export to Korea of three key materials required for the production of semiconductors and displays – photoresists, hydrogen fluoride and fluorinated polyimides – and at the end of August, it took measures to remove Korea from its “white list” of trusted trade partners. The Japanese government claimed Korea had neglected to carry out strict trade management of high-tech materials that can be used as weapons, and that Korea could no longer be recognized as a reliable country because the Korean government failed to take any action against the Supreme Court of Korea, which had issued a ruling ordering Japanese companies to compensate damages endured by forced laborers in the Japanese colonial era. The Japanese government's stance is that these claims were resolved by the Korea-Japan Claims Agreement in 1965.

The export restriction measures taken by the Japanese government in July 2019 cannot be interpreted as simply derived from the historical issues of Korea and Japan. Looking back on the Japan-China Senkaku Islands dispute that began in 2009, although there have always been historical and territorial disputes between Japan and China, this expanded to trade friction between the two when China emerged as a global economic power. Similarly, Japan's Abe Cabinet launched a trade dispute against Korea when the U.S. Trump administration initiated a trade dispute against China as a pretext for “America First” policies.

In response to Japan's export restriction measures, the Korean government announced measures to strengthen the nation's competitiveness in the materials, components, and equipment industries in August 2019, and expanded its scope of support to include the semiconductor and bio industries in July 2020, under the goal of becoming a global factory for high-tech industries. The Korean government's response suggests that it will be very difficult to resolve the current trade friction between Korea and Japan through diplomatic negotiations. After Japan's export restriction measures, the Korean government made various diplomatic responses, such as suggesting alternative compensation for forced laborers in the Japanese colonial era, filing a lawsuit at the WTO, and withdrawal from the GSOMIA agreement, but in the mid- to long-term, it appears that lowering reliance on Japanese advanced technologies would be the “second-best” way out of these history issues.

Nevertheless, in the coming August, the Korean and Japanese governments are facing diplomatic challenges to reach a smooth agreement on the issue of compulsory enforcement against Nippon Steel, the WTO lawsuit filed by Korea, and extension of the GSOMIA. The Japanese government has warned that further retaliation measures will be carried out if any compensation order for a Japanese company is actually executed. Looking back at the achievements of economic cooperation between Korea and Japan, and given that the COVID-19 pandemic is not looking to subside anytime soon, we must gather wisdom in a way that diplomatic conflicts between the two countries no longer disrupt interdependent economic relations. **KIEP**