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South Korea's Strategic Directions in the Context of the US-China Trade War: An Application of the ABCD Model

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Abstract

Purpose: South Korea is a close ally of the US and an important partner of China. Caught between the two most powerful countries, South Korea's strategic directions are critical. This article emphasizes that the deeper core of the US-China trade war is to improve the business environment to attract foreign direct investment (FDI) to boost the economy, rather than engaging in the trade war. **Research design, data, and methodology:** Considering the complexity of this issue, this article applies a systematic analytical tool, the ABCD (Agility, Benchmarking, Convergence, and Dedication) model, to provide strategic guidance for inducing investments into South Korea in the context of the ongoing US-China trade war. **Results:** Specifically, South Korea needs to provide a more attractive business environment along the four points: expedite commercial activities through deregulation (Agility); adopt global standards of the flexible labor markets and technological developments (Benchmarking); integrate various industries and connect them to global value chains (Convergence); and create more economy-friendly policies rather than politics-oriented ones such as protectionism (Dedication). **Conclusion:** This study stands out not just by utilizing the ABCD model but, also by providing more systematic analysis and practical implications, particularly within the context of the escalating US-China competition. Unlike many existing studies that analyze the broader impacts of this geopolitical rivalry, this research delves into specific strategic guidelines for South Korea to attract FDI. The findings also provide implications for multinational corporations (MNCs) in choosing the locations for their overseas operations, particularly in South Korea.

Keywords: South Korea, Strategic directions, US-China trade war, FDI, ABCD model

Major Classification Code : M30, M31, M39

1. Introduction

South Korea's unique position as both a close ally of the US and a significant partner of China requires a careful strategy for the sustainable growth of its economy. Despite its efforts, South Korea faces limitations in influencing US-China relations, which greatly impact Korean affairs. To navigate this, South Korea must leverage its assets, such as its security alliance with the US and economic ties with China, while minimizing involvement in uncontrollable issues (Chung, 2001; 2007). Key priorities for South Korea include economic growth, development, peace, security, and reunification. While China holds importance in economic relations (Snyder, 2009; Ye, 2017; He & Ju, 2020), the South Korea-US alliance is paramount for national security

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and military defense (Chung & Kim, 2016; Hwang & Lee, 2017).

The US-China relationship has entered a new and prolonged phase of economic, diplomatic, technological, and military tensions. The tensions between the US and China are not limited to their bilateral relationship but are of global concern. China's rise is, perhaps, the single most important economic and political phenomenon in the twenty-first century (Grosse et al., 2021). China has been the most seriously debated emerging power, viewed by academics, politicians, and large parts of the public alike to be capable of effectively challenging the hegemonic position of the US in global as well as Asia-Pacific affairs (Fels, 2016).

South Korea is particularly vulnerable to the trade conflict between the two economic giants because the US and China are its two largest trading partners (Suh, 2019). Since China's accession into the World Trade Organization (WTO) in 2001, South Korea has benefited from the rapid economic growth of China and has maintained China as its number one trading partner for the last two decades, accounting for a quarter of total trade (Yeo, 2024). The 2018-initiated US-China trade war stemmed from concerns over China's alleged unfair economic practices, including intellectual property theft and trade imbalances. This led to consecutive tariff impositions by both nations, disrupting global trade and supply chains. While initially economic, the conflict has spread into a wider geopolitical rivalry, driven by ideological disparities. Persistent tensions, despite occasional attempts at negotiation, continue to affect global trade and the relationships among major economies (Bown & Wang, 2023). South Korea has been affected tremendously by the US-China trade war (Jeong, 2019).

While the US-China trade war disrupts direct trade channels, the complexity of global trade networks allows Chinese exports to reach the US indirectly through third countries, contributing to the continued flow of goods between the two nations (Freund et al., 2023). Itakura (2020) also argued that the US-China trade war indirectly impacts FDI by altering global trade dynamics and investment preferences. There are some studies proposing cooperative potential between the US and China by utilizing the comparative advantages of the two countries each other (e.g., Huang et al., 2024, forthcoming). However, the tension between the two countries is still real and in such an environment, countries, including South Korea, need to adjust strategies to attract FDI amidst evolving global economic landscapes. The analysis of this article utilizing the ABCD model highlights the imperative for South Korea to enhance its domestic investment environment, particularly to entice more FDI from both the US and Chinese companies, in particular. This strategic choice is crucial for revitalizing the Korean economy and ensuring its sustained development. Furthermore, this study provides tailored strategies for South Korea to attract FDI and provides practical implications amid the growing US-China competition, offering actionable insights for policymakers and investors.

2. Literature Review

South Korea remains caught in the middle of an intensifying strategic competition between the US and China (Kim, 2022). The relationship between the US and China has entered a new phase characterized by prolonged tensions across economic, diplomatic, technological, and military domains. These tensions extend beyond bilateral ties and have significant global implications (Grosse et al., 2021). China is fast emerging into a global superpower that could rival the US (Doshi, 2021). The US views China as a strategic competitor on multiple fronts, leading to economic and political challenges (Prestowitz, 2021).

With the advent of the Trump administration and the subsequent US-China trade conflict, South Korea's trade policy is under immense pressure (Sohn, 2019). The Trump administration imposed economic sanctions on China with tariffs and regulations on technologies, intensifying trade protectionism. The COVID-19 pandemic exacerbates de-globalization, escalating tensions between the US and China. The Biden administration's continuation of the 'tech war' intensifies trade disputes (Erlbacher & Schmalz, 2023). Concurrently, China's stance has shifted towards a less passive approach, signaling readiness to counter additional US measures on technology and trade.

Trade is often viewed as a zero-sum game in the debates on the connection between trade and employment; that is, one country's gain in exports means the other country's loss through imports, and the conflict between the two nations extends beyond trade and involves complex issues (Cho & Moon, 2022; Moon et al., 2022). While the US-China trade war disrupts direct trade channels, the complexity of global trade networks allows Chinese exports to reach the US indirectly through third countries, contributing to the continued flow of goods between the two nations (Freund et al., 2023). This kind of triangular trade may bypass the trade war to some extent, however, FDI can provide a more fundamental solution to the trade problems. Globalization has driven policymakers to pay more attention to FDI by MNCs (Yang & Kang, 2023). FDI goes beyond trade by addressing market inefficiencies, fostering job creation, and enhancing productivity, and management practices (International Monetary Fund, 2023a). Its complexity lies in its diverse effects on economies, making it a valuable tool for economic development (Farole et al., 2013).

The US-China trade war indirectly impacts FDI by altering global trade dynamics and investment preferences (Itakura, 2020). As tensions continue, countries, including South Korea, adjust strategies to attract FDI amidst evolving global economic landscapes. The intensifying US-China tension significantly affects South Korea, in particular, posing a strategic challenge as it balances its US alliance and economic ties with China. Disruptions in global supply chains and market uncertainties directly impact South Korea's trade relations. Navigating this competition between the US and China requires South Korea to skillfully safeguard its national interests amid evolving geopolitical dynamics (Lee, 2023).

There is a strong and positive impact of FDI on South Korean economic growth (Koojaroenprasit, 2012). South Korea is pursuing industrial policies for economic growth, job creation, nurturing of future growth engines, and so on, by attracting FDI through selective means using economic, information, and organizational inducements (Kim, 2019). However, the share of FDI inflows in GDP has been, in general, relatively low in South Korea compared with other economies that have grown rapidly (Mah, 2010). This paper goes beyond the narrow lens of trade wars. Instead, it acknowledges the reality of the US-China trade war and, from a more fundamental and broader perspective of FDI. To this end, this paper employs the ABCD model to systematically analyze how South Korea can enhance its business environment amidst the US-China trade war. By leveraging its conditions, South Korea can attract more overseas investment, thereby stimulating economic growth and fostering sustainable development.

3. Analytical Framework

3.1. Foundation and Development of FDI Theories

John Dunning's OLI (ownership, location, and internalization) paradigm, established in various works spanning from 1958 to 2000, forms the foundation of FDI theories, asserting that firms with ownership advantages invest abroad to navigate unfamiliar business environments (Dunning, 1958; 1980; 1998; 2000). However, traditional FDI models fail to explain how MNCs from developing countries, lacking apparent ownership advantages, invest in more developed nations. This anomaly is exemplified by South Korean companies Samsung Electronics Co. Ltd. (SEC) and LG Electronics (LGE), where despite LGE's weaker position in its home country compared to SEC, it pursued FDI, leading to the formulation of the "imbalance theory" by Moon and Roehl (2001). Moon and Yim (2014) and Moon (2016a) further expand on this theory, introducing the concept of complementary capabilities, including agility, benchmarking, convergence, and dedication, which aid MNCs from developing countries in overcoming deficiencies. These studies propose a competitive advantage framework tailored for such firms venturing abroad, incorporating features from latecomers' strategies to address disparities.

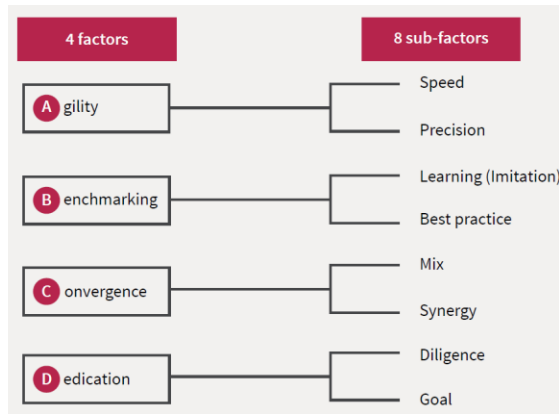

Figure 1: The ABCD Model

3.2. Introduction of the ABCD Model

Moon (2016b) details four factors that comprise the ABCD model (refer to Figure 1) and illustrates how the South Korean government, corporations, and people have exemplified these factors in achieving their current level of success. The four factors are agility (speed and precision), benchmarking (learning and best practices), convergence (mixing and synergy creation), and dedication (diligence and goal orientation), and together, they have enabled South Korea's economic success and will continue to drive the next level of growth. Specifically, agility combines speed with precision to enhance productivity, while benchmarking involves learning the best practices for efficient catch-up. Convergence entails mixing synergistically to create new advantages, and dedication requires diligence with goal orientation for a strong commitment (Moon, 2012; 2016b; 2017).

3.3. The Efficacy of the ABCD Model in Analyzing FDI Attraction Factors

The rationale for applying the ABCD model, as proposed by Moon (2016), lies in its efficacy in assessing and enhancing a nation's competitive advantages. Specifically, the model offers a structured framework encompassing four factors: Agility, Benchmarking, Convergence, and Dedication, which can be tailored to analyze regulatory efficiency in attracting FDI. In the context of FDI attraction, regulatory efficiency plays a pivotal role in shaping a country's attractiveness to investors. By employing the ABCD model, policymakers can systematically evaluate and improve regulatory frameworks to foster a conducive environment for FDI inflows (Moon, 2016). Additionally, the ABCD model offers a holistic approach valued by investors for assessing opportunities, as demonstrated by South Korea's economic success attributed to the ABCD factors. This success serves as a compelling case study, showcasing the model's effectiveness and providing evidence for investors seeking proven strategies. Moreover, the model's practicality and relevance to both developing and developed countries make it particularly useful for FDI analysis, offering opportunities for global expansion and strategic diversification, thus drawing investors seeking such prospects. Compared to alternative models like Michael Porter's diamond model (Porter, 1990), the ABCD model offers deeper insights into competitive advantages and growth potential (Moon 2016b; 2018). Porter's diamond model is a useful comprehensive framework for describing national competitiveness and FDI location factors, whereas, Moon's ABCD model illustrates specific strategic guidelines for how to enhance the competitive advantage of location factors for FDI.

4. Enhancing South Korea's Competitiveness in Attracting FDI: An Analysis Using the ABCD Model

Since the early 1980s, South Korea has emerged as a prime destination for FDI and a pivotal hub for MNCs seeking to establish operations or expand across the Asia-Pacific Region. Leveraging an extensive treaty network, strategic alliances, particularly with partners like the US, and a robust legal framework, South Korea has fostered a secure environment conducive to sustained economic growth. Over recent decades, South Korea's economic landscape has undergone a notable evolution, transitioning from a manufacturing-centric model heavily reliant on exports to a dynamic global economic powerhouse. With a current ranking as the 10th largest economy globally and the 4th largest in the Asia-Pacific Region, South Korea hosts sixteen Fortune 500 companies (The American Chamber of Commerce in Korea, 2024). Positioned at the forefront of cutting-edge industries such as semiconductors, electric vehicles, and Internet platforms, South Korea is driving innovation and shaping future industries. Moreover, South Korea is actively attracting new FDI and diverse businesses, catapulting up the global value supply chain and solidifying its status as a key business leader in the Asia-Pacific region. Given its strategic location neighboring China, robust infrastructure, and evolving geopolitical dynamics, South Korea emerges as an optimal destination for MNCs seeking growth and expansion (The American Chamber of Commerce in Korea, 2024).

Nevertheless, South Korea's FDI net inflow in 2022 was around US$18 billion, resulting in a decline in its global ranking from 16th in 2021 to 20th in 2022 (World Investment Report, 2023). Meanwhile, the top four countries/regions with the highest FDI net inflows globally in 2022 were as follows: the US, with an inflow of approximately US$285 billion, marking a substantial decrease of about US$100 billion compared to 2021; China, experiencing an increase of approximately US$10 billion compared to the previous year, reaching approximately US$190 billion; Singapore, observing a rise of roughly US$10 billion compared to 2021, totaling around US$140 billion; and Hong Kong SAR, China, encountering a decrease of approximately US$20 billion compared to 2021, amounting to approximately US$120 billion (World Investment Report, 2023).

South Korea's strategies to attract FDI can be systematically evaluated through the lens of the ABCD model. Firstly, 'Agility' is evident in the country's ability to swiftly adapt to changing market conditions and investor preferences, enabling it to maintain competitiveness. Secondly, 'Benchmarking' involves comparing and learning from successful FDI attraction practices globally, allowing South Korea to identify best practices and implement them effectively. Thirdly, 'Convergence' refers to the alignment of government policies, industry efforts, and market needs to create a conducive environment for FDI, fostering collaboration and synergy. Lastly, 'Dedication' is demonstrated through continuous efforts to improve the investment climate, enhance infrastructure, and provide support to investors, showcasing South Korea's commitment to attracting and retaining FDI. By employing these ABCD model factors, South Korea can bolster its position as an attractive destination for foreign investors. More detailed explanations are provided as follows:

4.1. Agility (Speed and Precision)

Through a combination of speed and precision in deregulation efforts to expedite commercial activities, South Korea can effectively position itself as a competitive and dynamic hub for FDI, driving economic growth and prosperity in the region (Lee, 2013; Moon, 2022).

Speed. Efficient deregulation, to enhance the speed of business, involves expediting bureaucratic processes and decision-making, allowing businesses to swiftly navigate regulatory hurdles and establish operations. By implementing efficient procedures and reducing administrative burdens, South Korea can enhance its appeal to foreign investors seeking rapid market entry and operational efficiency. This proactive approach to streamlining processes can significantly reduce the time and resources required for businesses to establish a presence in the country, making it a more attractive investment destination (Santander, 2024).

Precision. On the other hand, precision involves tailoring deregulation efforts to address specific pain points and barriers faced by potential investors. By conducting thorough assessments of regulatory frameworks and identifying areas for improvement, South Korea can ensure that deregulatory measures are targeted and effective. This precision in deregulation demonstrates South Korea's commitment to creating a business-friendly environment tailored to the needs of investors, further enhancing its reputation as an attractive destination for FDI (Invest KOREA, 2023).

The Example of Singapore. Agility is a crucial factor in attracting FDI, as exemplified by Singapore's success. By swiftly and precisely implementing deregulation measures to streamline commercial processes, Singapore has established itself as a prime destination for FDI. This approach has facilitated rapid entry and operational efficiency for MNCs, leading to significant FDI inflows. South Korea can emulate Singapore's agility strategy by enacting prompt regulatory reforms and fostering a business-friendly environment (International Monetary Fund, 2023b). By prioritizing speed and precision in deregulation efforts, South Korea can enhance its attractiveness to investors, positioning itself as a competitive and dynamic FDI hub in the region. This approach would drive economic growth, spur innovation, and foster prosperity, aligning with Singapore's successful model.

4.2. Benchmarking (Learning and Best Practices)

To enhance FDI attraction in South Korea, it is essential to leverage benchmarking through learning and best practices by adopting global standards of flexible labor markets and technological developments.

Learning. Learning involves studying global standards, particularly in flexible labor markets and technological advancements, to adopt and implement effective strategies. By examining successful models from countries with robust labor market flexibility and cutting-edge technological infrastructures, South Korea can identify areas for improvement and implement policies to align with global benchmarks (U.S. DEPARTMENT of STATE, 2023). This approach fosters continuous learning and innovation, positioning South Korea as a competitive destination for FDI by demonstrating its commitment to staying abreast of international best practices.

Best Practices. Moreover, embracing best practices entails not only adopting global standards but also implementing them efficiently and effectively. South Korea can benchmark against countries renowned for their successful labor market policies and technological advancements, such as the United States and the European Union (Sim et al., 2018). By integrating these best practices into its regulatory framework and business environment, South Korea can create a conducive ecosystem that fosters innovation, productivity, and investment attractiveness (U.S. DEPARTMENT of STATE, 2022). This approach not only enhances the country's competitiveness but also showcases its commitment to providing a conducive environment for foreign investors, thereby facilitating the inflow of FDI into South Korea.

The Example of Hong Kong. Hong Kong's success in attracting FDI through benchmarking provides a compelling case study for South Korea. Hong Kong has effectively benchmarked global standards of flexible labor markets and technological advancements, aligning its policies with best practices. By emulating Hong Kong's approach, South Korea can enhance its FDI attraction strategy. Learning from Hong Kong's practices, such as implementing flexible labor policies and embracing technological advancements, South Korea can create a more conducive environment for foreign investors (Jeong & Lee, 2022). This strategic benchmarking allows South Korea to leverage global standards, positioning itself as an attractive destination for FDI and fostering economic growth and prosperity in the region.

4.3. Convergence (Mixing and Synergy Creation)

Through its subfactors of mixing and synergy creation, convergence plays a pivotal role in integrating various industries and connecting them to global value chains.

Mixing. Mixing involves blending different sectors of the economy, leveraging their strengths, and fostering cross-pollination of ideas and resources. By strategically combining diverse industries such as technology, manufacturing, and services, South Korea can create innovative products and services that resonate with global market demands (FasterCapital, 2024). This approach not only enhances the competitiveness of domestic industries but also facilitates their seamless integration into global supply chains, thereby expanding market reach and driving economic growth.

Synergy creation. Another aspect of convergence is synergy creation, which focuses on maximizing the collaborative benefits derived from the integration of different industries. By fostering collaboration among diverse sectors, South Korea can amplify synergies and capitalize on collective strengths (Oh, 2018). Through joint research and development initiatives, shared infrastructure, and knowledge exchange platforms, synergies can be harnessed to develop cutting-edge technologies and innovative solutions that address global challenges (Kang, 2017). This collaborative approach not only accelerates technological advancements but also positions South Korea as a hub for innovation and excellence in the global arena, fostering sustained economic development and prosperity.

The Example of the US. Convergence, characterized by mixing and synergy creation, has been instrumental in the US's success in attracting FDI. By blending different industries and fostering synergies among them, the US has created a dynamic ecosystem that attracts investments from around the world (Mahmood et al., 2019). This convergence strategy has enabled the US to establish itself as a key player in global value chains, facilitating the integration of diverse sectors and maximizing economic growth (Antonietti & Mondolo, 2023). South Korea can draw valuable lessons from the US by adopting similar convergence strategies to integrate its industries, promote collaboration among sectors, and enhance its attractiveness to FDI. Leveraging convergence, South Korea can position itself as a competitive destination for FDI and drive economic development through enhanced integration into global value chains.

4.4. Dedication (Diligence and Goal Orientation)

Dedication, characterized by diligence and goal orientation, underscores the importance of crafting economy-friendly policies over politics-oriented ones like protectionism.

Diligence. In policy-making, diligence involves thorough research, analysis, and consideration of the long-term implications on the economy (KPMG Consulting, 2001). Prioritizing diligence in decision-making, the government seeks more assured success. Diligence demands sustained effort and courage, guiding policies towards economic principles. This approach fosters stability and predictability in the business environment, which is crucial for attracting foreign investment and stimulating economic growth (LinkedIn, 2024).

Goal Orientation. Furthermore, a goal-oriented dedication entails aligning policy objectives with overarching economic goals such as fostering innovation, promoting competitiveness, and enhancing productivity (Santander, 2024). By setting clear economic targets and designing policies to achieve them, governments can create an environment conducive to sustainable growth and prosperity. This strategic approach to policymaking not only attracts foreign investment but also catalyzes domestic entrepreneurship and innovation, driving overall economic development (U.S. DEPARTMENT of STATE, 2022). Therefore, dedication, through its subfactors of diligence and goal orientation, plays a pivotal role in shaping policies that prioritize economic growth and competitiveness over political considerations.

The Example of Sweden. Sweden's net FDI inflow in 2022 ranked ninth in the world and first in Europe (World Investment Report, 2023). Sweden's success in attracting FDI can be attributed to its dedication characterized by diligence and goal orientation. The country's commitment to crafting economy-friendly policies, prioritizing economic growth over political considerations like protectionism, has positioned it as an attractive destination for FDI. Sweden's approach involves creating a conducive environment for investment through consistent efforts to streamline regulations, enhance infrastructure, and promote innovation. By focusing on economic development and aligning policies with long-term growth objectives, Sweden has been able to attract significant FDI inflows, serving as a model for countries like South Korea seeking to enhance their competitiveness in the global market (Baker Mckenzie, 2023). South Korea can draw valuable lessons from Sweden's dedication by aligning its policies and strategies with long-term economic goals, prioritizing market-driven approaches, and fostering a conducive environment for foreign investment to enhance its FDI attractiveness.

5. Conclusions

This study delves into the complexities of the US-China trade war and proposes a strategic solution that focuses on attracting companies, whether foreign or domestic, to invest in the home country. It suggests that instead of engaging in protectionist policies like tariffs and battling foreign governments, a more beneficial approach is to create an environment conducive to investment within the domestic market. To achieve this goal, this paper utilizes the ABCD (Agility, Benchmarking, Convergence, and Dedication) model to undertake a thorough and comprehensive analysis of location advantages. Its objective is to formulate strategies for South Korea to effectively attract FDI amid the ongoing tensions between the US and China.

Key findings of this paper reveal that swift deregulation efforts (agility) are crucial and should be prioritized for positioning South Korea as an attractive destination for FDI and fostering economic growth. Additionally, adopting global standards in labor markets and technology (benchmarking) enhances the investment environment. Integration of industries and connection to global value chains (convergence) further elevate South Korea's attractiveness for investment. Advocating for economy-friendly policies over protectionist measures (dedication) sustains FDI inflows. The study's originality is underscored by its explicit focus on implications within the context of US-China competition, providing actionable insights for policymakers and investors to navigate this dynamic landscape.

In addition to employing the ABCD model, this study distinguishes itself from other research by its explicit focus on implications, especially within the context of the intensifying US-China competition. While many studies analyze the impact of this geopolitical rivalry on global trade and investment, this paper uniquely delves into the specific strategies that South Korea can adopt to navigate this landscape and attract FDI. By providing actionable recommendations grounded in the ABCD model, this study offers practical insights for policymakers and investors seeking to capitalize on South Korea's potential amidst the shifting dynamics of the US-China relationship. Through its emphasis on implications, this research aims to contribute not only to academic discourse but also to practitioners including policymakers and business managers for investment strategic planning in the global economy.

This study offers significant contributions to the field by providing valuable insights into strategic planning for South Korea's economic development. Notwithstanding, we acknowledge the inherent challenges in accurately forecasting the outcomes of proposed strategies, given the complexities of evolving geopolitical dynamics of the US-China relations and regulatory frameworks. However, by recognizing these limitations, the study opens avenues for further research and refinement of proposed approaches. Moreover, the acknowledgment of external factors, including global economic conditions, demonstrates a comprehensive understanding of the multifaceted nature of economic policymaking. By addressing these limitations with transparency and scholarly rigor, the study fosters a constructive dialogue within academia and policymaking circles, facilitating the development of more robust and adaptive strategies for sustainable economic growth. Through continued scholarly inquiry and interdisciplinary collaboration, these limitations can serve as catalysts for innovation and refinement, ultimately contributing to the advancement of FDI theory and practice.

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