

## ***US Foreign Policy Towards East Asia and the Korean Peninsula***

***James A. Baker III***

It's a great pleasure for me to appear before you today and to share, briefly, a few of my thoughts on the US foreign policy towards East Asia and the Korean Peninsula.

Many are already predicting that the year 2000 will mark the beginning of the "Pacific Century." Here in the Republic of Korea, at least, the "Pacific Century" has already begun—because Korea is surely one of the world's most extraordinary success stories.

This success is perhaps most notable in the economic realm. With a per capita GDP near \$7,000, growth estimated this year to run in the 7percent range, workers of extraordinary productivity, a sophisticated high-tech sector, and a growing global presence, South Korea stands at the very forefront of the newly industrialized countries.

More generally, East Asia now represents one of the largest—and certainly the most dynamic—regional economies of the world. East Asia is now a full partner, with the United States and Western Europe, in the international economic arena and its importance will only increase with time. And, as you know, economic issues already represent a critical and often contentious element in US foreign policy towards the region.

For these reasons—and because of the composition of this audience—I would like to begin my remarks today by focusing

on our economic relations before turning to political and security issues. In specific, I would like to start by discussing how the world's major economic powers, including East Asia, can work together to strengthen the international economic system.

## Strengthening an Open Global Economic System

Over the last two years, the global system of open trade and investment has successfully weathered twin storms, one economic and the other economic - political.

The economic storm, of course, was the global downturn that saw North America, Western Europe, and Japan plunged into recession. The economic - political storm, in many ways just as significant, was the renewed battle between protectionism and free trade.

In the United States, the economic recovery is now well-established and indeed may have peaked. Growth this year should be in the respectable 3 percent range. Unemployment is 5.8 percent. Just as importantly, the Federal Reserve is committed to keeping inflationary pressures under control.

Western Europe, too, has begun its recovery. This year, Germany, France, Italy, and the United Kingdom are all likely to post healthy growth. Japan's recovery has been slower and may be set back further by the recent dramatic rise in the value of the yen. While the other economies of East Asia, like South Korea's, largely avoided the worst of the global downturn, most of them are likely to benefit from economic recovery in developed markets in North America and Western Europe.

If the last two years have seen good news on the growth

front, trade liberalization, too, has experienced a major breakthrough. I refer, of course, to the long - delayed conclusion of the Uruguay Round of GATT trade talks. The importance of this development cannot be overestimated. Concluding GATT marked a reaffirmation of liberal trade by the international community as a whole. It also represents a huge economic boost as the industrialized nations move from recession to recovery.

Yet the picture is not altogether unclouded. We should not forget exactly how close GATT came to failure. As the Duke of Wellington said of the battle of Waterloo, it was a "close - run thing." The particularly rancorous and potentially dangerous argument between the United States and Japan over automobiles and automotive parts reminds us that trade disputes remain a fact of international economic life.

Moreover, the global economic recovery currently underway is far less robust than many would have hoped. In Japan, growth continues to be well below historic levels. Western Europe, despite its brightening economic outlook, is still dogged by high and intractable unemployment rates. And my own country's expansion appears to be faltering with growth expected to drop below 3 percent next year.

Sustaining global growth, I believe, will require a multidimensional strategy by the major economies. So, let me suggest a four-part approach for your consideration.

### **Macroeconomic Coordination**

First, the G-7 economies must achieve a greater level of macroeconomic policy coordination. This is important, not just



for their own sake but for the broader international economy.

High German interest rates and weak Japanese demand, for instance, plainly lengthened and deepened the worldwide recession from which we are just now emerging.

I experienced first-hand the difficulties of economic policy coordination as Secretary of the Treasury when I worked with my country's major economic partners to bring some order to a chaotic international currency market. Though ultimately successful, the process was painful, protracted, and extraordinarily politicized. And it will remain so.

Particularly important is a revitalized G-7 process to encourage sustained fiscal and monetary coordination. Impressive photo opportunities and elegant communiques are not enough. It is particularly important to avoid floating flashy last-minute initiatives such as the Clinton Administration's "Market 2000" proposal at the G-7 Summit last year in Naples.

G-7 finance ministries and central banks will need to work closely together if the Western economies are to attain the twin objectives of sustained global growth and low inflation.

## Renewed Commitment to Free Trade

Sustained growth also demands, I believe, a renewed commitment to expanded trade, the second element of a multidimensional approach to global growth.

One explanation for rising protectionism around the world is, ironically, precisely the economic interdependence that has provided much of the prosperity of the post-war era. In a way, the workers and business communities of South Korea and the

other nations of East Asia have an advantage over their counterparts in the United States and Western Europe. You have long understood your dependence on the international marketplace. For many Americans and Western Europeans, however, with their large continental markets, the idea of interdependence remains alien and even threatening.

As my nation's own debates over NAFTA and GATT showed, decisions on international trade have potent domestic political consequences. It takes extraordinary courage for politicians to take a firm stand for free trade and against the domestic constituencies agitating for protection. Our experience since World War II clearly demonstrates that open trade and investment create far more economic winners than losers. If they didn't, there would be no East Asian economic "miracle," no talk of a "Pacific Century." And freer trade and more liberal investment will create even more winners. That is why the world, with the Uruguay Round behind us, cannot rest on its laurels. Internationally, it is time for the major economies to start laying the groundwork for yet another series of negotiations aimed at lowering barriers to trade and investment. The next G7 Summit in Halifax, Canada represents a perfect opportunity for beginning this critical task. Regionally, organizations like the Asia - Pacific Economic Cooperation forum (APEC) should begin developing their own timetables for dismantling remaining impediments to the free movement of goods, services, and capital. In short, the conclusion of the Uruguay Round should mark a beginning, not an end.

## Restructuring the Western Economies

This brings me to the third part of a multidimensional approach to global growth: The fundamental restructuring of the economies of North America and Western Europe.

As this audience knows so well, private sector restructuring is already underway around the world. The corporate streamlining we see everywhere reflects the fierce competition of the global marketplace. But economic restructuring can't end with the private sector. It must also include government itself. This is particularly true in Western Europe, Canada, and the United States. Western Europe is today discovering the crippling cost of the welfare state—what Mrs. Thatcher so aptly called “the Nanny State.” It is a price paid in sluggish growth and high long-term unemployment in the United States, our fiscal deficit represents a substantial drag on our economy, one that could determine our competitiveness for years to come. Yet my nation's deficit, like those of the Western European nations, is just a symptom. The disease is excessive government expenditure.

Budget deficits do not exist because government taxes too little, but because it spends too much. And it spends too much because it has acquired responsibilities that belong better to the individual, the family, or the local community.

The West, quite simply, must find a more efficient division of social labor between the private and public sectors.



## Transforming the Eastern “Miracle”

Finally, let me turn to the fourth page of a strategy to sustain economic growth: The transformation of the export - oriented economies of Japan and other East Asian nations.

Japan's experience demonstrates the limits of export - led growth. Over the long run, constant trade surpluses are no substitute for strong international growth. Chronic trade imbalances prompt international tensions and exact a real cost in terms of domestic consumption. Today, Japan is shifting towards a more balanced economic approach, one that stressed rising living standards for the Japanese people and not just export performance by Japanese firms. It is a shift that the United States and Japan's Asian neighbors should encourage.

But, progress sometimes seems glacial and its slow pace risks a sharp response. For instance, Japan's unwillingness to open its markets to US automobiles and automotive parts threatens to undermine the US - Japan partnership, which is perhaps the single most important bilateral relationship in the world. I did not have to tell you that the consequences of a fundamental rift between Tokyo and Washington would be dire for both nations and for the stability of East Asia.

The other East Asian economies are undergoing a similar transition. Some, like South Korea, are managing it more successfully than Japan. You are well placed to do so. Unlike the countries of Latin America, for instance, most East Asian nations have managed to achieve economic growth without extreme inequalities of income. The existence of an emerging middle class bodes well for more domestically - driven growth.

Indeed, there are strong signs of a new maturity in the East Asian economies. Private consumption has become a powerful engine of economic growth throughout the region. Imports are less the threat than they once seems to be. Still, much remains to be done in terms of opening markets and encouraging domestic demand. Broad-based domestic liberalization, in Japan and elsewhere in the region, must remain a top priority.

### **The Limits of Economics**

As important as a strategy for global growth is to our relations, economics represents only one challenge facing East Asia and American policy towards the region. A glance around the region shows just how important—and urgent—strategic and political issues remain.

For instance, the course of China's transition in the post-Deng era will have vast ramifications not just for China itself but for the region and indeed the world.

Deng's two-tracked approach of economic liberalization combined with political authoritarianism has yielded remarkable short-term growth.

It is not, however, sustainable in the long run. As experience here in the Republic of Korea and elsewhere has shown, the creation of an entrepreneurial class inevitably leads to increased demands for broader political participation.

By delaying the transition to a more popularly based form of government, the current regime in Beijing risks turmoil when the existing leadership passes from the scene. True, the likeliest outcome is a relatively benign one. Under this scenario,



competition among potential successors will not destabilize the country and will lead to the emergence of a center that keeps control and gradually liberalizes politically to keep pace with economic reform.

But there are other, more ominous possibilities. One is the rise of a military dictatorship prepared to suppress political discontent even at the cost of foreign investment. Such a dictatorship might well turn to foreign adventurism to rally support. Perhaps even more dangerous is the possibility that China might revert to the chaos it knew during the 1920s. Economic liberalization has already led to degrees of regional autonomy unheard of in recent Chinese history. It is conceivable that this trend could accelerate, in the absence of a strong central government, into outright conflict between competing centers of authority.

The United States, Japan, and the other countries of East Asia plainly have a powerful interest in China's long-term stability. And that stability, I believe, is best served by an approach that balances support for democracy in China with continued efforts to deepen Beijing's economic links with the outside world. An emphasis on the exclusion of the other risks deferring the day when China takes its rightful and responsible place in the international community.

Balance will also be crucial if we are to meet yet another vital test for the Far East in the years ahead: The emergence of Japan as a world power.

Japan, of course, is already an economic superpower. Despite the recent recession, Japan remains the premier model of economic development for the rest of the world. And, yet, for

powerful historic reasons, Japan has yet to exert political influence commensurate with its economic might. Since the mid-1980s, however Japan has been slowly but steadily expanding its international role.

I believe that the United States and Japan's neighbors in the Far East should welcome and indeed encourage this development. It should be perceived as nothing more than Japan's assumption, as a responsible democratic state, of its place in the community of nation. A greater Japanese role through the United Nations system—including, eventually, the possibility of some sort of status on the Security Council—can help ensure that Japan's power is a force for stability in the region and around the world.

That power should be seen as strengthening, not weakening, the US - Japanese strategic partnership, a linchpin for security in the region for over forty years.

Yet the US - Japanese partnership is in trouble. As I have mentioned, talks aimed at opening the Japanese market to US cars and car parts have stalled amidst rancor on both sides.

Trade disputes like this undermine the US - Japanese partnership—and they will continue to do so until Japan takes firm measures to open its domestic market and reduce its structural trade surplus, not just with the United States but with the world.

But the United States, too, must fulfill its side of the partnership, first by more disciplined fiscal policy, and, second, by resolve in our own commitment to regional security.

In the latter regard, the Clinton Administration's nuclear agreement with Pyongyang marks a dangerous step backwards. By acknowledging North Korea's status as a *de facto* nuclear

power, the agreement has bolstered one of the world's most irresponsible regimes and raised doubts about our resolve throughout the region. It is probably too late for the Administration to change course. But it is not too late to hold the North to the letter of its agreement or to signal our commitment to the South by beefing up our forces on the peninsula and by developing and deploying an advanced theater anti-ballistic missile system.

## Conclusion

In short, strategic and political—still matter a great deal for the United States and the nations of East Asia. And we neglect them at our peril.

Indeed, I would conclude by warning against what could be called “economism”—the idea that, with the Cold War behind us, only economics matter. This is a dangerous concept because it ignores the very risks and opportunities to security that I have mentioned.

But economism is dangerous at another level because it neglects human needs that transcend the purely material. We should support free markets, not because they are efficient (though they are) but above all because they are free. And freedom means much more than the choice of a new television set or a new car. It also means political freedom. The right to free expression, the right of unrestricted association, the right to vote in open and meaningful elections.

Some in the past have referred to these as “Western values.” With the end of the East-West conflict I'm not sure that the



term is any longer appropriate. Certainly there are powerful cultural differences between, say, the societies of South Korea and the United States—differences that all must understand and respect on both sides of the Pacific. But I also suspect that, at a fundamental level, when we talk about these values we are talking about human values—values that bind the peoples of the United States and the Republic of Korea just as strongly as do the ever - closer links of today's global marketplace.

As I have stressed today, sustaining global growth will be a critical task during the years ahead. But it is wise to remember that it is not our only task, if we are to work together, East and West, to make the world, not just a richer but a safer and better place in which to live.

## Discussions

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**C** Dr. Il SaKong (Chairman & CEO, IGE)

Thank you Secretary Baker for your most illuminating presentation. I am sure Secretary Baker would be delighted to entertain any questions or comments from the audience.

**Q** Amb. Thomas Harris (British Ambassador to Korea)

In light of the success of the Uruguay Round, the renewed commitment to the multilateral trading system disciplines and rules, what sort of example do you think the United States is setting when it threatens unilateral section 301 action so soon after the conclusion of the Uruguay Round?

**A** Mr. Baker

That is a very good question. Let me say to you that I personally do not favor the concept of targets, goals or quotas to open up the Japanese market which, I would argue to you, is extremely closed, especially in the automobile sector. I think most countries in western Europe would agree on that point. I don't like the concept of managed trade and I also don't favor unilateral sanctions, at this point - this is a big caveat.

I think perhaps we would have been better advised to take the dispute to the WTO. Japan is taking it the WTO. Test the dispute resolution. We didn't give up any sovereignty when we

joined the WTO, so we can enforce our laws later on when that is necessary. And, I am not sure, from a process and procedural point of view, about going this quickly with section 301 relief. As I mentioned in my remarks, domestic political concerns always play a part in trade disputes and in protectionism. In this case, I think the United States is on the side of the angels. We have a stronger argument and I don't think it is wise to dilute it by resorting to unilateral sanctions right off the bat. There will be time for that. And when we joined the WTO, we didn't agree that our procedures and processes would be preempted by the WTO. Somehow a way must be found by Japan and rest of the world to deal with the huge structural surpluses. Don't let anyone argue to you that the Japanese car market is open. When a manufacturer of Japanese cars can tell a dealer that you can put my cars on your show room floor provided that you don't have any foreign cars, that is not an open market. It is not a tariff, but it is a non-tariff barrier. And, a strong Japanese government could see to it that it did.

**Q** Sang K. Han

As President Carter and Clinton performed a crucial role in global coordination, do you foresee yourself, as a major member of the Republican party, playing a role in improving the coordination between the United States and this region?

**A** Mr. Baker

Well, we have a divided government in the United States.



Under our constitution that is not unusual. Under a parliamentary system you don't experience that. We had a divided government under President Reagan and also under President Bush. In the Reagan years, except for 5-6 years, we had a completely Democratic Congress and under Bush, we had a Democratic House and Senate. It makes it more difficult for the chief executive when you have a Congress controlled by the other party.

I have some disagreements with some of the approaches the Clinton administration is taking in the Pacific. I mentioned one in my remarks. However, I think that what they have done on the APEC was absolutely the right thing to do. I was encouraged to see President Clinton emphasize the importance of APEC because I was there when APEC was born. I was also there when we lobbied to get Korea admitted after the first year and when it was determined that the second APEC ministerial meeting would be held in Seoul. Therefore, I think there are many things the current chief executive is doing that I strongly support. Moreover, the current administration had to change its policy on China after coming to office criticizing the Bush administration's pragmatic approach to China. Now, they are following our policy which is the right policy.

**Q** Dr. Se Eung Oh (Chairman, Foreign Affairs and National Unification Committee, National Assembly)

As a representative of the Korean National Assembly, I would like to ask what thoughts you have on the talks between the US and North Korea in Kuala Lumpur tomorrow. In addition,

as a partisan Republican policy maker, what is your opinion on the Geneva agreement?

**A** Mr. Baker

Let me first say that Bob Gallucci worked for me when I was secretary of state and he is an outstanding public servant. He was assistant secretary of state under me and, given the restrictions he was under and given the top-down policy direction he received, I think Bob Gallucci negotiated the best agreement he could have negotiated. However, I have a fundamental problem with the agreement that we have entered into with North Korea.

Having said that, I hope the talks in Kuala Lumpur are successful. I would like for the agreement to succeed since it is the course our government has embarked upon. But, I have serious doubts that it will. And, my doubts go back to the genesis of the agreement itself. It seems to me that, overnight, the US abandoned a policy that we had been pursuing for almost 40 years—a policy of approaching North Korea with strength. We abandoned a policy of carrot and stick and we went to a policy that contains nothing but carrots. We took North Korea's word that it would permit us to do 5 years from now something that North Korea, agreed with the international community she would do 2 years ago. So, what we got was an agreement to do 5 years from now what North Korea was obligated to do, by international commitment, 2 years ago.

For that, what did we give? We gave 500,000 metric tons of oil free a year, 4 billion dollars in light water nuclear reactors,

courtesy of South Korea and Japan, and diplomatic contacts and discourse. My problem is that I don't think North Korea keeps her word. And her actions so far would indicate that she does not. It seems to me that she finds every possible way not to perform the agreement. I think we made a mistake in abandoning an approach we took for 40 years and in flip-flopping under a threat of belligerency, belligerent threats of war, which was a mistake. I think the North Korean regime is clearly unstable and dangerous. But, I think they would tend to understand strength more than what I perceive as weakness.

What I would have done was what President Clinton was beginning to do when President Carter made a trip to North Korea. I would have gone to the Security Council of the United Nations and asked for political and economic sanctions just as we did in the case of Iraq; sanctions because the IAEA had asked the Security Council to sanction North Korea for her refusal to live up to the safeguards agreement. I don't believe China would have vetoed the sanctions at the time. Based on the conversations I personally had with the Chinese, I believe the Chinese don't want a nuclear capability on the Korean peninsula. So, I think that could have been an approach combined with the beefing up of the forces here on the peninsula along with a quiet communication to the North. The communication would have made the point that the United States deterred aggression for 40 years in western Europe where the Soviet Union had a vast conventional superiority. And, we did so through the mechanism of our strategic deterrent. I would have made the point that we intend to perform our security commitments in this region. I hope the agreement works even



though Washington decided to go the other way. Let's hope it works because if we have to switch back to that stronger approach, it will be all that much more difficult.

I should also add that I don't think we worked as closely with our South Korean friends as we should have. I have seen reports from here expressing dissatisfaction with the way the negotiations were handled and the extent to which South Korea was consulted and I understand this point.

**Q** Dr. Kihwan Kim (Senior Advisor, Kim & Chang)

My questions relate to APEC. As you know the Bogota agreement issued by leaders was a landmark achievement. It committed nations in the Asia-Pacific to free trade by 2020. The ministerial meetings in Osaka this fall should produce a blueprint to implement that declaration. And, everyone is concerned that the host country this year will be Japan when Japan is known to take a rather gradual approach to this goal. What sort of blueprint would you like to see presented at the Osaka meeting?

**A** Mr. Baker

Well, I think you need an aggressive approach, as I mentioned in my remarks. I think that is a very worthy goal and I think the other APEC members should pursue as forward-leaning and expansive an approach as you can. I would not think that the Japanese, just because they have a chairmanship, would stand in the way of fulfilling the commitment of last year's summit.

I think APEC is a really useful tool for liberalizing trade and investment in the Pacific. I think those of us who are members ought to use it. People sometimes ask why the United States has a problem with EAEC proposal. It is because it is exclusive and draws the line down the Pacific. There has been a line drawn down the Pacific once in this century with terribly adverse consequences and catastrophic war. If there are countries in East Asia that want to enter into a free trading agreement like we have in America we have no objection to that, provided that it is GATT consistent. What the United States has a problem with is a situation that Pacific nations form a trading group that excludes the United States.

**Q** Dr. Soogil Young (President, Korea Transport Institute)

Your exchanges with Dr. Kim established a good background for my question. A new concept under the name of Trans-Atlantic Free Trade Agreement has begun to be circulated. What is the background to this concept, how seriously should we take it, what is the American position on this and how should we relate it to America's commitment to APEC as well as your position against EAEC?

**A** Mr. Baker

If it is a free trade agreement and GATT consistent, then, there would be no objection to it. It is a brand new concept as far as I can tell, and I frankly have not seen a whole lot of discussion on it. I have also seen talks about AFTA—Asian

Free Trade Agreement. Maybe we will get to that and it is fine as long as it is GATT consistent. I don't think I would be too concerned with a North Atlantic Free Trade Agreement just like I don't think Atlantic nations should be concerned if there were to be an AFTA. The reason is that it increases overall economic activity.

**Q** Dr. Chang-Yoon Choi (President, The Korea Foundation)

Thank you Secretary Baker. I would like to know your views on the role of Russia in the years to come.

**A** Mr. Baker

I don't think there is any foreign policy issue that is of greater importance to the US and to the West than successful reform in Russia and the former Soviet Union. I think we should do everything we can to promote the success of reform in that region. I think we ought to be very careful, notwithstanding the humanitarian nightmare in Chechnya, to understand that Chechnya is part of the Russian Federation. While we can feel free to criticize the bombing of humanitarian civilian targets, we have to recognize that Russia is a nation of 21 federations. None of us has any interest in seeing Russia dissolve into anarchy and chaos. Therefore, we should be very careful in the Chechnya matter because it is a matter of Russian territorial integrity.

Contrary to what you read in the newspapers, I think the economy is doing better in Russia. Inflation is down, the ruble

has become quite stable, 35% of the work force now works in the private sector, 75% of all small businesses have been privatized. So, I think there are some good signs as well as some negative signs such as crime and lack of government control. Some people state that we stayed with Yeltsin too long. I reject that statement and I support the Clinton administration's commitment to Yeltsin. After all, he is the first democratically-elected president Russia has ever had in its history. So, who do you deal with if you don't deal with a freely elected president? I think we have a lot at stake in seeing successful reform in Russia.

Having said all that, I think it is important that the international community support reform in other republics in the former Soviet Union; not just support, but recognize their independence. Baltic states, Kazakstan, Azerbaijan, and a host of these new countries really want to separate from Russia and Russia is exerting some economic and political influence. Some of these countries like Belarus want to rejoin and form some sort of new alliance. We have a lot at stake there, but there are some talks about cutting off funding to Russia because of Chechnya and the sale of nuclear weapons to Iran. I think it is premature for us to cut off aid. Some in the US and other nations are even talking about forming an anti-Russian alliance. This is downright dangerous and stupid because I think that Russia is still making efforts to embrace western democratic principles.



**Q** Dr. Il SaKong (Chairman & CEO, IGE)

Before we conclude this morning session, I would like to ask the last question. Mr. Baker, you did mention in your formal remarks about G-7 cooperation. Also, we are well aware that the G-7 meeting went very well under your leadership. However, since you left your government, it seems like the G-7 is only paying lip-services. In this age of financial globalization, we experienced the Mexican peso crisis and unstable dollar-yen exchange rate problem. Therefore, some experts have proposed a new kind of international exchange rate system, for example, the flexible exchange rate band. Also, considering the G-7's legitimacy problem in coordinating international policies, some experts support a strengthened role for the IMF. What is your view on these issues?

**A** Mr. Baker

What I think necessary are better coordination and a more activist approach. I don't think we need a new international exchange rate system. I don't think we would be successful or that it would be necessary or wise. Back in the 1985-88 period, we were meeting almost every month at the deputy-finance minister level or the finance minister level and coordinating the underlying economic fundamentals of the countries in order to keep the currencies stable within an informal target zone system. We never admitted it at the time because target zones had a bad connotation, but that is what we were doing. As a result, we were able to achieve a certain degree of exchange rate

stability. I would like to see us get back to that system. I think it would work. Of course, to get there we would have to solve some trade disputes, for instance trade disputes between the US and Japan. With respect to whether the IMF should be the body as opposed to the G-7, I would strongly recommend against that for political reasons. It was hard enough to try to get an agreement between the major currency countries of the world in the G-5 or G-7 context. It is really difficult because coordinating the underlying economic fundamentals means taking actions that are not popular at home. In Germany, it meant reducing interest rates; in the US, it meant getting some spending reductions on the fiscal deficits; in Japan, it meant stimulating domestic demand. And, those things are hard enough to achieve in the form of G-5 and G-7 countries and it would be almost impossible in the larger form of the IMF. What I think is needed is not a new system, but rather better coordination, more work, more political will and an activist approach and maybe we can take another look at the target zone system that I think worked quite well in terms of promoting exchange rate stability.

