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DISSEMINATION CONTROL ABBREVIATIONS

NOFORN-	Not Releasable to Foreign Nationals
NOCONTRACT-	Not Releasable to Contractors or Contractor/Consultants
PROPIN-	Caution-Proprietary Information Involved
ORCON-	Dissemination and Extraction of Information Controlled by Originator
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Central Intelligence Agency



Washington D.C. 20505

DIRECTORATE OF INTELLIGENCE

17 January 1985

South Korea: Economic Performance
and Defense Spending [redacted]

25X1

We estimate South Korea's economic growth in 1984 was 7.5 percent, yielding a GNP of \$79 billion and putting South Korea once again among the world's growth leaders. The 9.5 percent real increase in GNP in 1983 was particularly important for President Chun because it was the first time his government achieved the high growth Koreans had come to expect during the Park years [redacted]

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Seoul has not only achieved high growth with low inflation -- a goal few economists thought possible -- but also reduced the current account deficit from \$2.6 billion in 1982 to \$1.6 billion in the last two years. Given Seoul's economic performance, South Korea has had little trouble attracting foreign capital to meet its financing needs despite its growing debt, which now totals \$43 billion [redacted]

25X1

President Chun and his economic advisers can take much of the credit for current economic conditions. When he came to office in 1980 Chun strengthened the austerity program begun by the Park government to wring high inflation and the expectation that it was a fact of life out of the economy as well as to curtail the growing foreign debt. Korean economic planners believed stable prices were mandatory for high growth during the 1980s [redacted]

25X1

This memorandum was prepared [redacted] Korea Branch, Northeast Asia Division, Office of East Asian Analysis for Admiral Burkhalter of the Intelligence Community Staff in preparation for his trip to the Far East. Comments and queries are welcome and may be addressed to Chief, Korea Branch at [redacted]

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Austerity remains the watchword in 1985. The growth in the money supply, which was reduced from 28 percent in 1982 to 15 percent in 1983, is targeted at only 9.5 percent this year. The 1985 budget, which provides a small surplus, pegs the increase in government spending to the rate of economic growth. [REDACTED]

25X1

Barring external shocks, we project 1985 as a good year for the Korean economy. South Korea is favorably positioned to achieve 6.5-7 percent real GNP growth. By gradually depreciating the won and keeping inflation low, Seoul will maintain its export competitiveness. [REDACTED]

25X1

In its defense spending for 1985, the South Koreans are concerned that new accounting ground rules for GNP required by the IMF would make it difficult for Chun to meet his pledge of allocating 6 percent of GNP to defense. To do so would require a boost of better than \$500 million in defense expenditures and force a sharp reduction in outlays in nondefense areas. We believe Seoul will make a serious effort to again reach the 6-percent target. Although slower economic growth this year will make the targeted ratio easier to attain in the short term, maintaining the ratio over the long term may become difficult because of declining growth in revenue. [REDACTED]

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Over the medium term South Korea's economic performance will depend heavily on global economic conditions and Seoul's ability to move up the technology ladder. Seoul has promulgated economic reform measures aimed at encouraging increased inflows of foreign equity investment particularly in technology-intensive sectors. These new regulations should increase the placement of technologically advanced products and processes in industries such as transport equipment, chemicals, electronics, and semiconductors, areas in which the United States in particular excels. General Motors and IBM are among the many companies who have recently announced large equity investments in South Korea in technology-intensive ventures. [REDACTED]

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[redacted]
Central Intelligence Agency



Washington, D.C. 20505

DIRECTORATE OF INTELLIGENCE

17 January 1985

Seoul's Bid for a Stronger Defense:
Force Improvement Plan II;
Third Country Sales of Military Equipment [redacted]

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Seoul's 1982-86 Second Phase Force Improvement Plan (FIP II) is designed to fill some specific gaps in South Korea's defenses, but it will not significantly alter the military balance on the peninsula. We believe the South will, in fact, fall further behind the North even with FIP II, and that the US troop presence will remain the most effective deterrent to a North Korean invasion during the 1980s. [redacted]

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The North's most threatening military advantage is in key ground force categories -- such as tanks and armored personnel carriers -- and its lead in these weapons probably will increase over the course of FIP II. Seoul will probably reduce its current disadvantage in long-range artillery, but P'yongyang will increase its lead in modern, mobile, self-propelled artillery. In naval power, P'yongyang probably will widen its lead by constructing more naval combat vessels than Seoul. [redacted]

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The South has made its biggest gains in recent years in the air balance and probably will continue to maintain its current advantage. Recently available information, however, indicates

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the North is preparing to build its own fighter aircraft, and this could prevent Seoul from significantly increasing its advantage in this area in the late 1980s. [redacted]

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Several key considerations have shaped Seoul's commitment over the past decade to strengthen its defense:

- o A perception in Seoul -- less acute now than during the Carter administration -- that the United States eventually might withdraw all its forces from the Korean Peninsula.
- o A growing desire to provide better forward defenses north of Seoul, an area that by mid-1970s had grown to encompass nearly a fourth of South Korea's population and industrial capacity. [redacted]

25X1

Seoul's military improvements, however, have lagged far behind those in the North, primarily because there are important economic constraints on defense spending. The Chun government, following the precedent of President Park, has continued to place a high priority on economic development as a means of fostering political stability in the South -- stability believed to be essential to deterring North Korean aggression. Planners believe defense spending above 6 percent of GNP will slow economic growth. [redacted]

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Planners also may be apprehensive that the more quickly the South approaches defense self-sufficiency, the sooner the United States may again be tempted to withdraw its forces from Korea, removing what many regard as the single greatest deterrent to North Korean military action, regardless of the Seoul-P'yongyang military balance. [redacted]

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Over the past decade, Seoul's military improvements have increasingly been supported by a rapidly growing defense industry that is based largely on US technology. The defense industries are saddled with significant idle plant capacity and are suffering financial losses because requirements for many basic items of military equipment have been met. Seoul's efforts to support the defense industries through third-country sales have been frustrated by US-imposed restrictions. Last year, Seoul cancelled lucrative sales of both lethal and nonlethal military items to Iran in response to US demarches on denial of support to the warring Gulf States. [redacted]

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