

# South Korean Trade Policy and FTAs

By *Chulsu Kim*

IT is well known that South Korea's economic growth in the last several decades has been based on an outward development strategy. This strategy has helped to transform the country from a subsistence agrarian economy in the early 1960s into the 12<sup>th</sup> largest trading nation today. Trade has been and continues to be the engine of growth. Exports and imports now constitute nearly 70% of Korea's gross domestic product (GDP).

In the earlier years of economic development in the 1960s, Korea's trade policies emphasized export promotion, particularly of labor-intensive light industrial products, such as textiles and footwear. In the 1970s, the emphasis shifted to policies aimed at promoting several key heavy and chemical industries which later became the backbone of Korean industry. While export promotion continued to be the mainstay of trade policy during this period, a strong element of import substitution was injected to protect the targeted "infant" industries, such as electronics, petrochemicals, shipbuilding, automobiles, machinery and steel. In the 1980s, when Korea emerged as a more important trading nation, its trade policy priorities shifted to market opening policies and improving trade rules so as to make them consistent with international standards. In the 1990s and onward, Korea's trade policy concerns centered around the multilateral trade initiatives such as the Uruguay Round. In the late 1990s Korea began to consider regional trade agreements (RTAs) as a trade policy instrument. Today this is one of the most important aspects of Korea's trade policy, along with policies with respect to the multilateral trade initiatives in the World Trade Organization (WTO), such as the Doha Development Round.

For many years, Korea had a negative view on regionalism and did not conclude RTAs. This policy was based on the premise that as a nation engaged in

global trade, Korea's trading interest would not be promoted by membership in RTAs, and that such arrangements might lead to mutually exclusive trading blocs that could undermine the multilateral trading system. Korea has, however, participated in regional economic cooperation agreements such as APEC for some time and has taken part in a limited number of preferential tariff arrangements among developing countries such as the Global System of Trade Preferences (GSTP), the Bangkok Agreement among Developing Member Countries of the Economic and Social Commission for Asia and the Pacific, and, since 2000, unilateral tariff concessions to the least developed countries.

The recent proliferation of RTAs, including some in Asia, particularly since the mid-1990s, has changed the minds of Korean government policymakers about membership in RTAs. RTAs are increasingly seen as an effective way of maintaining export markets and inducing foreign direct investment in Korea. The Korean government now takes the view that free trade agreements (FTAs), if properly concluded and managed in accordance with the relevant rules, can supplement the multilateral trading system and contribute to market opening in the world through bilateral and regional acceleration of trade liberalization.

## ■ Korea-Chile FTA

It is under these circumstances that the Korean government decided to negotiate an FTA with Chile in November 1998. The choice of Chile was based on the reasoning that it was one of the fastest growing economies in Latin America and could serve as a gateway to the region for Korean products. The fact that Chile had an extensive FTA network in the region was also an important consideration. Also, Korea's trading interests in Chile could be

adversely affected in the absence of an FTA with that country. The bilateral FTA negotiation, which began in December 1999, was concluded three years later in October 2002, and signed early in 2003. The agreement having been already ratified by the parliaments of the two countries, it was implemented as of April 1, 2004.

The Korea-Chile FTA (KCFTA) covers a comprehensive range of economic relations between the two countries, including trade in goods, investment, services, competition policy, government procurement and intellectual property rights. As far as trade in goods is concerned, both countries will eliminate import tariffs on 96% of the goods, in terms of tariff lines, within 10 years. Special provisions have been adopted on import sensitive items such as agricultural products in the Korean market. For rice, apples and pears, tariff elimination will not apply; for some products such as beef and chicken, tariff rate quotas are being introduced; for others, longer phase-out periods have been provided. Similar exclusions, limitations and longer phase-out periods have been agreed upon concerning Korean exports of some manufactured products to the Chilean market.

In the field of investment, national treatment and most-favored-nation treatment are to be accorded to the investment of the other party. Neither party may impose or enforce performance requirements and/or nationality requirements for senior management positions. In cross-border trade in services, both parties agreed to accord national treatment to services and service providers of the other party and neither party may require local presence as a condition for the cross-border provision of services.

In intellectual property rights, both parties agreed to protect geographical indications. The parties also agreed to cooperate in competition policy matters

in various ways, including exchanging related information. In government procurement, national treatment will apply and discriminatory practices such as the priority purchase of domestic goods and offset requirements will be prohibited.

In the KCFTA, which was the first FTA concluded by Korea, liberalization in the agricultural sector proved to be more difficult than originally anticipated as the trade in that sector was rather limited. This turned out to be a major hurdle not only in the negotiations but also in the ratification procedures, which took more than a year after the agreement was initiated in February 2003. Similar difficulties are expected in Korea's future FTAs with countries with substantial agricultural sectors.

### The FTA Roadmap

The new Korean government of President Roh Moo-Hyun seems determined to pursue other FTAs both regionally and trans-regionally. It announced the FTA Roadmap of the new government in August 2003. This points out the proliferation of FTAs in the world as well as in Asia and the risks they present to Korea if it remains isolated from these developments. It also points out that Korea needs a new catalyst in the international arena, in the form of FTAs, to restore its dynamism for growth as well as to provide a fresh impetus for economic reform. In view of this, Korea needs to pursue FTAs actively and strategically on multiple fronts. And Korea should negotiate FTAs with as broad a scope as possible, so as to maximize their economic benefits, while remaining consistent with the WTO.

As far as the choice of FTA partners is concerned, the Roadmap points out that big trading nations are ideal partners and FTAs with them should be pursued actively in the medium to long term. In the short term, however, the following



Former South Korean President Kim Dae-Jung (second from right) shakes hands with former Chilean Foreign Minister Cristián Barros after signing documents on a free trade agreement. Chilean President Ricardo Lagos (second from left) and former South Korean Foreign Minister Choi Sung-Hong also participated in the ceremony

criteria, among others, should be used to choose prospective FTA partners: (a) economic justification; (b) political and diplomatic considerations; (c) willingness of countries to conclude FTAs with Korea; and (d) potentiality of countries to serve as stepping stones to larger FTAs.

### FTAs with Singapore and Japan

In accordance with the Roadmap, the Korean government began FTA negotiations with Singapore and Japan at the end of 2003. The negotiation with Singapore followed a year of joint feasibility studies between the two countries. It is expected that the negotiations will be concluded in a relatively short period, possibly in 2004. As to the Korea-Japan FTA, it may take much longer to finish negotiations given the larger stake involved on both sides and the complex economic and political issues between

the two neighboring countries.

On Oct. 20 last year, President Roh and Prime Minister Koizumi Junichiro announced their intention to begin negotiation of a Korea-Japan FTA (KJFTA) with a view to completing the negotiations sometime in 2005. They endorsed the principles of comprehensiveness, substantial liberalization, mutual benefit and consistency with WTO rules and regulations as the guiding principles of this agreement. In accordance with this leaders' agreement, the two countries held the first negotiation meeting in Seoul on Dec. 22, 2003. At this meeting, they agreed on negotiating structures, including the establishment of negotiating sub-groups and the intervals of future meetings. The substantive negotiations began at the second meeting held in Japan in February this year.

Perhaps due to the fact that considerable discussion has already been held on

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South Korea and Japan held the first meeting for a Korea-Japan FTA in Seoul on Dec. 22, 2003

many aspects of the KJFTA at various levels, the two sides are in much agreement as to the basic principles to be applied in negotiating the bilateral FTA. Both governments also seem to share the view that their FTA should serve as a catalyst for creating broader regional economic integration such as a trilateral FTA involving Korea, Japan and China and, eventually, an East Asian Free Trade Area (EAFTA), involving the ASEAN countries and the above-mentioned three countries in Northeast Asia. They also seem to be committed to a high-quality FTA, with the KJFTA serving as a model for other economic integration efforts in the region as well as in other parts of the world. These common perceptions should go a long way to facilitate the negotiating process.

There have been many studies in Korea and Japan on the economic impact of the KJFTA on both countries. Generally speaking, they show substantial long term benefits for both countries. Seen from the perspective of Korea, these studies show that a bilateral FTA may in the short term worsen the present long-standing trade imbalance in

favor of Japan, but that its dynamic impact in the longer term would more than offset this short-term disadvantage, by promoting investment, increased competition, economies of scale and better utilization of resources of Korean industries in the expanded market.

Given the substantial trade and other economic ties and the high level of exchanges in other areas between the two neighboring countries, the FTA negotiation is expected to grapple with many difficult issues, including political ones. As the smaller and less developed partner, the difficulty is expected to be greater on the part of Korea. The most obvious difficulty for Korea may be the speed with which it can move on the path of liberalization in the manufacturing sectors where Korea is seen as less competitive than Japan, for example, in the automotive, electronics and machinery sectors. It is expected that Korea, in the FTA negotiations, will also raise the issues of private non-tariff measures, technology transfer, promotion of Japanese investment in Korea and other issues of economic cooperation in the FTA negotiations. As the Japanese gov-

ernment has traditionally considered some of these issues as problems of the private sector and not a subject of negotiation at the government level, the extent to which Japan can accommodate these Korean concerns may affect pace of the negotiations. On the other hand, the issue of liberalization in agricultural and fishery products may give the Japanese side some difficulty, although the Korean exports of these products to Japan are not that large.

Seen from this perspective, the KJFTA negotiations are likely to face some obstacles on both sides, which will not be easy for the working negotiators to resolve. Strong political leadership will be required to fulfill the aim of concluding the negotiations in 2005. I also believe that considerable work remains to be done to bring public opinion to support the KJFTA, particularly in Korea. While a good start has been made, it will be a big challenge for the negotiators of Korea and Japan to conclude the negotiations before the end of 2005 as agreed by their two leaders.

As negotiations have already begun with Japan and Singapore, Korea's FTA policy priorities will be these two countries for the time being. As the originator of the idea of an EAFTA, the Korean government is interested in realizing in the long term a trilateral FTA among Northeast Asian countries, and in the ultimate goal of forming an EAFTA. In the short term, however, the Korean government may seek to negotiate FTAs with ASEAN as a whole, or with some of its individual members, with Mexico and with the European Free Trade Area (EFTA), among others. **JS**

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