

# Trade Policy and National Economic Interests in Korea

I.A. Korgun, V.N. Zuev<sup>1</sup>

---

**Irina Korgun** – Senior Research Fellow, The Institute of Economics Russian Academy of Science; 38 k. 1 Novocheremushkinskaya Ulitsa, Moscow, Russian Federation; E-mail: irinakorgun@gmail.com Moscow, Russian Federation; E-mail: irinakorgun@gmail.com

**Vladimir Zuev** – PhD, Professor of Economic Sciences, National Research University Higher School of Economics; 20 Myasnitskaya Ulitsa, Moscow, 101000, Russian Federation; E-mail: vzuev@hse.ru

## Abstract

*Membership in the World Trade Organization (WTO) and participation in free trade agreements (FTAs) are important instruments for governments to realize national economic interests. The Republic of Korea has been particularly successful in doing so. As the experience of Korea shows, a trade policy mix between multilateral liberalization under the WTO and preferential liberalization through FTAs allows the government to optimally balance national interests and strive for higher levels of social welfare and economic effectiveness, while simultaneously protecting national industries. However, such results seem to be possible only if national economic interests are clearly defined and are synchronized with a country's goals regarding WTO membership and its strategy for FTAs. During recent decades, Korea has practiced an active long-term planning of trade policy so that trade benefits are not excessively concentrated in a narrow range of trade actors and are distributed more evenly in society. This meant appropriate balancing of liberalization and protection measures, reinforced by special support programmes that neutralized the negative impact of higher market openness. In this article, Korea's strategy regarding trade policy is analyzed, including the reasons Korea pursued an FTA-centric policy and the benefits it obtained in addition to those it obtained from WTO membership.*

**Key words:** trade policy national economic interests; World Trade Organization; free trade agreements; Korea

**For citation:** Korgun I.A., Zuev V.N. (2020) Trade Policy and National Economic Interests in Korea. *International Organisations Research Journal*, vol. 15, no 2, pp. 169–183 (in English). DOI: 10.17323/1996-7845-2020-02-11

## Introduction

Trade policy is an important tool that can be used to stimulate growth of a country's national welfare. The role of trade policy is determined by its close links with spheres of trade, production, investment, and technological exchange, as well as by its fundamental role in promoting and protecting the interests of national manufacturers. Korea belongs to a group of states that achieved remarkable economic success due to an active use of trade policy that led to improvements in each of the areas mentioned above and beyond. Before the Uruguay round of multilateral negotiations began, Korea had been passively involved in discussion on liberalization

---

<sup>1</sup> Author would like to thank the Department of World Economy and World Politics of HSE for help in preparing this study.

of trade under the General Agreement on Tariffs and Trade (GATT), the predecessor of the World Trade Organization (WTO). However, when the round began in 1989 it became obvious that the multilateral trading system could offer the export-oriented Korean economy numerous benefits by bringing down barriers to international trade. The realization of new possibilities turned Korea from a passive developing country into a proponent and active user of trade policy as a tool to increase national welfare. Growth opportunities that the WTO opened for the country were in later years multiplied through free trade agreements (FTAs) that Korea had pursued since the end of 1990s.

This research analyzes the evolution of Korea's trade policy in 1990–2010s by focusing on the country's transition from a WTO-centric trade policy to an FTA-centric policy, identifies key elements of its FTA strategy, and investigates the effects of trade policy. Certain tactical manoeuvres that Korea used in order to protect and at the same time to promote its economic interests within the WTO are highlighted, as well as how the country changed from being a passive observer of negotiations on trade into an experienced negotiator capable of initiating agendas with its FTA partners. The research indicates that Korea's success was founded on a deep understanding of the nation's fundamental economic interests and the necessity of aligning trade policy with them. In Korea's case, economic rather than geopolitical or strategic interests have always been a priority in its trade policy. The Korean government has sought to go beyond an incremental increase in macro indicators, or creating benefits for certain groups of manufactures, to achieve higher economic efficiency of the national economic system. Business interests were considered based on their role in the national economy and their ability to contribute to economic growth.

The article offers conclusions regarding the key elements that have made Korea's trade policy successful which can be borrowed by other countries, including Russia.

## Korea's Economic Interests and Their Place in Trade Policy

Numerous studies analyze relationship between trade policy and welfare. One of the first works on the problem, entitled "Trade and Welfare," was published by Nobel Prize-winner J.E. Meade in 1950s [1955]; this work laid the foundations for other significant research on the issue. Some of the more widely known works include the contributions of M. Amiti et al. [2017], R. Baldwin [1989], M.L. Busch and E. D. Mansfield [2011], W.M. Corden [1997], J. Eaton and G.M. Grossman [1986], K. Handley and N. Limão [2017], P.R. Krugman and Obstfeld [2009], and U B. Marchand [2017]. Although this list is far from exhaustive it supports the idea of the potential of trade policy to influence national welfare. This influence is even more obvious in case of small, open economies, a group of countries to which Korea belongs.

Korea is highly dependent on international markets. Its exports and imports combined exceed 80% of the country's gross domestic product (GDP), pointing to the strong influence of the external sector on the domestic economy and, consequently, on trade policy. Historically, Korea was successful in its economic achievements because it relied on an export-oriented growth model [World Bank, 1993, pp. 127–130]. This link between growth and export performance shaped national economic interests.<sup>2</sup> Over years these interests were carefully calibrated and adapted in order to reflect changes in international and domestic economies, and policies to achieve them were re-aligned with new realities. At the early stages of development when the foundations of Korea's manufacturing industry were created, trade policy was subordinated to industrial policy, prioritizing the protection of national manufacturers from competing imports and rewarding aggressive export manufacturers [Amsden, 1992, pp. 139–55]. As a result, trade-

<sup>2</sup> For more on Korea's economic nationalism see [Lee, Lee, 2015].

related measures were increasingly protectionist. But in later years the situation had changed, prompted by the demand for a more liberalized and open foreign trade which has emerged from within the country.

As Korea's economy became more complex, it accumulated competitive advantage and integrated into global production and distribution networks, which lead Korea's policymakers to turn their attention toward achieving a higher degree of openness. Representatives of strong manufacturing industries like electronics, auto- and chemical industries, too, supported liberalization as they viewed it from the perspective of more growth through international expansion [Gills, p. 667]. However other industries were still too weak to be subject to international competition. So, Korea needed a solution that would balance limited liberalization with protection. Under those circumstances, liberalization under the rules of the international trading system was seen as an optimal choice because it was possible to combine reasonable openness with protection of sensitive industries [Kim, 2004]. In addition, as a member of the WTO, created in 1995, Korea had access to a dispute settlement mechanism that allowed it to resolve trade conflicts and prevent unfair trade practices applied by other member-economies.

Attitudes toward liberalization underwent a greater change at the end of 1990s as Korea entered a phase of economic reform. At the end of 1990s the industrial dirigisme of previous decades no longer served the needs of Korea's more advanced economy; the country needed more flexibility and openness to continue to grow. As a result, an FTA strategy was formulated and occupied a central place in the transition. It is reasonable to question why, at that time, Korea diverted its attention away from the WTO, which it had praised for creating new development opportunities just a few years before. This can be explained by two major factors: a failure to achieve swift progress on Doha Development Agenda (DDA), and the greater emphasis placed on regional integration by the U.S. and EU. Progress on the DDA was essential for the Korean government to realize its ambitions to grow into an advanced economy, but as the process stalled Korea switched to preferential agreements that could unlock capacity for the further increase of Korea's export's and, thus, sustain dynamic growth of the national economy [Sohn, Yoon, 2001, pp. 11–5]. In addition, preferential agreements, represented largely by FTAs, allowed Korea to proceed with its economic reform plan, triggered by the Asian financial crisis of 1997–98, to increase flexibility and efficiency of the system and domestic economic institutions, and to strengthen intra- and extra-regional cooperation [Ibid.].

The Korean government aligned WTO- and FTA-related issues with the country's long-term development goals focused on creating an advanced economy. Ministries engaged in continuous work to simplify regulation and harmonize evolving trade rules and measures with ongoing structural changes in the economy. For example, as the country's manufacturing sector embarked on a globalization strategy and strengthened its international positions in the 1990s, governmental support was reconfigured toward the service sector in the 2000s in order to lead this sector to successful internationalization. Such timely adjustments of priorities have helped to maximize benefits on the national level: when trade policy was used to solve problems of certain industries, it used a complex, multifaceted approach that took into account interests of all parties – the state, business and society. If entry barriers for manufactured goods were removed, companies became eligible for indirect support of their activities, in the form of easier access to finance or additional government orders, which neutralized potential negative effect from liberalization.

Let us consider how some of the major indicators characterizing Korea's level of welfare have changed during the period of active trade policy from 1990–2018. According to statistics prepared by the United Nations Conference on Trade and Development (UNCTAD) and presented in Fig. 1, during this period the country's GDP increased fourfold from \$360 billion to more than \$1,600 billion. Another very important welfare indicator – GDP per capita – grew

at a similar magnitude from \$6,500 in 1990 to \$31,700 in 2018. Growth of these indicators in Korea looks even more remarkable if the fact that the country had to recover after two serious downturns is taken into account. One of the downturns followed the Asian financial crisis of 1997–98 and the second one was caused by the financial crisis of 2008. Despite these, Korea managed to make the transition from the group of higher middle-income countries to the high-income cohort.<sup>3</sup> Also, in 1996 Korea joined the Organisation for Economic Co-operation and Development (OECD) – an organization with members from developed economies only – an event that recognized Korea’s economic achievements (although by the World Bank’s classification it still formally belongs to a group of developing countries).

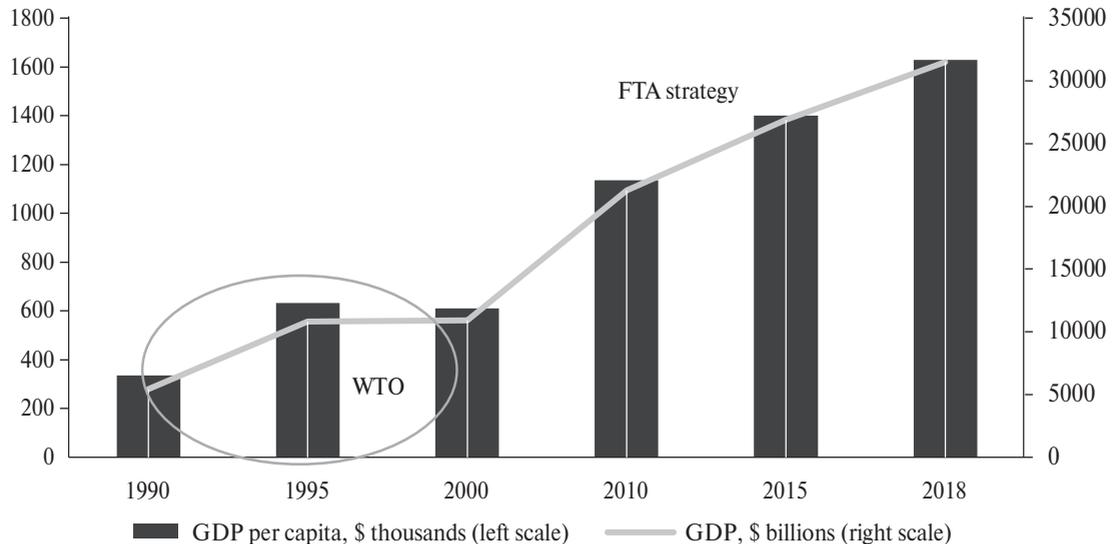


Fig. 1. Korea’s GDP and GDP per Capita in 1990–2018 and Phases of Its Trade Policy

Source: [UNCTAD, n. d.].

Trade growth, both in absolute indicators and as a share of world trade, was another achievement that Korea realized in the course of its active trade policy. For example, during 1990–2018, overall exports increased 9.3 times more dynamically than imports (which grew 7.7 times) despite starting from approximately the same level (Fig. 2). Trade liberalization through FTAs has contributed to this growth. Moreover, due to favourable terms of trade (higher exports and lower imports) Korea accumulated a significant trade surplus: in 2018 it was equal to \$69.6 billion, or almost 10% of Korea’s total exports. The existence of a surplus was a major change from previous decades during which Korea had struggled to keep its imports at lower levels than exports. Export growth had a positive impact on Korea’s share of the world trade, which grew from 1.8% in 1990 to 3.1% in 2018.

Adaptation of national trade policy to WTO, and later FTA, requirements has transformed Korea’s role in the international division of labour. In the 1990s Korea was predominantly a supplier of finished goods, but liberalized and simpler trade procedures have facilitated its transition to a supplier of intermediate products. In a study done by the WTO and the Japan External Trade Organization (JETRO) in 2011, it was emphasized that the country had improved its position as a supplier of high-tech intermediate products within Asian value chains

<sup>3</sup> In 1990, high income level was \$7,620; by 2018 it had risen to \$12,376 [World Bank, n. d.].

[IDE – JETRO, WTO, 2011, pp. 85–6]. Consequently, this change was reflected in the product structure of Korean exports. As of 2018, the share of intermediate goods in Korea’s industrial exports was 36% [World Bank, n. d.]. Specificities of trade in intermediate goods prompted the development of related services in Korea, stimulating further growth of the service economy. Korean logistic, insurance, and financial sectors became much stronger players as a result of their new role within regional and global value chains.

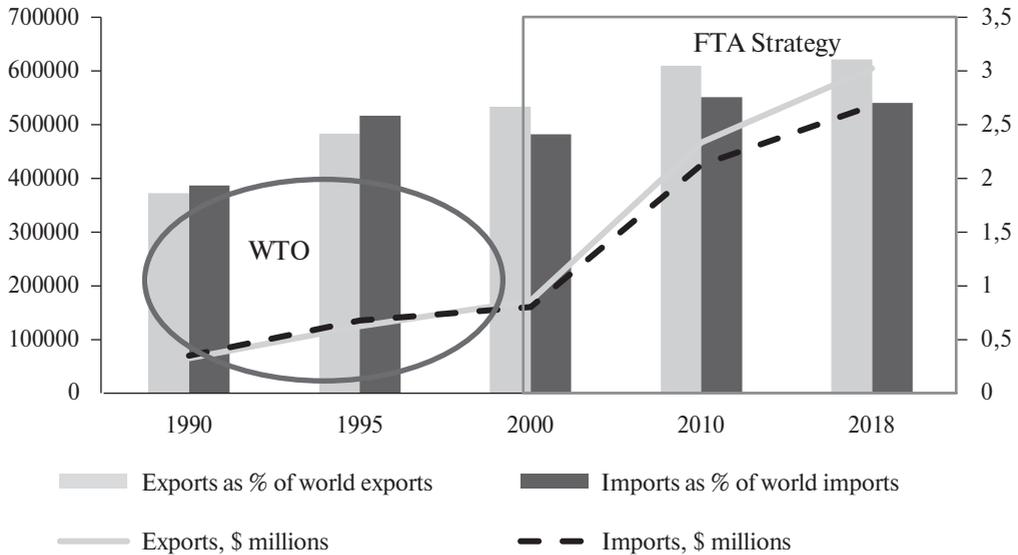


Fig. 2. Korea’s Foreign Trade, 1990–2018

Source: [UNCTAD, n. d.].

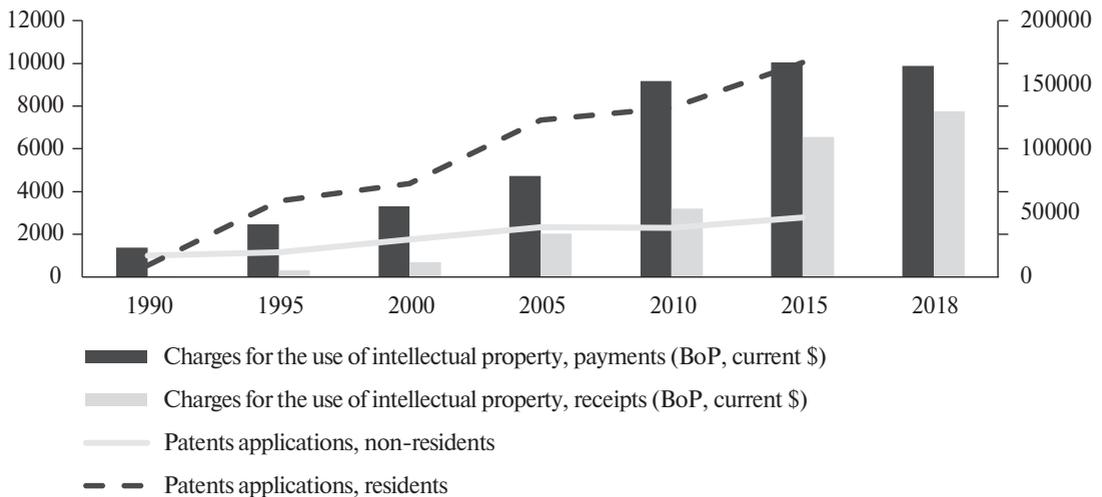


Fig. 3. Number of Patent Applications and Proceeds for the Use of Intellectual Property Rights and Korea’s Balance in Technological Trade

Source: [World Bank, n. d.].

Another important change that reflects how much Korea has gained in welfare occurred in the technological sphere. Korea has become a leader among OECD countries in research and development (R&D) spending relative to GDP, raising its gross financing of R&D from 2% of GDP in 1990 to 4.2% in 2018. More importantly, this spending generated results in the form of actual increases in patenting activity. In 1990 non-residents had outperformed residents in the number of applications for patents (Fig. 3), while in 2018 the situation reversed as residents applied for 167,000 patents versus 46,000 filed by non-residents [OECD, 2019]. As a result of this growth, Korea started to receive income from the transfer of intellectual property rights (as reflected in Fig. 3). Of course, this did not change Korea's status as a net-importer of technology, but it is a positive, stable trend toward greater exports of innovation products.

## The WTO and Korea's Economic Interests

The international trading system, formerly GATT, played a central role in Korea's economic achievements [Hyun, 2003]. Being part of the system from the early years meant that Korean trade policy has had an opportunity to observe changes in global approaches toward trade policymaking and develop in tandem with them. GATT rules regarding most-favoured-nation (MFN) and a clause about market access for the least-developed countries gave Korea opportunities to pursue a limited trade openness for imported inputs and at the same time practice industrial protectionism. The least-developed country clause unlocked access to developed markets and made Korea eligible for low levels of import tariffs when exporting to advanced countries while maintaining high import tariffs for industrial goods at home. The "infant industry" argument, very common among developing countries in the 1970–80s, also helped to justify protectionism [Korgun, Popova, 2011].

After the WTO was created, Korea continued to receive the benefits associated with its developing-country status despite the success of its development programme. This status enabled more flexible schedules for tariff reduction and longer adjustment periods for sensitive industries. In Korea's case, agriculture, the service sector and the sphere of intellectual property rights benefited from arrangements that allowed longer timelines for bringing national regulations into compliance with WTO norms. The Korean government used this time wisely and introduced measures to support weak sectors (mostly R&D financing) and to prepare them for future liberalization.

As a result of the Uruguay round, Korea accepted a level of liberalization for its industrial sector on the same scale as developed countries; in effect, this meant that Korea was ready to abandon distortional policies for industrial protection, such as high tariffs, preferential financing, and the subsidizing of domestic manufacturers. Table 1 provides a snapshot of how Korea has kept its commitments for industrial market access and tariff binding in the WTO. As the numbers show, progress was substantial: the average applied rate decreased from 20% to 9.8% for industrial goods and from 72.4% to 58% for agricultural products in 1996–2018. In addition, Korea joined some countries in initiating an agreement on 0%-level tariffs for trade in electronic goods and information technologies.

Assessments conducted by the Korean government found that during the first several years following the creation of the WTO, Korea gained \$28 billion as a result of lower barriers to exports negotiated during the Uruguay round [Republic of Korea, 1996, p. 20]. In 1995 Korean exports were worth \$125 billion and multilateral liberalization of trade added approximately 20% to that, stimulating domestic industrial production. More flexible terms of liberalization in other sectors mentioned above, were, also considered a success and in line with national economic interests.

*Table 1.* Changes in Korea's Tariff Rates After the WTO Was Created, 1996 and 2018

	1996		2018	
	Simple Average	Simple Average MFN Applied	Simple Average	Simple Average MFN Applied
Binding Coverage, %	91.0		94.9	
Tariffs	Simple Average	Simple Average MFN Applied	Simple Average	Simple Average MFN Applied
All tariff lines	27.6	14.4	16.5	13.7
– agricultural products	72.4	51.8	58.0	57.0
– non-agricultural products	20.0	7.7	9.8	6.7

*Source:* [Republic of Korea, 2004, p. 43–44; WTO – ITC – UNCTAD, 2019, p. 111].

Thus, despite having formal status as a developing country, until October 2019 Korea practiced a dual status inside the WTO, trying to realize gains meant both for developed and developing countries. This dual status markedly differentiated Korea from other member-economies that belonged either to developing or developed groups of countries. This dual status laid the groundwork for a sophisticated manoeuvring of trade policy by Korea which is still viable in today's FTA-centric trade policy.

Fundamentally, the Uruguay round was the first round of negotiations in which Korea openly faced pressure from developed countries had to be active in protecting its interests. Successful results and apparent benefits for the national economy transformed how Korea approached the formulation of its trade policy, and actually brought trade policy to the forefront of instruments used to increase national welfare. From that point on, Korean trade policy became very active, and at times even aggressive, when thinking about the multitrack FTA strategy it had pursued since late 1990s. The normative aspect of the WTO's rules for trade regulation was borrowed and implemented in Korea's FTA strategy. Issues regulated by the WTO formed the basis for texts of FTAs and lack of progress in further WTO negotiations made Korea broaden scope of its FTAs.

Finally, China's accession to the WTO in 2001 had a positive impact on the Korean economy. At a time when Korean economy was struggling with sluggish domestic demand after the domestic credit card bubble of 2003, Chinese was able to support Korean manufacturing and GDP growth. The correlation coefficient between rates of GDP growth and growth rates of Korean exports to China in the 2000s (Fig. 4) is very strong, suggesting the existence of dependency. For 2003–13 the correlation ties are even stronger, reflecting the growing dependence of Korea's economic performance on external trade to enhance the value of the trade policy overall.

Due to China's commitment to decrease barriers to trade, Korean companies, both large and small- and medium-sized business, received opportunities to enter one of the world's biggest markets. The geographical proximity of the two countries was an additional advantage. As a result, in 2004 China became the largest trade partner of Korea, making up 30% of Korea's total foreign trade [KITA, 2019]. Also, China become the largest recipient of Korea's outward foreign direct investment (OFDI) as in 2003–05 40% of Korea's total OFDI went to China's manufacturing industries [The Export-Import Bank of Korea, n. d].

Korean FDI in China contributed to the development of regional and global value chains. While Korean firms supplied intermediate inputs, they were also filling up demand for domestic manufacturing industry. Until 2013 over 35% of parts and components exported from Korea went to China. In addition, since 2005 intermediate products have made up more than 60% of Korea's total exports to China [KITA, n. d.]. High-tech industries were strongly involved

in this trade exchange from Korea's side; in particular electronic, electric machinery, and auto industries have benefited the most since they provided more than half of the country's intermediate exports [Ibid.]. According to research by the Korean Institute of International Economic Policy, the formation of such manufacturing and distribution networks improved competitiveness and effectiveness of Korean business in the international arena.

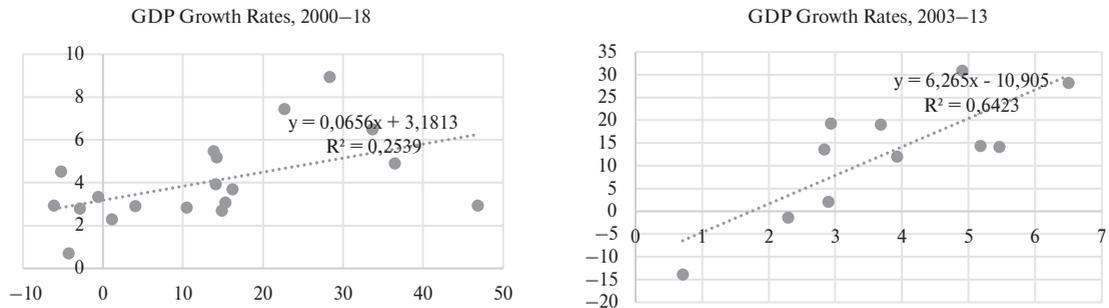


Fig. 4. Results of Correlation Analysis Between Rates of Korea's GDP Growth and Growth Rates of Export to China in 2000–18 and 2003–13

Source: Calculated by the authors.

Overall, the GATT and WTO multilateral trading system presented Korea with real opportunities to realize the potential of its export-oriented industry, increase the scale of its economy, and adapt its domestic regulation system to international practices. Korean companies employed opportunities created by reduced barriers to trade as they were able to increase export production and improve their international standing despite slower domestic demand. While the export sector was growing, the Korean government took measures to protect and support sensitive sectors, providing tools to prepare them for future liberalization.

## Free Trade Agreements and Korea's Economic Interests

At the end of 1990s Korea started to appreciate the necessity of FTAs for continued development. Initially, this realization was a reaction to the spread of integration initiatives in the world, but in later years it grew into a strong belief that FTAs were necessary in order to transform the Korean economy for the future [Sohn, Yoon, 2001, p. 15]. In the second half of the 1990s the national leadership expressed deep concerns that its major trade partners – the U.S. and European countries – were preoccupied with their own regional integration projects. It was feared that regional integration would create obstacles for Korea's export-dependent economy and distance it from its main export markets and sources of investments [Ibid., p. 14]. Asian neighbours, too, provided enough reasons for similar worries. Japan and China showed interest in the Association of Southeast Asian Nations (ASEAN) and embarked on strategies for regional integration, whereas Korea remained passive. Korean political circles were slow to accept preferential agreements because they meant a departure from multilateralism which, while still rather new, was more understandable to them. Moreover, they did not want additional liberalization beyond the scope of Korea's WTO commitments. As a result of such sentiments, in 2003, among the WTO members only Korea and Mongolia did not have a single FTA [Liou, 2008].

However, lack of progress on the DDA gave Korea a strong incentive to launch an FTA strategy. After the failure of the ministerial meeting in Seattle in 1999 it became obvious that the

country needed alternatives to multilateralism to expand its trade and sustain economic growth [Park, Moon, 2006]. President Roh Moo-hyun referred to FTAs as an existential choice for his country, whose welfare depended on openness to trade [Liou, 2008, p. 186]. Providing further arguments in favour of an active FTA policy, the Korean government paid attention to such benefits as better, deeper and more effective economic cooperation with individual partners and, more importantly, new opportunities to compete with Japanese and Chinese manufacturers in third countries due to the fact that FTAs would improve the price positioning of Korean products through lower tariffs.

The choice in favour of FTAs has not been easy for Korea and involved political debates inside the country. Some representatives of political elites were against further liberalization because they saw it as a threat to agriculture, in the first place, and other weaker industries [Ibid., p. 184]. The FTA with Chile, the first FTA for Korea initiated in 1999, became a victim of these debates as its ratification was delayed by three years because the Korean parliament could not come to consensus on the necessity of the FTA strategy. A breakthrough came only when Korean companies started to lose market share in Chile to Japanese and Chinese competitors. In the end, the Korea-Chile FTA was ratified in 2004 and gave a start to Korea's active, sometimes even aggressive, strategy in matters of regional integration.

Korea's FTA strategy was based on three pillars corresponding to its national goals. The first and most important one was to secure agreements with the U.S., the EU and China, as these markets could provide demand for Korean products, grow trade in services and improve access to technologies [Sohn, Yoon, 2001, p. 10]. The next priority was to initiate FTAs with Asian partners – to deepen cooperation with ASEAN and create conditions for a trilateral FTA between Korea, Japan and China.<sup>4</sup> Finally, Korea planned to make extra-regional agreements in order to expand market horizons beyond traditional spheres of interest and to increase the globalization of the Korean economy. The FTA with Chile fell under the last pillar as it opened a window for Korea into Latin American markets where it was under-represented at the beginning of 2000s.

Realization of this strategy and particularly its third part implied that smaller countries with more or less complimentary interests would initially be chosen as FTA partners in order to avoid difficulties during negotiations [Koo, 2008; 2010]. After Chile, Singapore and the European Free Trade Association (EFTA) became Korea's next partners. They were economies with small agricultural sectors located in different geographical areas close to big markets. The first three agreements gave Korea enough confidence to move closer to its main goal and open negotiations with the U.S., the EU and China at the end of 2000s. Many negotiations took place simultaneously as the Korean government wanted to maximize outcomes in the shortest amount of time. By the end of 2018, in 16 years Korea had managed to sign and ratify 16 FTAs (with Chile, Singapore, EFTA, ASEAN, India, the EU, Peru, the U.S., Turkey, Australia, New Zealand, Columbia, Canada, China, Vietnam and Central America); an additional three FTAs are signed and awaiting for ratification, and seven more are under negotiation (including an FTA with Russia). There are another three feasibility studies under way [Korea FTA, n. d.].

As mentioned above, in the first years of its FTA strategy Korea used the WTO agenda to negotiate FTAs. This resulted in many similarities among its first FTAs with a range of issues discussed under the WTO framework. Agreements with Chile, Singapore, EFTA and Vietnam primarily regulate national treatment and market access, rules of origin, customs procedures, safeguard measures, antidumping and dispute settlement; they hardly touch

<sup>4</sup> Despite multiple rounds of negotiations, the agreement between Korea, Japan and China has not been signed due to numerous disagreements on agricultural and non-agricultural market access, IP protection, and some ongoing historical disputes.

trade in services and do not venture into other issues [Koo, 2008]. For example, the Korea-Chile and Korea-Singapore FTAs practically copy Uruguay round questions as they revolve around barriers to trade and protection of sensitive sectors. In later agreements, though, Korea became more ambitious and included a wider range of issues, such as the environment and development, which do not directly relate to trade. Later agreements include measures to reduce barriers to trade in services, stricter application of intellectual property (IP) protection (starting from the KORUS FTA), protection of geographical names (KOREU FTA), migration (KORCHINA FTA), and environmental protection (FTAs with the U.S., the EU and China) [Korea FTA, n. d.].

However, despite numerous similarities with the WTO in approach to trade regulation, FTAs had their own value added. In case of the early agreements this came in the form of better terms of market access for Korean export-oriented companies because they could enjoy lower import tariff rates. In addition, the Korean government was able to exclude from the agreements sectors that needed protection due to national security concerns or simply because they were too weak to compete.

The extent to which Korea was able to intensify export growth through its early FTAs can be determined through a comparative analysis of export flows to the three markets – Chile, Singapore and EFTA – before and after FTA with each partner was ratified, using the methodology outlined in the manual of the Asia Development Bank [Plummer et al., 2010]. This methodology is based on calculating a weighted average of exports growth rates before the FTA came into force and then extrapolating these results onto the period after the FTA came into force. After extrapolation, the calculated and real value of exports were compared. A four-year period was used for analysis. Since the Korea-Chile FTA took effect in 2004, the analysis focused on the periods 2000–03 and 2004–07; FTAs with Singapore and EFTA came into force in 2006, so the periods analyzed were 2002–05 and 2006–09. Results of the analysis are summarized in Table 2.

*Table 2.* Calculated and Real Growth Rates of Korean Exports to Chile, Singapore and EFTA After the Ratification of FTAs

	Calculated Four Years After the FTA	Actual	Difference Between Actual and Calculated, %
Chile	587315.3	3115103	4.303971
Singapore	11800845	13616994	0.1539
EFTA	1456242	1956196	0.343318

*Source:* Authors' calculations.

If an FTA with Chile had not been signed, Korea's exports to this country would have been 430% lower than its actual value in 2007; thus, the effect of lower tariff barriers as a result of the FTA was considerable. In the cases of Korea-Singapore and Korea – EFTA FTAs, the magnitude of difference was smaller but still in the same direction as the real values of export in the fourth year after the FTAs came into effect were higher than the calculated values. More importantly, a positive effect was observed despite decreases in Korean exports to these markets in 2007 (exports to EFTA decreased by 35%) and 2009 (exports to Singapore decreased by 16% and to EFTA by 22%).

Overall, the FTA strategy had a positive effect on Korean exports to FTA-partner countries. According to estimates by the Korean Customs Office, the maximum effect was achieved

between three and four years after ratification of an FTA [Customs, 2019]. The rate of FTA utilization by Korean businesses is high too, and as of 2018 it achieved 70%. The FTA with Canada has the highest utilization rate (over 80%) and the same is true for the U.S., the EU and Chile, while the lowest utilization rate is of the FTA with China. Korean consumers also see the benefits of their country's FTA strategy. In 2019 in a survey of Korean consumers regarding their assessment of FTA policy, 67.5% of respondents had a positive opinion, which is 21% higher than in 2015 [Customs Office of Korea, n. d.]. Consumers observed the largest effect in the diversification of product choices and in decreased prices of imported goods and services [Korea Consumer Agency, n. d.].

In the case of later agreements, value added could be considered through the internationalization of Korea's service sector, more trade in products subject to IPR protection, and transformation of the Korean economy. However, it should be noted that although FTAs provided stimuli for expansion of trade in services, this issue was treated unequally in different FTAs. The most robust provisions for trade in services were set in the KORUS FTA while other deals have a more modest framework. In most cases agreements discuss transborder trade in services, but some FTAs only mention the issue without getting into much detail. The Park Geun-hye government considered the inclusion of trade in services within the KORChina FTA to be a diplomatic success because until then China had not discussed the issue in other FTAs. Let us consider major tendencies in service trade between Korea and the U.S., the EU and China to see whether and how patterns of trade in services changed.

The KOREU and KORUS FTAs, ratified in 2011 and 2012 respectively, had a positive effect on Korea's trade in services with these partners. The effect was also felt in the technological sphere, which is captured by statistics in proceeds for the use of intellectual property rights. By 2016 trade in services with the EU had grown by 15%, and with the U.S. by 6% compared to pre-FTA levels in 2010 (Fig. 5). In the case of the KORChina FTA, trade in services showed high growth rates in 2011–14 before the FTA was signed. Trade in services expanded due to active exports from Korea and much less from Korea's imports from China. But bilateral trade suffered from tensions between the two countries following deployment of the Terminal High Altitude Defense (THAAD) on the territory of Korea by the U.S., an action that was protested by China [Reuters, 2017]. Despite this temporary difficulty, the Chinese service market represents a high potential for Korea's export of services; moreover, it is a market where the balance of trade in services is to Korea's advantage. China presents opportunities for Korea to balance deficits in trade with other countries. Currently, the two countries are in the process of negotiating an additional agreement on trade in services.

Despite the negative balance in services trade with the EU and the U.S., its size remained stable after the FTAs were ratified. This means that Korea grasped opportunities to export services in parallel with growing imports of services from its partners. One of the most dynamic areas opened for Korea by FTAs is in commercial services.

In case of the KOREU FTA, a marked increase in proceeds from the transfer of intellectual property rights was also observed. Over the period 2011–16, Korean exports in this category grew from \$500 million to \$1.2 billion while imports from the EU reached \$2.7 billion in 2016. In the same year Korea transferred \$5.6 billion to the U.S. in the form of payments for intellectual property rights use (in 2011 Korea imported \$4.6 billion worth of services) while Korea's own exports to the U.S. were worth \$700 billion (\$1.6 billion in 2011) which is much lower than to the EU. The rapid increase of Korea's imports in the category under discussion was due to increasing transfer of technologies. Thus, after the signing of FTAs access to technologies for Korea had widened.

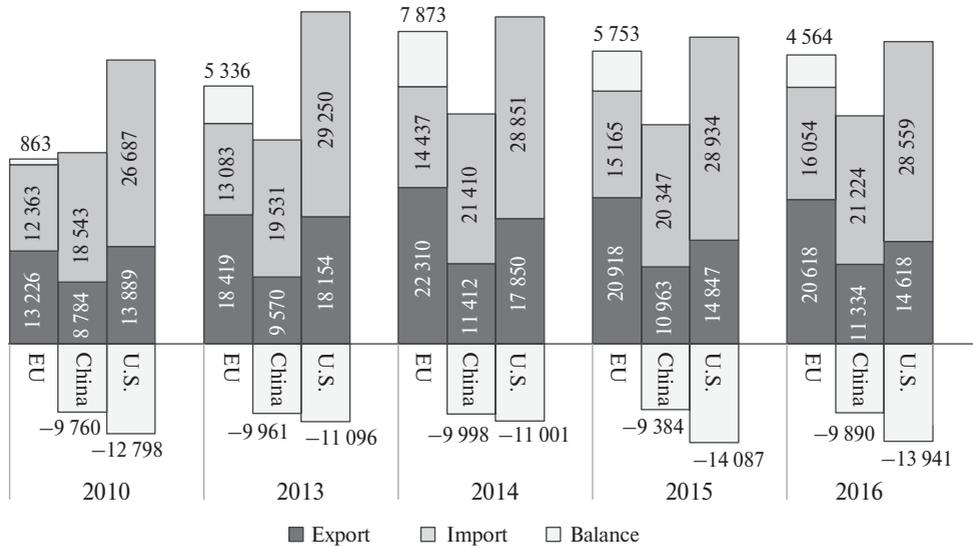


Fig. 5. Korea's Trade in Services With China, the EU and the U.S., in 2010–16, \$ millions

Source: Compiled by the Authors Using UNCTAD [n. d.] Statistics.

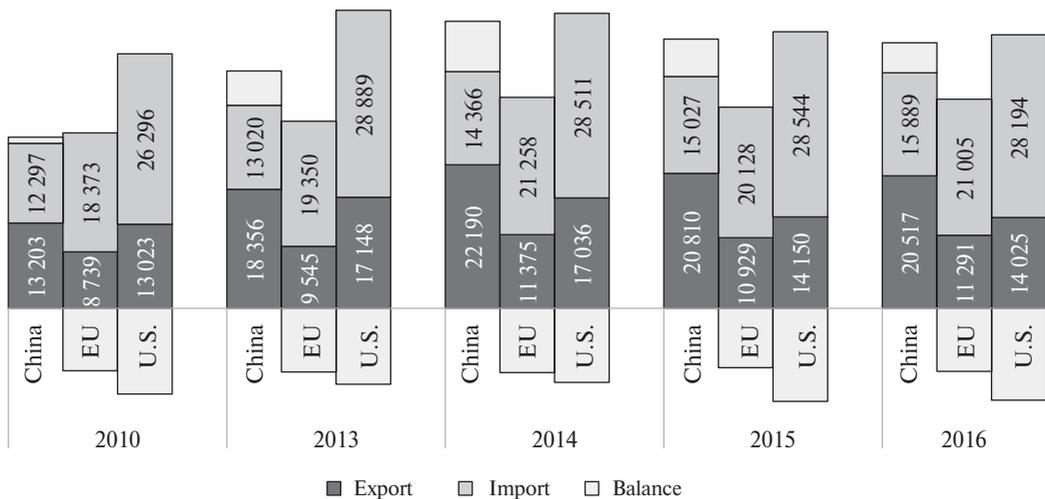


Fig. 6. Trade in Commercial Services Between Korea and China, the EU, and the U.S., 2011–16, \$ millions

Source: Compiled by the Authors Using UNCTAD [n. d.] Data.

Effects from the FTA policy were felt beyond the growth of trade. The overall level of openness of the Korean economy and the quality of the domestic business environment has improved markedly. The Korean government succeeded in reducing the amount of trade and business-related regulation through continuous revision and streamlining. As a result, Korea has moved up in international business ratings. For example, in 2005–06 the country occupied

27th position in the Doing Business rating published by the World Bank, but in 2020 it was in 5th place, ahead the U.S. and the UK [World Bank, 2020]. Korea has shown remarkable progress in decreasing the time and bureaucracy associated with launching a business. It is now among the leading countries in ease of trade procedures, observance of contractual obligations, convenience of the tax system, and protection of minority shareholders rights.

FTAs have produced some unforeseen effects as well. The process of negotiating FTAs has paved the way for different parties inside the country to work together to reconcile their interests in order to achieve benefits for the nation. The interests of manufacturers and agricultural producers had to be balanced through various mechanisms. One of the mechanisms the Korean government used involved special support measures to compensate losses associated with FTAs. Such measures were first introduced with regard to FTAs with the EU, the U.S., China, Vietnam, and New Zealand, and included export support through easier access to financing, additional investments to R&D to help to increase competitiveness of exports, and infrastructure funds for agriculture, among other things. Other mechanisms that proved to be quite effective were consultation services that explained how FTAs work and how businesses can take advantage of them. Relevant ministries ran special programmes for small- and medium-sized enterprises on a regular basis and created an online system to check the spectrum of tariff rates for each FTA. This mechanism proved to be so effective that a similar system was later done for the WTO so that companies can check WTO-related regulations. At the request of businesses, the Korean government created a committee to deal with the negative effects of FTAs. Any company can file a complaint and a committee has to investigate and reply to their request.

At the regional level the FTA strategy gave Korea more authority in trade negotiations. One of Korea's advantages that helped to maximize its number of FTAs was that Korea neither offered a competing integration programme nor exercised pressure to achieve a desired outcome or tried to suggest a normative base to unify regulation. Rather, it approached its partners in search of mutual economic benefits. At the start of its FTA strategy Korea did not suggest negotiating agendas and relied instead on existing WTO formulas. As it accumulated experience it began to take bolder actions and to include new issues on the agenda with support from its partners. Because it had experience, it could refer to already existing FTAs to provide a rational argument. Each new FTA served as a stepping block for the next one. In the end, the FTA strategy helped Korea to take its regional role more seriously and to show initiative on various regional matters.

Under the current situation one more positive aspect of the FTA strategy can be identified. As uncertainty remains about the future of the WTO appellate body that deals with disputes, FTAs allow Korea to regulate cooperation with its partners and manage disputes. FTAs serve as a safety valve that Korea can use in case of emergency in multilateral procedures.

## Conclusion

Korea's experience supports the idea that trade policy can be a powerful tool to achieve national goals including raising welfare. Its influence stretches beyond trade in goods to services and technology. In the case of Korea, trade policy also helped to balance the sometimes polarized interests of national producers and facilitate transformation of the economy. Korea started to use trade policy actively in the mid-1990s, and since then the country improved its global standing both in terms of GDP and business environment. Much of the success can be attributed to the role of the Korean government, which was able to find an optimal balance between the possibilities provided by a multilateral trading system and preferential trade agreements. Even when Korea has shifted toward FTAs, it continued to derive benefits from WTO membership including, those associated with China's accession.

Several aspects were key in enhancing the effectiveness of trade policy for the purpose of advancing national interests. In the first place, the Korean government determined its goals in each dimension (multilateral and preferential) of its trade policy. In case of the WTO, questions of protection for weak sectors of the economy and promotion of Korea's exports globally were prioritized. FTAs, in their turn, served to create additional advantages for entering new markets and promoting exports of other sectors – things that were hard to achieve through WTO membership.

Second, Korea's case shows that an FTA strategy can produce swift results because the country used a gradual multitrack model of negotiation moving from weaker to stronger partners and opening several negotiations simultaneously.

Third, gains from trade policy were distributed between economic agents at different levels, which enhanced the impact of the trade policy. The government initiated various training programmes for business that explained how to use FTAs or the WTO in their activities. As a result, rates of FTA use are relatively high.

Fourth, the agenda for FTA negotiations was broadened gradually. Korea created momentum as it coordinated different agreements and adjusted its regulations. The broadening of the issues was also beneficial because, as a result, Korea was able to suggest a clear economic programme and avoid sensitive political issues with its economic partners.

## References

The Policy Briefing. (2019) *Import and Export Trade in FTA 2018*. Available at: <http://www.korea.kr/news/pressReleaseView.do?newsId=156315815#pressRelease> (accessed 18 July 2019) (in Korean).

Amiti M., Dai M., Feenstra R., Romalis J. (2017) *How Did China's WTO Entry Affect U.S. Prices?* NBER Working Paper No 23487. National Bureau of Economic Research. Available at: <https://www.nber.org/papers/w23487> (accessed 28 June 2019).

Amsden A. (1992) *Asia's Next Giant*. New York: Oxford University Press.

Baldwin R. (1989) The Political Economy of Trade Policy. *The Journal of Economic Perspectives*, vol. 3, no 4, pp. 119–35. Available at: <https://www.jstor.org/stable/1942913> (accessed 28 June 2019).

Customs Office of Korea. (n. d.) Available at: <http://www.customs.go.kr> (accessed 28 May 2020). (in Korean)

Busch M.L., Mansfield E.D. (2011) The Political Economy of Trade Policy. *The International Studies Compendium Project* (R.A. Denmark, R. Marlin-Bennett (eds)). Oxford: Wiley-Blackwell.

Corden W.M. (1997) *Trade Policy and Economic Welfare*. London, New York: Oxford University Press. Available at: <http://doi.org/10.1093/0198775342.001.0001>.

Eaton J., Grossman G.M. (1986) Optimal Trade and Industrial Policy Under Oligopoly. *The Quarterly Journal of Economics*, vol. 101, no 2, pp. 383–406. Available at: <https://doi.org/10.2307/1891121>.

Gills B. (1996) Economic Liberalisation and Reform in South Korea in the 1990s: A 'Coming of Age' or a Case of 'Graduation Blues'? *Third World Quarterly*, vol. 17, no 4, pp. 667–88. Available at: <https://www.jstor.org/stable/3993279> (accessed 28 June 2019).

Handley K., Limão N. (2017) Policy Uncertainty, Trade and Welfare: Theory and Evidence for China and the United States. *American Economic Review*, vol. 107, no 9, pp. 2731–83. Available at: <http://doi.org/10.1257/aer.20141419>.

Hyun J. (2003). Free Trade Agreements and Korea's Trade Policy. *Journal of International and Area Studies*, vol. 10, no 2, pp. 21–37. Available at: <https://www.jstor.org/stable/43107077>.

Japan External Trade Organization (IDE – JETRO) – World Trade Organization (WTO). (2011) Trade Patterns and Global Value Chains in East Asia: From Trade in Goods to Trade in Tasks. Available at: [https://www.wto.org/english/res\\_e/publications\\_e/stat\\_tradepat\\_globalvalchains\\_e.htm](https://www.wto.org/english/res_e/publications_e/stat_tradepat_globalvalchains_e.htm) (accessed 28 May 2020).

Kim Chulsu (2004) South Korean Trade Policy and FTAs. *Japan Spotlight*, May/June, pp. 10–2. Available at: [https://www.jef.or.jp/journal/pdf/cover%20story%202\\_0405.pdf](https://www.jef.or.jp/journal/pdf/cover%20story%202_0405.pdf) (accessed 28 May 2020).

- Koo M.G. (2008) *South Korea's FTAs: Moving From an Emulative to a Competitive Strategy*. Presented at the International Symposium "Competitive Regionalism," Ibuka International Conference Hall, Waseda University, Tokyo, 30–31 May.
- Koo M.G. (2010) Embracing Free Trade Agreements, Korean Style: From Developmental Mercantilism to Developmental Liberalism. *The Korean Journal of Policy Studies*, vol. 25, no 3, pp. 101–23. Available at: <http://citeseerx.ist.psu.edu/viewdoc/download?doi=10.1.1.1017.5062&rep=rep1&type=pdf> (accessed 28 May 2020).
- Korgun I.A., Popova L.V. (2011) *Vneshneekonomicheskij faktor v razvitiiji Respubliki Koreja (1950–2011)* [*Foreign Economic Factors in the Development of the Republic of Korea (1950–2011)*] (S. Sutyurin (ed.)). St. Petersburg: St. Petersburg State University Publishing House. (in Russian)
- Korea Consumer Agency. (n. d.) *Consumers Survey*. Available at: [http://english.kca.go.kr/brd/m\\_11/view.do?seq=467](http://english.kca.go.kr/brd/m_11/view.do?seq=467) (accessed 24 November 2019).
- Korea FTA. (n. d.) Available at: [www.fta.go.kr](http://www.fta.go.kr) (accessed 13 July 2019).
- Korean International Trade Association (KITA). (n. d.) Available at: <https://www.kita.net/> (accessed 28 May 2020).
- Krugman P.R., Obstfeld M. (2009) *International Economics: Theory and Policy*. Boston: Pearson Addison-Wesley.
- Lee Y., Lee K.T. (2015) Economic Nationalism and Globalization in South Korea: A Critical Insight. *Asian Perspective*, vol. 39, no 1, pp. 125–51. Available at: <http://doi.org/10.1353/apr.2015.0012>.
- Liou T.H. (2008) South Korea's FTA Strategy Under Roh Moo-hyun. *Taiwanese Journal of WTO Studies*, vol. 8, pp. 177–212. Available at: <https://doi.org/10.1177/0015732515080103> (accessed 28 May 2020)
- Marchand U.B. (2017) *How Does International Trade Affect Household Welfare?* IZA World of Labor. Available at: <https://wol.iza.org/articles/how-does-international-trade-affect-household-welfare> (accessed 1 July 2019).
- Meade J.E. (1955) *Trade and Welfare*. London, New York: Oxford University Press.
- Park Y.B., Moon S.-B. (2006) *Korea's FTA Policy Structure*. Available at: <https://faculty.washington.edu/karyiu/confer/seoul06/papers/park-moon.pdf> (accessed 28 May 2020).
- Plummer M., Cheong D., Hamanakh Sh. (2010) *Methodology for Impact Assessment of Free Trade Agreements*. Manila: Asian Development Bank. Available at: [https://aric.adb.org/pdf/FTA\\_Impact\\_Assessment.pdf](https://aric.adb.org/pdf/FTA_Impact_Assessment.pdf).
- Republic of Korea. (1996) *Trade Policy Review of the Republic of Korea*. WT/TPR/S/19. World Trade Organization.
- Republic of Korea. (2004) *Trade Policy Review of the Republic of Korea*. WT/TPR/S/137. World Trade Organization.
- Reuters. (2017) *China Lodges Stern Protest With South Korea Over THAAD Deployment*. 7 September. Available at: <https://www.reuters.com/article/us-northkorea-missiles-china-southkorea/china-lodges-stern-protest-with-south-korea-over-thaad-deployment-idUSKCN1BI0TL> (accessed 1 November 2019).
- Sohn C.H., Yoon J. (2001) *Korea's FTA Policy: Current Status and Future Prospects*. KIEP Discussion Paper No 01–01, Korea Institute for International Economic Policy.
- The Export-Import Bank of Korea. (n. d.) *Statistics on Korean OFDI*. Available at: <https://www.koreaexim.go.kr/site/main/index001> (accessed 15 July 2019).
- United Nations Committee on Trade and Development (UNCTAD). (n. d.) *Statistics*. Available at: <https://unctad.org/en/Pages/statistics.aspx> (accessed 15 July 2019).
- World Bank. (1993) *The East Asian Miracle: Economic Growth and Public Policy: Main Report*. Available at: <http://documents.worldbank.org/curated/en/975081468244550798/Main-report>.
- World Bank. (n. d.) Available at: <https://datacatalog.worldbank.org/> (accessed 2 November 2019).
- World Bank. (2020) *Doing Business 2020: Comparing Business Regulation in 190 Countries*. Available at: <https://openknowledge.worldbank.org/handle/10986/32436> (accessed 20 November 2019).
- World Trade Organization (WTO) – International Trade Centre (ITC) – United Nations Committee on Trade and Development (UNCTAD). (2019) *World Tariff Profiles 2019*. Available at: [https://www.wto.org/english/res\\_e/booksp\\_e/tariff\\_profiles19\\_e.pdf](https://www.wto.org/english/res_e/booksp_e/tariff_profiles19_e.pdf).