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The impact of free trade agreements (FTAs) on business in the Republic of Korea

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The Impact of Free Trade Agreements (FTAs) on Business in the Republic of Korea

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Abstract

The Republic of Korea (hereafter Korea) continues to promote an open-trade system via the conclusion of free trade agreements (FTAs), arguing that Korean enterprises will obtain considerable business opportunities under the FTAs the government has implemented. However, the FTAs that are currently being implemented in Korea are said to be beneficial only to some enterprises. This study presents new evidence from a survey conducted from July–August 2008 on 120 Korean firms. The paper explores critical questions regarding the utilization of FTAs, their perceived costs and benefits, perceptions of multiple rules of origin (ROOs), and policy and institutional support mechanisms for FTAs.

One of the key findings is that most of the currently implemented FTAs in Korea were concluded with small- and medium-sized developing countries. Moreover, within these FTAs, the range of preferential tariffs is not very broad in scope; as such, only one out of five enterprises was found to be utilizing them. However, since the conclusion of FTAs with the United States and the European Union, Korean businesses have become very interested in utilizing those respective FTAs. The government should make efforts for early implementation of these FTAs. In the FTAs concluded by Korea, ROOs are strict and complicated. In future FTAs, a more neutral and lenient form of ROOs should be adopted.

JEL Classification: F15, F13

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1. INTRODUCTION

Despite its limited natural resources and small domestic consumer market, the Republic of Korea (hereafter Korea) has grown into one of the largest economies in the world, having taken advantage of globalization and global trade liberalization under the General Agreement on Tariffs and Trade (GATT) system.[1] Even in the face of the current international financial crisis, Korea continues to promote an open-trade system and has pushed forward with the restructuring and domestic reform that trade liberalization entails. It is also an active participant in various bilateral free trade agreements (FTAs) and Doha Development Agenda (DDA) multilateral trade negotiations.

Over the past several years, Korea's perception of the advantages of an open economy has greatly improved. With its elevated global economic position, Korea has recognized that the principle of mutual reciprocity has to be applied to trade liberalization. When Korea was a developing country, it opened up its market only to a minimum, expecting the concession of foreign countries. Today, however, it is well aware of the fact that such action will not gain international support.

Lee Myung-bak's government, which was inaugurated in February of 2008, decided on the construction of a "global FTA network" as its core foreign-trade policy. The government's position is that it will implement the FTA that Korea has concluded with the United States (US), and that it will conclude Korea's FTA with the European Union (EU), which was already in the final stage. It also plans to consider starting negotiation for bilateral FTAs with Japan, the People's Republic of China (PRC), and Russia, as well as with the Southern Common Market of Central and South America (more commonly known as Mercado Comun del Sur or Mercosur, or Mercosur)[2]. It plans to improve the country's declining trade environment owing to the recent global financial crisis, and to reinforce the country's economic-growth momentum through the conclusion of FTAs.[3]

There are many internal forces that oppose the promotion of FTAs. The contention of protectionists is that opening up the economy and liberalization are harmful and that protectionism supports the national interest. Because of this, the former government of Roh Moo-hyun had political difficulties concerning FTAs with broad coverage of trade liberalization. The first FTA that Korea concluded with Chile allowed several exceptions in many items, and the agreements that the country concluded afterward were also partially less comprehensive and negligible. After accumulating several FTA experiences, however, Korea was able to conclude an advanced, high-standard agreement. Its FTA with the US could be evaluated as the world's most comprehensive FTA in terms of market opening, service, investment, and trade rules (Cheong 2007, 2008, 2009).

While the Korea-US FTA has yet to be implemented due to its delayed ratification by both countries, Korean enterprises expect that they will obtain considerable business opportunities when it is implemented. The FTAs that are currently being implemented in Korea are said to be beneficial only to some enterprises. The government has been widely collecting the interests and opinions of the Koreans, but it has had limitations in reflecting those into its FTAs. It has been pushing the conclusion of FTAs, but has been less successful in providing information concerning how to utilize the existing FTAs, which is needed by enterprises.

[1] Korea was recorded as the14th largest economy in the world in 2006, 11th in 2007, and 14th in 2008.

[2] Mercosur is the common market shared by Argentina, Brazil, Paraguay, Uruguay, and Venezuela.

[3] Refer to Baldwin and Rieder (2007); Holmes (2005); Raff (2004); and World Trade Organization, Committee on Regional Trade Agreements (2002) for a general discussion on the economic effects of FTAs.

This study summarizes key findings from previous surveys[4] and presents new evidence from a survey conducted from July–August 2008 on 120 Korean firms, exploring critical questions regarding the utilization of FTAs, their perceived costs and benefits, perceptions of multiple rules of origin (ROOs), and policy and institutional support mechanisms for FTAs.[5]

Based on the 120 firm samples, only 25 firms use FTAs currently, while 65 use or plan to use FTAs.[6] There are several reasons why only a small share of firms utilizes FTAs. The most important impediment to using FTAs is likely to be the low tariff preference of Korean FTAs (43 firms), followed by the lack of information on FTAs (41 firms). Others are: complicated rules of origin (ROO) (18 firms), administrative costs (13 firms), and non-tariff barriers (5 firms). Although the Korean government's active promotion of FTAs has been largely positively evaluated, this paper asserts that the government's FTA promotion system should be improved through its supplementation. Moreover, the government should push forward schemes for enhancing the enterprises' utilization of the existing FTAs. This paper also examines the ways by which the Korean government pushes FTAs forward and analyzes the actual conditions of the FTAs as utilized by enterprises. Finally, it presents schemes for enhancing the degree of the enterprises' utilization of the existing FTAs.

2. BACKGROUND: KOREA'S FTA POLICIES

2.1 Korea's System for Promoting FTAs[7]

This section provides general information on the main elements contained in the FTAs of Korea. While Korea has not had any specific model agreement for its FTA, the general framework of the agreement texts Korea pursued in its negotiations with Chile, Singapore, and the US were modeled after the text of the North American FTA (NAFTA), although the specific structure and provisions of each agreement varied, reflecting various negotiating needs. The draft text of an agreement with European Free Trade Association (EFTA) at the start of negotiation was based on the EFTA-Singapore agreement. The FTA between the Association of Southeast Nations (ASEAN) and Korea has a similar structure with the ASEAN Free Trade Area (AFTA) and ASEAN-PRC FTA.

As its experience in FTA negotiations accumulates, Korea is gradually building a database of agreement texts, which will help formulate its own agreement pattern. For example, the text of the Korea-US (KORUS) FTA became a model text for its FTA with the EU.

In terms of substantive aspects of FTAs, however, Korea has maintained a high degree of consistency. First of all, it has pursued comprehensive FTAs, covering all sectors and substantially all trade, in line with Article XXIV of GATT 1994 and Article V of the General Agreement on Trade in Services (GATS). Secondly, Korea has improved the quality of FTAs over time in terms of liberalization in trade in goods and services.

[4] The previous studies include: (i) Cheong (2006), an early survey analyzing the ranking of FTAs by firms based on the preference of countries with which Korea has concluded an FTA; (ii) Korea Small Business Institute (2007), a survey of 500 small- and medium-sized Korean firms; and (iii) Korea Trade Investment Promotion Agency (KOTRA) (2008), whose survey was conducted in April 2008 for 505 export-import companies.

[5] Comprehensive analysis on preferential ROO and related issues can be found in Falvey and Reed (2002), Gretton and Gali (2005), and Grossman and Helpman (2005).

[6] FTA utilization findings were also presented at a seminar by the Korea Association of International Trade and Industries (Cho and Cheong 2008).

[7] This section is based on the documents "Main elements in Korea's FTAs" and "Korea's Legislative Framework for FTA Negotiations" by Korea's Ministry of Trade (2005).

2.2 Korea's legislative framework for FTA negotiations[8]

Under the Korean Constitution, treaty-making power lies in the authority of the President. When the President, as the head of the government, concludes and ratifies a treaty,[9] the text of the treaty is published on the official gazette. The treaty then becomes incorporated into the Korean domestic legal system with the same effectiveness as domestic laws.

Under the Government Organization Act, the Minister of Foreign Affairs and Trade is responsible for trade negotiations and conclusion of trade-related agreements with foreign countries.[10] Therefore, the Office of the Minister for Trade within the Ministry of Foreign Affairs and Trade leads and coordinates Korea's negotiations on FTAs, in which various relevant ministries and agencies participate.

Unlike in the US, the Korean National Assembly, the legislative body of the Government, does not have authority for trade negotiations and, therefore, is not directly involved in FTA negotiations. However, the treaties, which fall into the category of Article 60[11] of the Constitution, should win the consent of the National Assembly before their ratification by the President. An FTA falls under such category. It should be noted that a request for the National Assembly's consent to the ratification of a treaty is placed after that treaty is signed. Therefore, the Government (administration body) normally seeks to involve the National Assembly during the process of its FTA negotiations by providing relevant information to its members to facilitate the consent procedure at a later stage.

Detailed procedures, which must be followed by the government officials participating in FTA negotiations, are set up in the form of the "Presidential Directive on Procedures for the Conclusion of Free Trade Agreements (Directive)."[12] The Directive governs the entire process of negotiations, including the pre- and post-negotiation stages, of an FTA the Korean Government undertakes.

Under the Directive, the Ministers' Meeting for External Economic Affairs (MMEEA) has the authority to make decisions on major policy issues with regard to negotiations on FTAs Korea pursues with its partner countries. Such issues include the selection of countries with which Korea will negotiate FTAs; the timing and the method of such negotiations; the mandates that will be given to the negotiating team; and other important directions for the negotiations. The Deputy Prime Minister for Economy and Finance chairs the MMEEA with the participation of relevant economic ministers.

The Directive has established three committees: the FTA Committee, the working-level subcommittee, and the FTA Advisory Committee. These three committees all together draw up roadmaps for FTAs, make decisions on Korea's important negotiating position for each FTA negotiation, and undertake follow-up measures after the conclusion of an FTA.

The FTA Committee, which is chaired by the Minister for Trade and consists of Deputy Ministers of relevant ministries, is primarily responsible for making Korea's FTA policy,

[8] See Ministry of Trade (2004) for an overview of Korea's FTA promotion policies.

[9] Article 73 of the Constitution

[10] Article 30(1) of the Government Organization Act stipulates that "[t]he Minister of Foreign Affairs and Trade shall exercise general supervision over diplomacy, trade negotiations with foreign countries, and general management and coordination of trade negotiations, treaties and other international agreements, protection of and support for Korean nationals abroad, and research on international situations and immigration."

[11] Article 60 of the Constitution stipulates that "[t]he National Assembly shall have the right to consent to the conclusion and ratification of treaties pertaining to mutual assistance or mutual security; treaties concerning important international organizations; treaties of friendship, trade and navigation; treaties pertaining to any restriction in sovereignty; peace treaties; treaties which will burden the State or people with an important financial obligation; or treaties related to legislative matters."

[12] The Directive has been established to facilitate consultations and coordination among relevant ministries and to increase the understanding and participation of the general public in the FTA process. The Directive entered into effect on June 8, 2004. Unofficial translation of the Directive can be found in Ministry of Trade (2004).

overseeing FTA negotiations, and undertaking any follow-up measures. The subcommittees under the committee provide information on the promotion of FTAs by the government for private sectors. The FTA Committee works with semiofficial organizations such as the Korea Trade Investment Promotion Agency (KOTRA) and the Korea International Trade Association (KITA), in collecting companies' opinions on FTAs and disseminating information on FTAs. Many ministries have close networks with industrial organizations regarding FTA issues, and these channels are utilized for FTA promotion. One good example of an FTA promotion is the "FTA EXPO" held at the COEX Center exhibition hall in December 2007, which was designed to provide FTA utilization schemes and comprehensive FTA information to the public.

The FTA Advisory Committee, which is chaired by the Minister for Trade, and consists of experts from academia and businesses, gives advice to the Government in the pursuit of FTAs.[13] As per pre-negotiations procedures, Korea's FTA partner and basic strategy for its execution is drafted by the FTA Committee and endorsed by the MMEEA.[14] The FTA Committee recommends to the MMEEA candidate countries for FTA partners on the basis of economic feasibility studies undertaken by domestic research institutes. It is the Korean Government's usual practice to carry out a joint study with a candidate FTA partner to examine the feasibility of an FTA[15] before it starts negotiations. However, a joint study is not mandatory under the Directive. Korea launched negotiations with Chile after two preliminary consultations. During the period of the joint study, such issues as the economic effect of the FTA, the scope and coverage of the FTA, and negotiating modalities are normally discussed.

When a joint study or any other form of preliminary consultation ends with the conclusion that the proposed FTA is expected to bring benefits, the FTA Committee recommends to the MMEEA the launching of FTA negotiations. A public hearing must be held prior to the MMEEA's decision and the result of the public hearing should be presented to the MMEEA at its deliberation. The MMEEA has a final say whether or not to launch the negotiations. This procedural requirement ensures that various interested parties and sectors will have a chance to be fully heard by the Government before the Government makes any formal decision on the launching of negotiations.

2.3 Coverage of Trade by Korean FTAs

Korea participated belatedly in the bandwagon of FTA regionalism when it first enforced the Korea-Chile FTA in April 2004. Since then, it has been implementing trade liberalization under FTAs with many countries by "pushing forward synchronized multiple FTAs" under the policy goal of securing export markets and economic advancement.[16] As of October 2008, Korea put four FTAs into effect: with Chile (April 2004), Singapore (March 2006), EFTA (September 2006), and ASEAN 9 (June 2007).[17] Korea has officially signed its FTA with the US June 2007, and the FTA with India August 2009. FTA negotiations with EU, Canada, Mexico, and Peru are currently underway, and the joint research on FTAs with the PRC and Mercosur has been completed. Table 1 summarizes the status and progress of Korean FTAs.

[13] Article 9 of the Directive

[14] Article 13 of the Directive

[15] Before the launch of FTA negotiations with Japan, the Joint Study Group met seven times during the period of 2002–2003. After two meetings of the Joint Study Group in 2004, Korea launched FTA negotiations with EFTA in January 2005.

[16] See Choi (2008) for more information on Korea's progress in FTA negotiations.

[17] In February 2009, Thailand acceded to the ASEAN-Korea FTA.

Table 1: Status of Korean FTAs

Item	Country, Region, Economic Bloc	Progress	Remarks
Concluded	Asia Pacific Trade Agreement	- Implemented (1976)	
	Chile	- Implemented (April 2004)	
	Singapore	- Implemented (March 2006)	
	EFTA	- Implemented (September 2006)	
	ASEAN	- Implemented (June 2007)	- FTA with Thailand is under ratification
	US	- Officially signed (June 2007)	- Korea is under ratification process
	India	- Officially signed (August 2009)	
	EU	- Virtually concluded (August 2009)	
Under Negotiation	Mexico	- Under negotiation	
	Canada	- Under negotiation	
	ASEAN	- Gradual Progress	- Currently negotiating on investment issues - Services agreement signed in November 2007
	GCC	- Under negotiation	
	New Zealand	- Under negotiation	
	Australia	- Under negotiation	
	Peru	- Under negotiation	
	Canada	- Under negotiation	- Possibly resume negotiation in near future
	Japan	- Under negotiation	- Possibly resume negotiation in near future
Official Discussion	Mercosur	- Agreed to start official talk	- Joint report in May 2006
	PRC		- Possibly start negotiation in near future
	Russia		- Joint study in 2008
Long-term FTAs	PRC-Japan-Korea		- Joint study under progress since 2002
	EAFTA		- Joint study since 2005

Sources: Korea Ministry of Foreign Affairs and the ADB Asia Regional Integration Center FTA database (data as of April 2009)

The Korean government promotes FTAs in accordance with the FTA Promotion Roadmap that was established in September 2003. This roadmap classified the Korean government's promotion of FTAs into the short-term promotion with Japan, Singapore, and the ASEAN and the mid- and long-term promotion (3–5 years) with big economies like the EU, the PRC, and the US. Korea's FTAs with most of the countries included in the FTA Roadmap have been promoted as originally scheduled. In 2008, the promotion of the Korea-Japan FTA was discussed, and official FTA negotiations for a FTA with the PRC will begin soon.

As the FTA promotion environment at home and abroad had been changing, the FTA Promotion Roadmap was supplemented in May 2004. In the meeting of the foreign ministers comprising the 2nd Korea-India Joint Economic Committee held in New Delhi in December 2003, both countries agreed to set up a Joint Study Group to establish a comprehensive cooperative relationship in the trade, investment, and service sectors of both countries, after which both countries are expected to have the same position on the conclusion of an FTA. Moreover, as the promotion of an FTA with EFTA has been agreed upon, FTAs with India and EFTA have been added to the existing roadmap.

Lee Myung-bak's government, which was inaugurated in February 2008, has been promoting the construction of a "global FTA network" after the drafting of the FTA promotion policies of the Participatory Government. The promotion of FTAs with Japan, PRC, Russia, and the Gulf Cooperation Council (GCC), which were not emphasized or considered in the existing FTA Roadmap, is now under consideration. The government is hoping that Korea's FTA with the US will be ratified, and it is focusing its efforts on the conclusion of Korea's negotiations with the EU, which are nearing their end.

The Korean government was able to implement or promote many FTAs within a short period of 4–5 years, and synchronized multilateral FTA policies proved effective along with the Roh Moo-hyun government's policy intentions. The background of the Roh government's promotion of synchronized multilateral FTAs is as follows: First, to catch up with the global trend of spreading FTAs within a short time, the synchronized multilateral promotion of FTAs with many countries is needed. Second, the experience in the Korea-Chile FTA negotiation process can be cited as the background. When the negotiations with Chile came to a deadlock due to the Korean government's FTA promotion strategy of "one-at-a-time" approach in which the government could not explore any other FTA alternative plan until the negotiations with Chile ended. The trade policy staff in charge who experienced problems during the negotiations with Chile in 2001–2002 proposed the promotion of the synchronized multilateral FTA. Third, the promotion of synchronized multilateral FTAs was needed to minimize the burden on the country's weak industries. Lee (2008) notes that the policy of synchronized multilateral FTAs were promoted in consideration of the fact that the burden of opening up the market is concentrated too much on a specific industry when an FTA is promoted lopsidedly with either an advanced country or with a developing country (a country that exports industrial or agricultural products).

The countries with which the Korean government promoted synchronized multilateral FTAs were mostly those to which Korea exports. As was pointed out by Lee, minimizing damages and expanding exports served as the major factors for the promotion of synchronized multilateral FTAs. The top ten countries and regions to which Korea exported in 2007, in descending order, were: (1) PRC, (2) EU, (3) US, (4) ASEAN, (5) Japan, (6) Hong Kong, China, (7) Taipei,China, (8) Mexico, (9) Russia, and (10) India. Of these, the EU, US, and ASEAN, which rank 2nd, 3rd, and 4th, respectively, in terms of the volume of Korea's exports thereto, have put into effect, have concluded, or are in the process of negotiations for an FTA with Korea. Besides, FTA negotiations with Mexico and India, excluding the special cases of Hong Kong, China and Taipei-China, are underway, which means that Korea has either concluded or is in the midst of FTA negotiations with its major trading partners, except Japan and the PRC, its biggest trading partners. Korea's exports to the countries with which it has concluded FTAs up to October 2008 accounted for 25.78% of its total exports in 2007 (Table 2), and if the countries with which FTA negotiations are currently

underway will be included, this percentage will increase to 41.8%. If the FTAs that are currently being discussed will be included, approximately 88% of Korea's foreign trade will be attained in the FTA system (Lee 2008).

Table 2: Korea's Trade Share by FTAs

Item	FTAs	Trade Share (%)			
		Export	Import	Export + Import	Total
Concluded	Chile	0.48	1.23	0.85	0.85
	EFTA	0.53	0.71	0.62	1.47
	Singapore	2.92	1.90	2.42	3.89
	ASEAN	9.85	9.61	9.74	13.63
	US	13.31	10.92	12.15	25.78
Under Negotiation	EU	14.91	9.72	12.39	41.80
	India	1.70	1.18	1.45	
	Canada	1.11	1.00	1.06	
	Mexico	1.93	0.26	1.12	
Under Discussion	PRC	21.34	15.69	18.59	87.88
	Japan	8.15	16.78	12.36	
	Australia	1.44	3.66	2.52	
	New Zealand	0.21	0.31	0.26	
	Russia	1.59	1.48	1.54	
	Mercosur	1.08	1.07	1.07	
	GCC	2.39	17.48	9.74	

Source: UN COMTRADE (2006) cited in Lee (2008)

To expect high economic benefits from the conclusion of an FTA with a particular country, the FTA should be comprehensive and the range of the market opening should be wide. Particularly, the ratio of the immediate abolition of tariffs should be high, and the rules of origin in the neutral and less stringent forms should be adopted in the agreements. Although Korea has promoted FTAs with many countries, the FTAs that had been concluded before the Korea-US FTA was concluded are seen as having allowed limited market opening. In particular, the FTAs that Korea has concluded with developing countries are considered insufficient.

In Korea's FTA with Chile, Korea's major export items, such as home appliances (including washers and refrigerators), were not included among the items whose tariffs were abolished, and the FTA with the ASEAN designated over 200 items as ultrasensitive items so they would not be affected by the FTA. As a result, the ASEAN was able to maintain the existing tariffs on Korea's major export items.[18] In Korea's FTA with Singapore, the ratio of tariff abolition is almost 100% as shown in Table 3, but as Singapore is virtually a region with free trade, the FTA had no significant effect on Korea's export companies. Fortunately, it has been agreed that the tariffs on most trade items will be abolished immediately when the agreement arrived at in the most recently concluded Korea-US FTA is implemented. Moreover, Korean enterprises are highly interested in the implementation of the Korea-US FTA because of the large domestic market of the US.

[18] Due to political sensitivity to the opening of agriculture, Korea excluded many items from its exports to Chile, but after the implementation of the agreement, its exports to Chile increased an annual average of 61% for four years. According to the research results of Kim (2008) who conducted proven analysis on Korea-Chile trade using an econometric model, the increase in trade between the two countries are mostly attributable to the implementation of FTA.

Table 3: Tariff Eliminations in Korea's FTAs
(unit: %)

FTA	Country	All Sectors	Manufacturing	Agriculture
Korea-Chile	Korea	Tariff Elimination: 6.4%, Immediate Elimination: 87.2	Tariff Elimination: 100, Immediate Elimination: 99.9	Tariff Elimination: 71.2, Immediate Elimination: 15.6
	Chile	Tariff Elimination: 99.0, Immediate Elimination: 41.8	Tariff Elimination: 99.8, Immediate Elimination: 30.6	Tariff Elimination: 94.2, Immediate Elimination: 92.9
Korea-Singapore	Korea	Tariff Elimination: 91.6, Immediate Elimination: 59.7	Tariff Elimination: 97.4, Immediate Elimination: 68.8	Tariff Elimination: 66.6 Immediate Elimination: 16.0
	Singapore	Immediate Tariff Elimination (100%)		
Korea-US	Korea	Tariff Elimination: 99.7 Immediate Elimination: 80.4	Total: 100 Immediate Elimination: 91.6	Tariff Elimination: 98 Immediate Elimination: 38.1
	US	Tariff Elimination: 100 Immediate Elimination: 82.1	Total: 100 Immediate Elimination: 87.7	Tariff Elimination: 100 Immediate Elimination: 58.7

Source: Authors' calculations based on Korean FTAs

With regard to this, some criticize that the Korean government has promoted FTAs in such a way as to make the number of FTAs and not their contents the central object. Choi (2007) points out that the conclusion of an FTA should not be its own object since an FTA is only a means to strengthen competitiveness and enhance efficiency, and since Korea's basic FTA policies focus on external expansion, the effects of trade liberalization are less than what are expected. In Korea FTA has been used as one of policy tools for achieving an advanced economy. Currently, the Korean economy is confronted with a sluggish growth potential internally and with intensified globalization externally. Under these circumstances, lasting growth can no longer be guaranteed by the existing economic-growth paradigm of increasing inputs. Without strengthening the innovative competencies of enterprises, entering the circle of developed countries is impossible. In the agreements that had been concluded before the conclusion of the Korea-US FTA, the contents that induce industrial competitiveness are insufficient. As such, they are not expected to have any effect on the advancement of the economy other than boosting the country's exports. The Korea-US FTA is evaluated as having included many policy means that reinforce competitiveness, such as deregulations and the advancement of the economic system.

3. FINDINGS FROM EXISTING LARGE SCALE SURVEYS

Whether the countries with which the Korean government has concluded an FTA are those that the Korean enterprises prefer can have a great impact on the utilization of the existing FTAs and on their economic effects. As such, the FTA countries surveyed in 2006 that the Korean enterprises prefer were compared in this study with the countries with which Korea has concluded FTAs so far. Table 4 summarizes the results of Cheong (2006).

FTAs bring about the effect of economic growth by expediting the accumulation of material, human, and knowledge capital. When the tariff and non-tariff barriers are removed, the

resources are shifted from the industries with a weak competitive power to those with a strong competitive power, thereby increasing the efficiency in resources allocation from the viewpoint of the country as a whole. It is difficult, however, to evaluate the countries with which Korea has concluded an FTA by industry since there are many enterprises even within the same industry that have a different position with regard to FTAs. Despite this difficulty, it will be ideal to select the countries with which to conclude an FTA while considering the FTA partner countries preferred by the major industries.

Table 4: FTA Preferences by Industry

Industry	First Preference	Second Preference	Third Preference
Auto	EU, US, PRC	Canada, Australia, Mexico	Brazil, India
Machinery	EU, US, PRC, Mexico	Canada, Australia	Brazil, India
Electronics	PRC, Mexico, EU	Mercosur, ASEAN	Japan, India, US
Chemicals	PRC, India	US, EU, Mercosur	Mexico, Australia, Canada
Steel	ASEAN, PRC, India	Mercosur, Canada, Australia	US, EU
Textiles	US, Canada	PRC, India	Japan, EU, Mexico, Australia

Source: Cheong (2006)

In 2006, with the support of the Federation of Korean Industries, the authors conducted a survey among Korean enterprises regarding their preferred country to conclude FTAs with. The results were presented in the 2006 seminar "The Promotion of FTAs and the Gain and Loss by Industry," held at the Federation of Korean Industries in Seoul. The analysis covered the automobile, steel, electricity and electronics, petrochemicals, and textile industries.

The results of the aforementioned analysis showed that the Korean industries prefer FTAs to be concluded with big economic blocs like the PRC, US, and EU. This shows that while the Korean government has been promoting FTAs with small-scale economies like Chile, Singapore, and EFTA, Korean enterprises consider the promotion of FTAs with the big economic powers as more urgent than the promotion of FTAs with small regions. The Korean business circles considered the conclusion of an FTA with PRC the most urgent in 2006. In particular, the electricity and electronics and petrochemicals industries ranked PRC first among the Korean enterprises' preferred FTA partner countries, while the steel industry ranked it second, after the ASEAN. The automobile and general-machinery industries, on the other hand, regard an FTA with PRC as less attractive than FTAs with the EU and the US. The Korean textile industry, whose price competitiveness is weaker than that of PRC, considers the promotion of an FTA with the US most urgently needed.

The results of the aforementioned survey show that the countries with which Korea had concluded an FTA before the Korea-US FTA was concluded are remotely preferred as FTA partner countries by Korean enterprises. The Korean government began FTA negotiations with the U.S in the early part of 2006 and began official FTA negotiations with the EU in mid-2007. This shows that the Korean government's FTA policies coincide with the wishes of Korean enterprises.

The Korean enterprises' positions toward the countries with which the Korean government is promoting or considering an FTA are examined herein as follows. As of October 2008, the Korean government is negotiating FTAs with Canada, India, Mexico, EU, and GCC. Most of the contents of the FTA with India were concluded in the September negotiations, but it is known that some controversial points should be resolved before it is officially signed. The Korean enterprises want the government to actively promote FTAs, but they differ among

themselves in terms of their preferred FTA partner countries, according to the survey results by KOTRA (2008).[19]

As for the reasons (based on the most preferred country) for the conclusion of FTAs with the countries with which Korean enterprises want FTA negotiations to be resumed or initiated, the respondents cited reasons that are directly related to them, such as "high frequency and big volume of trade" and "it (the FTA partner country) is a major export-import country." They also cited reasons related to future marketability and profitability, such as "expected improvement of its (the FTA partner country's) export performance" and "the scale and potentials of the country's economy and market" (see Table 5). Concerning the enterprises' hope that FTA negotiations with Japan be resumed, the reasons that most of the enterprises cited were that "it is advantageous for importing raw materials/materials/parts" and "because Japan is a major trading country." Regarding the enterprises' hope that Korea-PRC FTA negotiations be started, the reasons that most of the enterprises cited were that "PRC is a major trading country" and that "both the trade volume and frequency of the country are big." As for concluding FTAs with Russia and India, these countries' "economic growth potential and high marketability" were considered a big factor, as seen in Table 6.

Table 5: Reasons Cited for Early Conclusion of FTAs

Reason	No. of Firms
Large trade/trade frequency	127
Reduction of costs on imported materials and parts	43
Large market/high potential for economic growth	122
Elimination of high tariffs	36

Source: KOTRA (2008)

Table 6: Reasons Cited for Early Start of Negotiations

Reasons	No. of Firms
Large trade/trade frequency	131
Reduction of costs on imported materials and parts	35
Large market/high potential for economic growth	79
Elimination of high tariffs	22

Source: KOTRA (2008)

The Korea Institute for International Trade Report (2008) proposed that FTAs be promoted first with resource-rich countries and requested the government to carefully consider whether to conclude FTAs with PRC and Japan because such FTAs will have a great impact on Korea's domestic industries. The report examined the order of priorities in promoting FTAs with 11 economic blocs with which FTA negotiations are underway or are being considered, not including the economic blocs with which FTA negotiations have already been concluded or are imminent (India and the EU). In examining the order of priorities, the five points that were considered were: (i) market scale and growth potential; (ii) tariff level; (iii) the possibility of damaging the country's industries; (iv) the current amount of resources and energy; and (v) the counterpart country's current environment concerning the promotion of FTAs. When

[19] Refer to Appendix regarding the major findings in KOTRA (2008). KOTRA, the country's largest trade promotion organization, and International Trade Business Institute under Korea International Trade Association (KITA) published the list of countries that the Korean enterprises prefer to have FTAs with in 2008.

the above-mentioned five items were taken into account, Russia was given the first priority, followed by GCC, Australia, India, PRC, Mercosur, and Mexico (see Table 7).

Table 7: Ranking of FTA Priorities with Trading Partners

Country/ Region	Market Size and Growth Potential	Tariff Level	Damage to Domestic Industry	Endowment of Resources and Energy	Attitude Toward FTA	Overall Evaluation
Japan	7	10	7	11	9	**11**
PRC	1	5	11	2	8	**5**
Canada	8	8	10	4	6	**9**
India	5	1	6	6	6	**4**
Mexico	9	2	8	8	1	**6**
GCC	4	7	1	7	4	**2**
Russia	3	4	2	3	9	**1**
Mercosur	2	3	9	5	9	**6**
Australia	6	8	5	1	3	**2**
New Zealand	11	11	3	9	4	**10**
South Africa	10	6	4	9	2	**8**

Source: International Trade Business Institute (2008)

Based on these results, we can propose the following tasks of Korea in relation to the promotion of FTAs: (i) the early implementation of the Korea-US FTA, (ii) the early conclusion of the Korea-EU FTA, and (iii) the early settlement of the FTAs with GCC, India, and Mexico, which are expected to put a relatively small burden on the Korean economy. The Korea Institute recommends that FTAs also be concluded with Russia, Australia (and New Zealand), and Mercosur and advised the government to carefully consider entering into FTA negotiations with PRC and Japan as this is expected to produce an adverse impact on the country's industries.

To sum up, Korean enterprises are hoping that a broader market opening will result from the FTAs that the government is promoting, and they prefer the promotion of FTAs with countries that have big economic scales. Particularly, they expect many business opportunities to be generated by the Korea-US FTA, which is currently awaiting ratification by the National Assembly, and they expect that both the governments of Korea and the US will implement the FTA between the two countries soon. The FTA policies that the government of Korea is promoting appear to considerably coincide with the wishes of Korean enterprises. It can be said that the government is promoting FTAs with the regions preferred by Korean enterprises. The promotion of FTAs with Japan and the PRC, however, is slower than those with other regions. This appears to have a correlation with the fact that Korean enterprises' preference for FTAs with these countries is relatively lower than their preference for FTAs with the US or EU.

4. NEW EVIDENCE: FINDINGS FROM THE 120 FIRM SURVEY

4.1 Sample Profile

The enterprises surveyed included 120 companies that manufacture automobiles and automotive parts, electrical goods, machinery, petrochemicals, textiles, steel and metal products, and sundries. Seventeen enterprises represented the petrochemical industry; the rest of the industries had 17 representative enterprises. Thirty-three firms have more than 300 employees, 88 have 100–299 employees, while seven have 50–99 employees.[20]

Table 8: Sample Profile

Industry	No. of Firms	No. of Firms Per the Size of Employees		
		50–100	101–300	300+
Auto, parts	17	0	12	5
Electrical goods	17	3	10	4
Machinery	17	0	12	5
Chemicals	18	0	10	8
Textiles	17	0	13	4
Metal, products	17	0	12	5
Sundries	17	4	11	2
Total	120	7	80	33

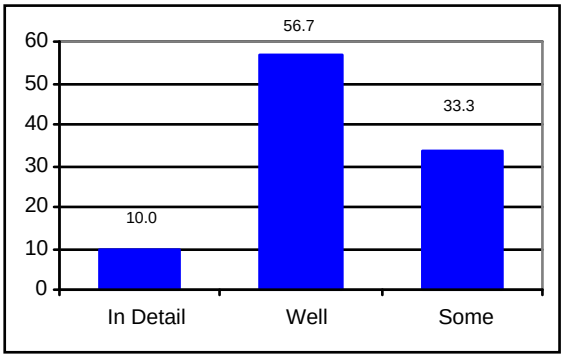
Source: Authors' calculations based on 120 firm samples.

4.2 Awareness and Knowledge of FTAs

The 120 enterprises surveyed were all found to be aware of the contents of the existing FTAs. Eighty were found to be well aware of the contents of the existing FTAs while 40 were found to be only partially aware. Of the 80 firms that were found to be well aware of the contents of the existing FTAs, 12 (10%) indicated that they were well aware of these agreements' detailed contents, and 68 (57%) indicated that they understood most of the parts of these agreements (see Figure 1).

[20] Of the 120 firms, 45 recorded annual exports of more than 100 million dollars, 46 recorded annual exports of 10 million–100 million dollars while the rest recorded annual exports of 1 million–10million dollars. Also, most of these firms are engaging in both exports and domestic sales. The respondents to were mostly deputy general managers in charge of export and import while in some firms, their CEOs directly responded to the survey.

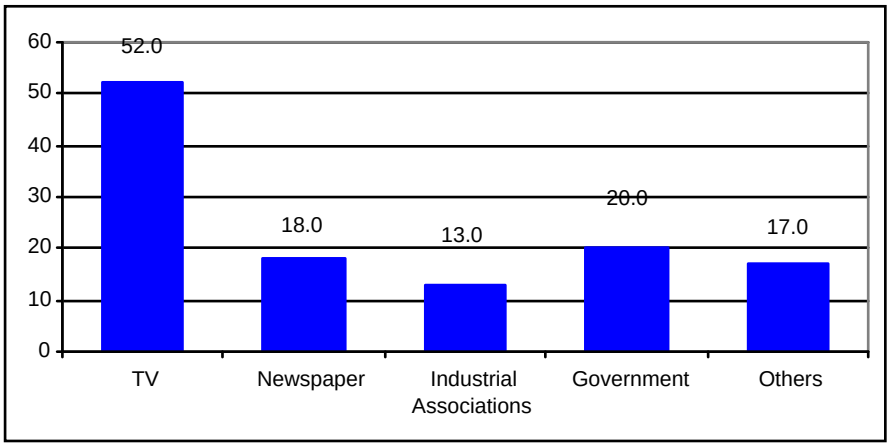
Figure 1: Awareness of FTA Provisions (unit: %)



Source: Authors' calculations based on 120 firm samples.

Over the past several years, Korea's foreign-trade authorities have extensively publicized the promotion of FTAs among the Korean people. In particular, as the agricultural and labor sectors seriously opposed the Korea-US FTA (for which negotiations started in 2006) and those opposed to open market staged big anti-FTA demonstrations, the government increased the FTA promotion budget and posted FTA advertisements in diverse media. The government staged campaigns to disseminate factual information about FTAs to the people, utilizing TV and radio, the Internet (homepages, blogs, portal sites, and press sites), and press media (national- and regional-circulation newspapers). Since Korea has a well-developed Internet and communication network and is densely populated, information dissemination was conducted easily, leaving a general public that is well informed about FTAs. As a result, in the public-opinion poll that was conducted toward the end of 2006, FTAs were supported by 60% of the general public, and the Korean government's negotiating team was able to negotiate with the US with confidence.

Figure 2: Sources of Information on FTAs (unit: %)



Source: Authors' calculations based on 120 firm samples.

The enterprises that had been surveyed were found to have obtained FTA-related information mainly from the TV and by visiting the offices of business associations or government organizations related to international trade policies (Figure 2). Businessmen can gain access to advanced trade information through diverse associations by industry or trade organization, and it is not difficult to grasp not only the contents of the promotion of FTAs but also the detailed contents of the agreements through the Internet, with a little more effort. Businessmen complain to the government, however, of the shortage of detailed information about the utilization of FTAs under implementation, and despite the diverse efforts of the government to obtain FTA-related information, the problem of insufficient FTA information

has not been resolved. There were also fewer people from the business circles who attended the FTA Expo in 2007 than expected. The reason for the mismatch between the government's FTA promotion activities and the enterprises' interest in FTAs is that the government's promotion has focused mainly on the FTA policies. Hardly any information related to business activities was provided in the FTA presentation meeting or seminar held by the government.[21]

Table 9 shows the results of the survey that was conducted on the recognition of FTAs by industry. The enterprises that understand FTAs well are evenly distributed in most industries, with the textile and automobile parts industries having the highest ratio, followed by electricity and electronics, petrochemical, and sundries industries. The degree of FTA recognition by the steel and metal industries was relatively low. Since low or no tariffs are applied to the steel and metal industries in accordance with the sectoral-liberalization policy of Asia-Pacific Economic Cooperation (APEC), the enterprises belonging to these industries were found to be relatively uninterested in FTA policies.

Table 9: Awareness of FTAs by Industry
(unit: number of firms)

Industry	In Detail (1)	Well (2)	Subtotal (1) + (2)	Some (3)	Don't Know (4)	Subtotal (3) + (4)
Auto, parts	3	10	**13**	4	0	**4**
Electrical goods	1	11	**12**	5	0	**5**
Machinery	1	9	**10**	7	0	**7**
Chemicals	2	9	**11**	7	0	**7**
Textiles, clothing	4	10	**14**	3	0	**3**
Metal, products	0	9	**9**	8	0	**8**
Sundries	1	10	**11**	6	0	**6**
Total	12	68	**80**	40	0	**40**

Source: Authors' calculations based on 120 firm samples.

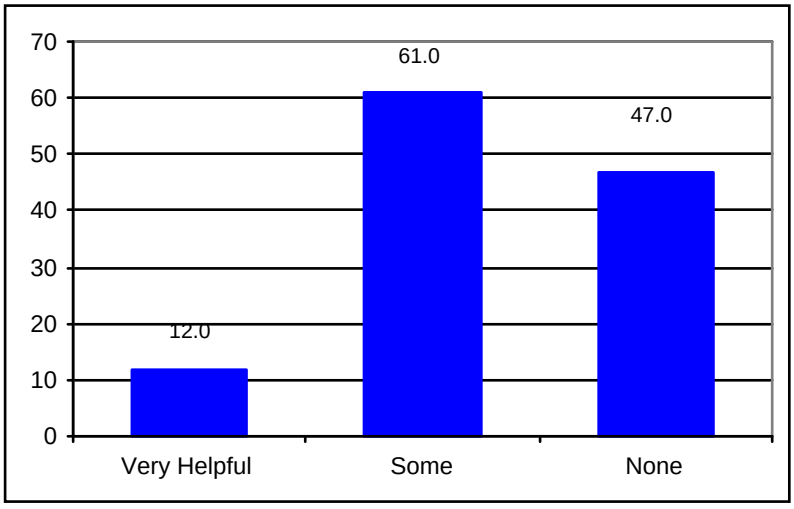
4.3 Cost and Benefits of FTAs

According to Figure 3, about 61% (73 firms) of the respondent companies indicated that the FTAs that the Korean government has concluded so far are helpful to their respective businesses; about 39% (47 firms), on the other hand, indicated that such FTAs are not helpful or have nothing to do with their businesses. Majority of these belong to the steel industry. The firms with positive responses see how much FTAs contribute to the improvement of the business environment in the partner countries, particularly concerning tariff eliminations on item with high tariff rates.[22]

[21] See Hyun (2008) for more information on tasks to improve business environment as part of a seminar held by the Korea Society for International Trade.

[22] Though 61% of firms evaluate FTAs to be positive for their business, currently only 21% of the firms utilize FTAs in their business in applying preferential tariffs.

Figure 3: Benefits and Costs of FTAs
(unit: %)



Source: Authors' calculations based on 120 firm samples.

The finding that most of the companies surveyed were not properly utilizing the FTA preferential tariffs was also substantiated in the results of the KOTRA (2008) survey, which showed that only 19% of all the respondent firms were utilizing the FTA preferential tariffs and that 81% were not utilizing them.

Of the 73 companies that indicated that the government's promotion of FTAs would be helpful to their businesses, 47 employed 101–300 employees each, 21 employed more than 300 employees each, and five employed 50–100 employees each.

Although all industries surveyed in this research indicated that the promotion of FTAs by the government was helpful for their businesses, there are differences in the number of firms across industries. There are more votes from sundries, auto parts, textiles, and electrical goods, while relatively small numbers of votes came from metal, machinery and chemicals, which have lower tariff barriers.

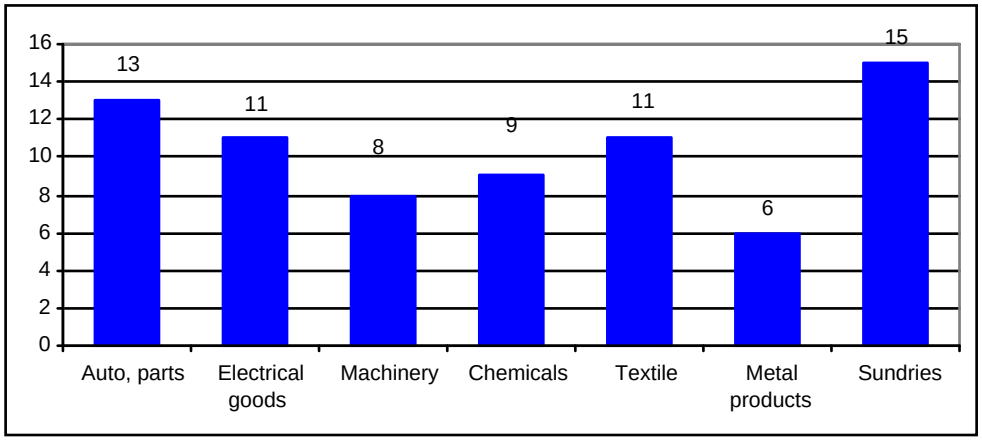
Table 10 shows the numbers of firms with indifferent impact of FTAs on business, which is the other side of Figure 4. Large numbers of firms in the metal, machinery, and chemicals industries showed "less interest" on FTAs.

Table 10: Benefits and Costs of FTAs by Industry
(unit: number of firms)

Industry	No. of Firms	Very Helpful (A)	Some (B)	Subtotal (A+B)	None
Auto, parts	17	3	10	13	4
Electrical goods	17	1	10	11	6
Machinery	17	1	7	8	9
Chemicals	18	2	7	9	9
Textiles	17	2	9	11	6
Metal, products	17	1	5	6	11
Sundries	17	2	13	15	2
Subtotal	120	12	61	73	47

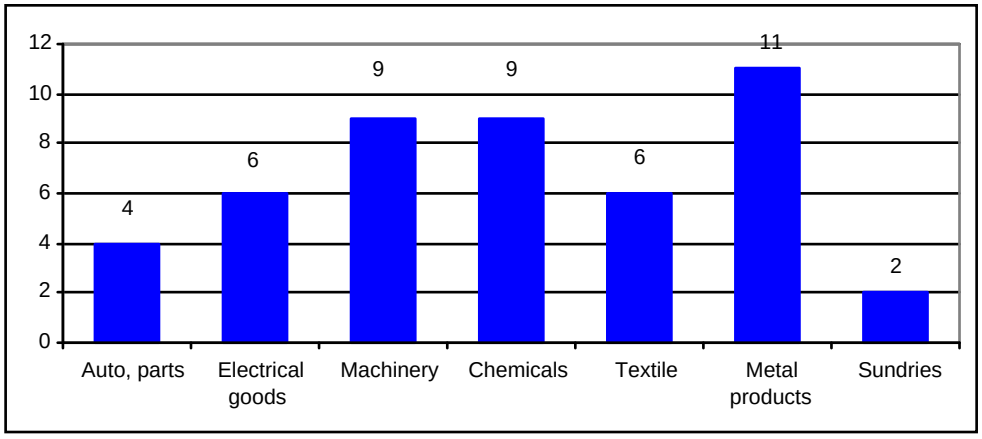
Source: Authors' calculations based on 120 firm samples.

Figure 4: Positive Impact of FTAs on Business by Industry (unit: number of firms)



Source: Authors' calculations based on 120 firm samples.

Figure 5: No Impact of FTAs on Business by Industry (unit: number of firms)

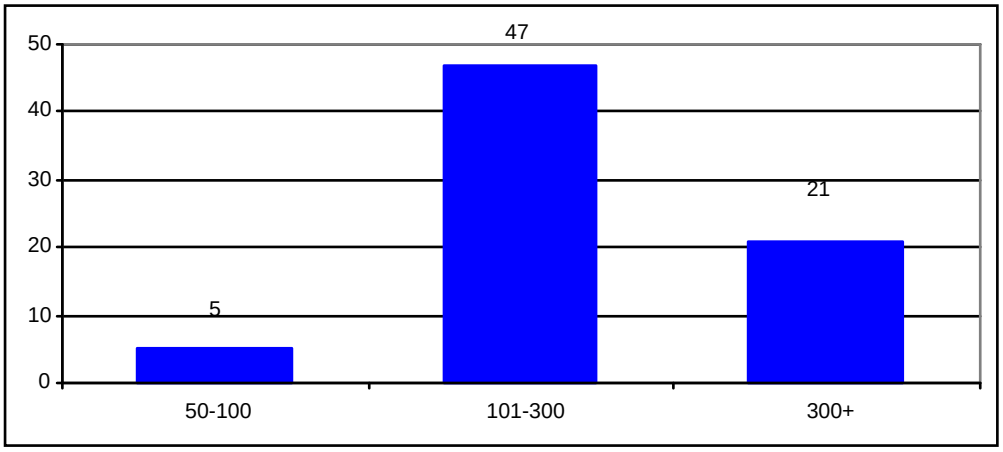


Note: A few firms evaluated economic losses from FTAs.

Source: Authors' calculations based on 120 firm samples.

Considering the size of employees of firms in Figure 6, medium-sized firms (101−300 employs) occupied the largest share, followed by large firms (300+ employees). However, this finding may be misleading, since the survey sample has 80 medium-sized firms out of 120 firms surveyed (see Table 8).

Figure 6: Positive Impact of FTAs on Business by Firm Size (unit: number of firms)



Source: Authors' calculations based on 120 firm samples.

The number of companies that indicated that the government's promotion of FTAs would be helpful to their businesses was not found to have a distinct correlation with the number of their employees. About 60% of all the companies that had been surveyed recognized the usefulness of FTAs. About 71% of the respondent companies whose employment size is small (50–100 employees) indicated that the government's promotion of FTAs would be helpful to their businesses,[23] and about 59% of the respondent companies whose employment size is medium (101–300 employees) indicated the same. On the other hand, about 64% of the respondent companies whose employment size is relatively large (more than 300 employees) recognized the usefulness of the existing FTAs to their respective businesses. This percentage is higher than that of the companies with a medium employment size.

Table 11: Perception of FTAs and Firm Size Distribution

No. of Employees	No. of Firms	No. of Firms with Positive Perception of FTAs (B)	Share (B/A)
50–100	7	5	71.43%
101–300	80	47	58.75%
300 +	33	21	63.64%
Subtotal	**120**	**73**	**60.83%**

Source: Authors' calculations based on 120 firm samples.

The degrees of the respondent companies' recognition of the existing FTAs appear to have an unclear correlation with the respondent companies that indicated that the government's promotion of FTAs would be helpful to their businesses. Table 12 shows that 22 of the 73 companies that indicated that the conclusion of FTAs would be helpful to their businesses claimed that they were partially recognizing the existing FTAs, and 17 of the 47 companies that responded that the conclusion of FTAs would not be helpful to their businesses registered a low recognition of the existing FTAs. Only six of the 12 companies that understand FTAs in detail indicated that FTAs would be helpful to their respective businesses, five companies indicated that FTAs would be partially helpful to their businesses, and the remaining company (manufacturing petrochemical products) indicated that the conclusion of FTAs would not be helpful at all to its business.

[23] The number of enterprises each of which employs 50−100 employees is only seven, so this may raise the question of the reliability of the survey.

Table 12: Awareness of FTAs and Perception of FTAs Distribution

	No. of Firms	Beneficial to Business (A)	Not Helpful (B)	Share (A/B)
Understand FTAs in detail	12	11	1	91.67%
Understand FTAs well	69	40	29	57.97%
Know FTAs a little	39	22	17	56.41%
Subtotal	**120**	**73**	**47**	**60.83%**

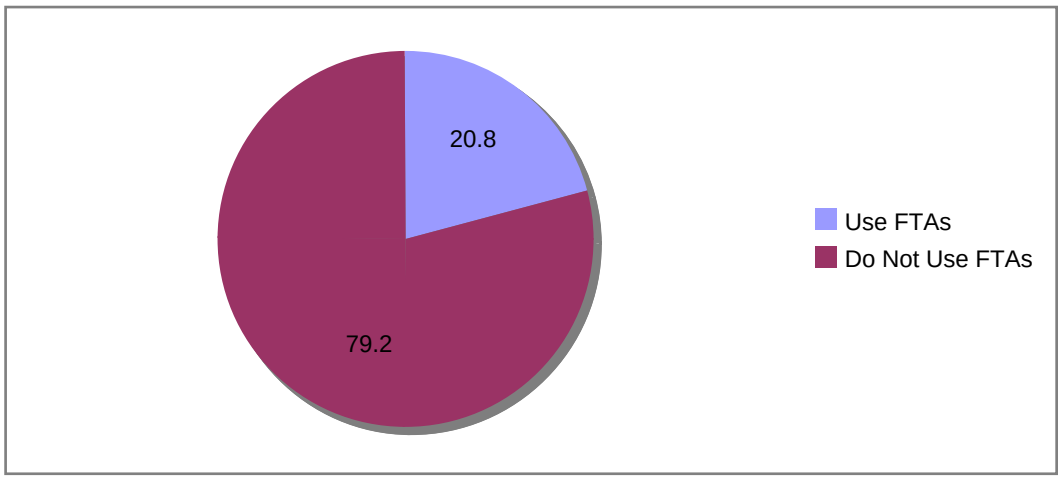
Source: Authors' calculations based on 120 firm samples.

4.4 Utilization of FTAs

The Korean enterprises, on the whole, consist of a small number of big corporations and a large number of small and medium enterprises (SMEs). Most of the 10 largest Korean corporations are classified as multinational corporations, whose exports account for roughly 50% of Korea's total exports. These corporations are not only friendly to the FTA policies but are also actively utilizing the existing FTAs for their respective businesses. It is not difficult for them to utilize the existing FTAs since they have a considerable number of manpower exclusively handling such task. For example, company A, an automobile manufacturer, has been operating exclusive teams to handle FTA rules of origin for two or three years and has built a database for procuring entire parts of its own products and a system of analyzing the production process and rules of origin. It has also constructed computer programs and a manpower system to automatically check whether the rules of origin are met. Most SMEs, however, do not fully recognize FTAs and have not secured manpower to exclusively handle international trade.

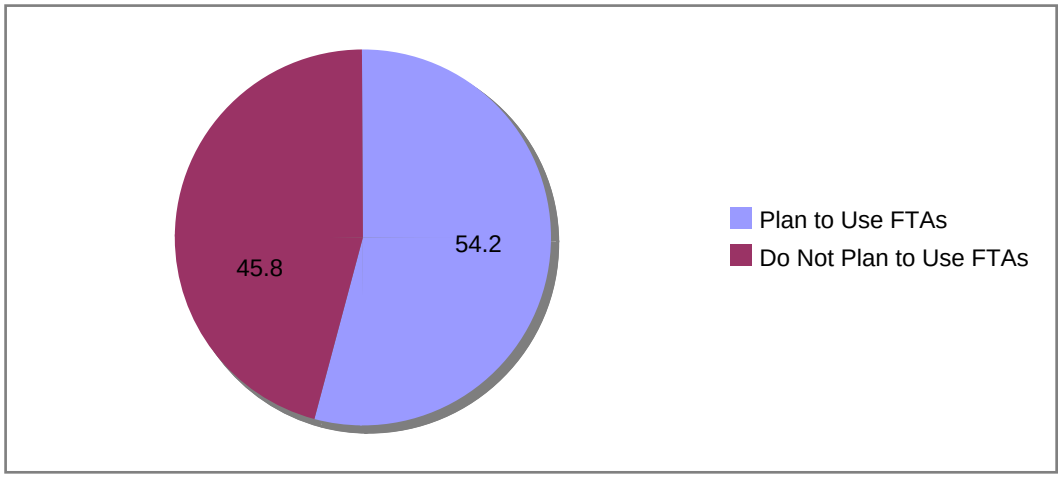
The number of companies that actually utilize the existing FTAs in their respective businesses was found to be far lower than the number of companies that recognize the contents of the existing FTAs. The survey showed that the Korean enterprises are well aware of the existing FTAs that their government is promoting, but only one out of the five companies that had been surveyed is currently utilizing the existing FTAs. When asked, however, whether they plan to utilize the existing FTAs, 54% of the companies responded that they plan to do so.

Figure 7: FTA Utilization
(unit: %)



Source: Authors' calculations based on 120 firm samples.

Figure 8: Plans to Use FTAs
(unit: %)



Source: Authors' calculations based on 120 firm samples.

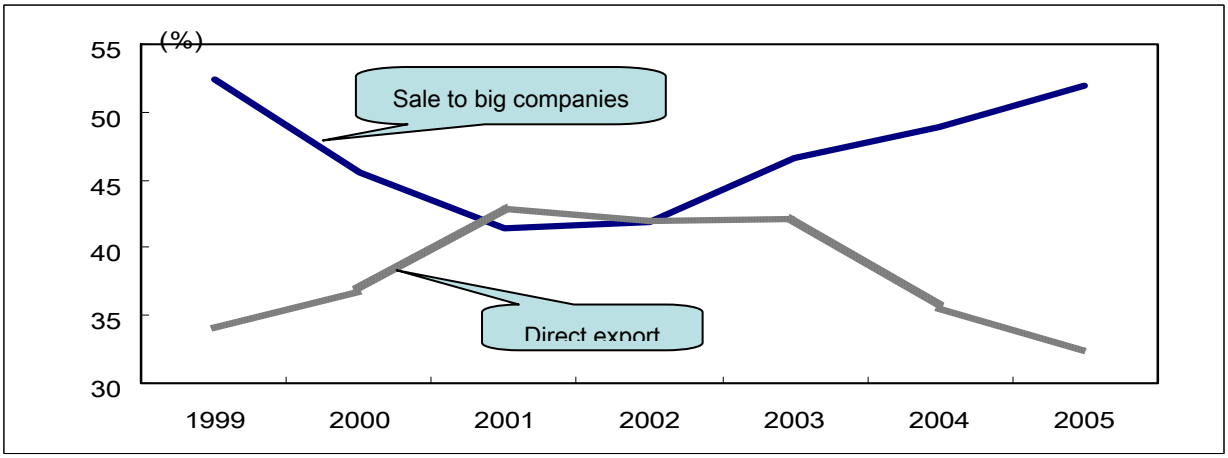
When the 25 companies that responded that they are currently utilizing the existing FTAs were classified by industry, most of the companies were found to belong to the textile and petrochemical industries (five each), followed by the sundries industry (four). Traditionally, these industries have high dependence on exports, and have been oriented for export-oriented growth. The three companies whose degrees of recognition of FTAs are low were found to be currently utilizing the existing FTAs.

The SMEs; FTA utilization degrees cited in this paper can be attributed to their business activities. According to the Korea Small Business Institute (2007), SMEs supply goods to the big corporations within the country rather than export goods directly or sell these in the domestic market. In recent years, the ratio of SMEs' exports to their total sales has been declining, while their supply of goods to the big corporations has been sharply increasing, as seen in Figure 9.[24] The increase in the SMEs' supply of goods to the country's big corporations is due to the increase in the demand of the big corporations (34.8%) and the pursuit of stability in business management (30.4%).

In the case of the SMEs' supply of goods to the domestic enterprises, 97.6% (plural responses) of them are dependent on the supply of goods to the big corporations. This shows that their dependency on the big corporations is absolutely high. Of the goods supplied by them, 14.8% are for export and 85.2% are both for export and for domestic consumption. The SMEs' supply of goods to the big corporations accounts for an average of 50.0% of their total sales.

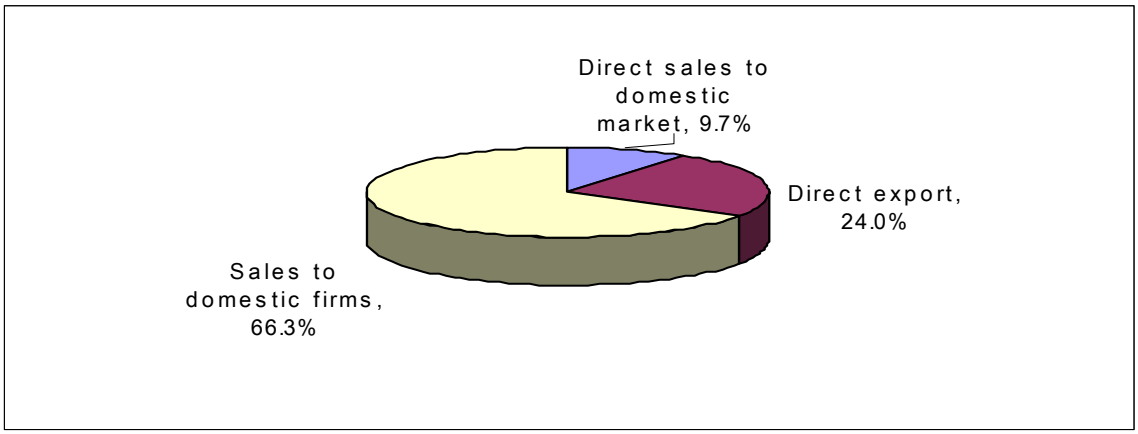
[24] In case of Korea, big corporations are defined as firms with more than 500 workers, though small variations of workers are allowed depending on industry.

Figure 9: Share of SMEs' Direct Export and Sale to Big Companies



Source: Korea Small Business Institute (2007).

Figure 10: Share of the Type of Sale of SMEs



Source: Korea Small Business Institute (2007)

The SMEs' dependence on the big corporations in terms of exports is high, and their ratio of production for domestic consumption to their total production has been increasing every year. SME exports in 2007 amounted to 167 trillion won, of which the SMEs' direct exports amounted to 106 trillion won, representing 63% of their total exports, while their indirect exports amounted to 61 trillion won.

As is shown in Table 13, the SMEs' indirect exports through big corporations are increasing. Their indirect exports in 2007 amounted to 61 trillion won, representing an increase of 22 trillion won compared with 2001, and during the same period, the indirect exports through SMEs decreased by two trillion while the indirect exports through the big corporations increased by 25 trillion.

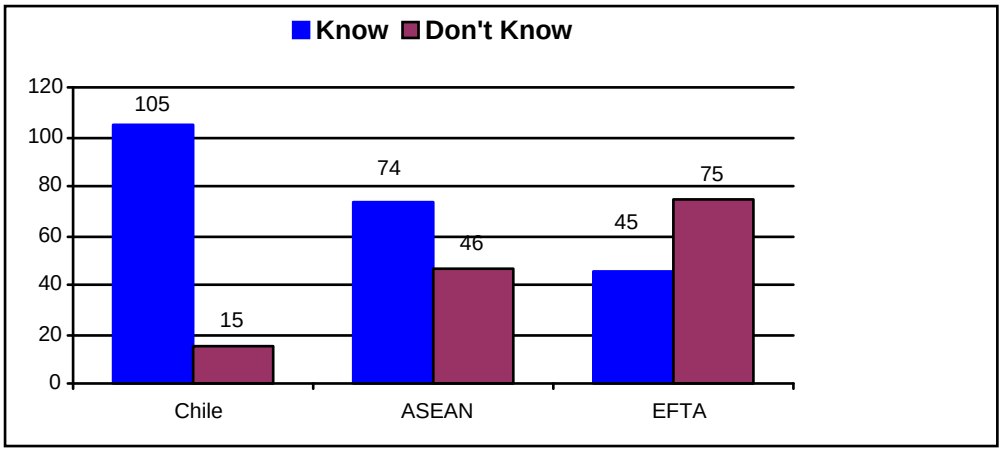
Table 13: Export Potential of Korean SMEs
(unit: trillion Won)

Year	Export Potential	Direct Export	Indirect Export		
			Subtotal	SMEs	Large Companies
2001	122	83	39	20	18
2002	124	85	39	19	20
2003	143	97	46	20	25
2004	155	103	51	19	32
2005	149	94	55	17	38
2006	154	98	56	17	39
2007	167	106	61	18	43

Source: Korea Small Business Institute (2007)

KOTRA (2008) shows that the Korean enterprises highly recognize the Korea-Chile FTA. The enterprises' degree of recognition of the countries in which FTAs have become effective was highest in Chile. Of the countries in which FTAs have become effective, the degree of recognition of FTAs is highest in Chile (87.9%), which concluded an FTA with Korea for the first time, followed by the ASEAN countries (61%), such as Singapore, Malaysia, Indonesia, and Viet Nam, and the EFTA countries (37.4%), such as Switzerland and Norway.

Figure 11: Perception of Implemented FTAs
(unit: number of firms)



Source: Authors' calculations based on 120 firm samples.

Although only about 20% of the Korean enterprises are currently utilizing the existing FTAs, more than half of the enterprises that had been surveyed responded that they plan to utilize such FTAs. Most of the enterprises that produce automobiles, automobile parts, and sundry goods are establishing plans to utilize the existing FTAs. The enterprises in the petrochemical and steel industries, on the other hand, were found to have minimal plans to utilize such FTAs.

Table 14: Utilization of FTAs by Industry

Industry	Yes (A)	No	Subtotal (B)	Share (A/B)
Auto, parts	3	14	17	17.65
Electrical goods	3	14	17	17.65
Machinery	2	15	17	11.76
Chemicals	5	13	18	27.78
Textiles	5	12	17	29.41
Metal, products	3	14	17	17.65
Sundries	4	13	17	23.53
Total	25	95	120	20.83

Source: Authors' calculations based on 120 firm samples.

Therefore, why the enterprises of Korea, which is heavily dependent on exports, have little use for the existing FTAs, and why only about half of the enterprises that were surveyed have future plans to utilize such FTAs, must be determined. First, most of the countries with which Korea has concluded FTAs so far have modest scale of trading with Korea.

Table 15: Firms that Plan to Use FTAs

Industry	Yes (A)	No	Subtotal (B)	Share (A/B)
Auto, parts	15	2	17	88.24
Electrical goods	6	11	17	35.29
Machinery	10	7	17	58.82
Chemicals	2	16	18	11.11
Textiles	13	4	17	76.47
Metal, products	5	12	17	29.41
Sundries	14	3	17	82.35
Total	65	55	120	54.17

Source: Authors' calculations based on 120 firm samples.

The Korea-Chile FTA, which became effective in April 2004, showed an average annual export growth of 61% for four years since the FTA came into effect. The Korean-made products' market share in the import market of Chile showed favorable growth, from 3.0% in 2003 to 3.1% in 2004, 3.6% in 2005, and 4.7% in 2006, representing a more favorable growth in Korean exports compared with the competitor countries. With regard to the export performance of major trade items, the exports of automobiles, wireless phones, and color TVs, whose tariffs were abolished immediately after the FTA came into effect, increased sharply right after the agreement became effective. The exports of steel sheets and gasoline, whose tariff abolition period is 5–13 years, increased sharply due to the lowered tariff in the third year of the agreement's coming into effect.

Table 16: Impact of Chile-Korea FTA on Bilateral Trade (unit: %)

Item	Before FTA	1st Year	2nd Year	3rd Year	4th Year
Month-Year	April 2003–March 2004	April 2004–March 2005	April 2005–March 2006	April 2006–March 2007	April 2007–March 2008
Export Growth	9.6	57.6	46.8	50.0	89.7
Import Growth	63.8	45.0	32.5	60.5	8.3

Source: KOTRA 2008, based on trade data from the Korea International Trade Association.

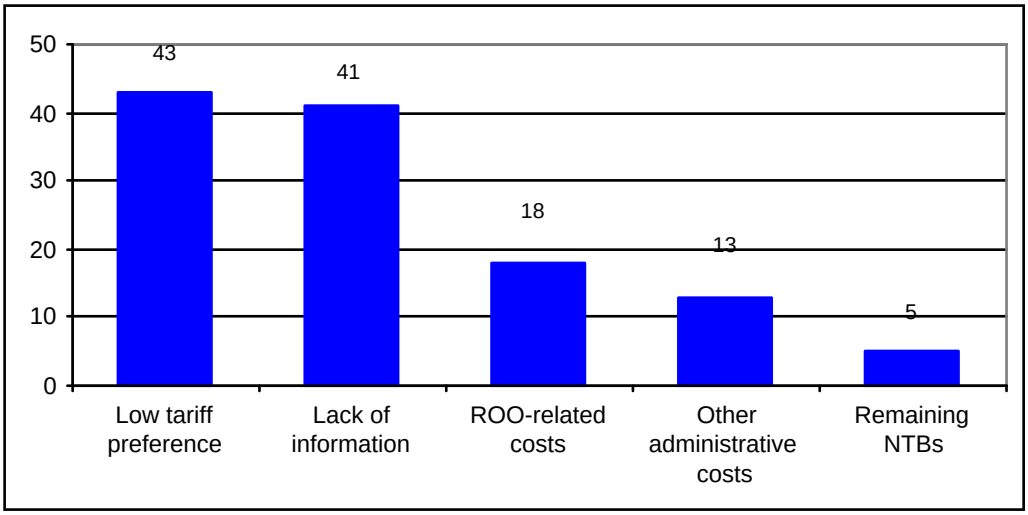
Due to its great geographical distance and small domestic market, only a small number of big corporations have currently advanced into Chile. Accordingly, Korea's many SMEs virtually have no business opportunity there. Moreover, in the subsequent FTAs with Singapore and EFTA, it is difficult for the Korean enterprises to find substantial incentive to utilize the existing FTAs as the FTA preferential-tariff margin is thin since the other party's import market is small or its Most-Favored-Nation (MFN) tariff rate is low or near zero.

The FTA with the ASEAN, which was implemented in June 2007, is in a similar situation. The export-import effects of the Korea-ASEAN FTA were expected to be great since the ASEAN is not only geographically near Korea but also the fifth- to sixth-largest trading partner for Korea. The Korea-ASEAN FTA, however, has not yet produced substantial trade effects since a number of ASEAN member countries effectuated FTAs with Korea only in June 2007: Singapore, Indonesia, Malaysia, Myanmar, and Viet Nam. Korea's regional FTA with the Philippines came into effect only in January 2008, and its FTAs with Brunei, Lao People's Democratic Republic, and Cambodia came into effect only in July, October, and November 2008, respectively. Thailand has only acceded to the ASEAN-Korea FTA in February 2009.

According to the plans agreed upon by Korea and the ASEAN, in principle, both parties should abolish the tariffs on 90% of their imports (based on tariff lines) from each other by 2010 and should lower the tariffs on 7% of the imports (sensitive items) by 0–5% by 2016. For the remaining 3% of the imports, which are ultrasensitive items, diverse protective measures such as permit exclusion, long-term tariff reduction, and the setting up of a tariff quota were put in place. The problem is that Korea's main export items are included in the remaining 3% ultrasensitive items. As such, ASEAN's tariffs on such items, the exports of which Korea expected to sharply increase, were not lowered.

Particularly, the difference between the Korea-ASEAN preferential tariff and the MFN tariff is more or less than 1%, and the FTA preferential level felt by the enterprises is low. Moreover, the expenses to be incurred to meet the rules of origin are also burdens to the enterprises. As the enterprises do not feel the necessity of utilizing the existing FTAs, they will certainly not be willing to bear the burdens associated with the rules of origin. The reasons for not utilizing the FTA preferential tariff that were cited by the respondent enterprises in the 2008 KOTRA survey included the two similar-numbered responses of "having had no substantial tariff preference or having had no actual benefits from such" (39.0%) and "lack of information about the conditions of the existing FTAs or about how to utilize them" (37.3%).

Figure 12: Impediments to FTA Use
(unit: number of firms)



Source: Authors' calculations based on 120 firm samples.

The results of the survey also show that the Korean enterprises are very interested in Korea's FTAs with the US and EU but that since the Korea-US FTA has yet to be ratified by the National Assembly of Korea and the Congress of the US, the enterprises are not able to utilize such FTA. The FTA negotiations with the EU are in the concluding stage, but it will take more than one year for the agreement to be ratified and implemented. The number of Korean enterprises utilizing the existing FTAs may be low, but the number of Korean enterprises planning to utilize the existing FTAs is high. This can be attributed to the fact that Korean enterprises are considering FTAs with big economic blocs such as the US and EU. The results of the survey show that even SMEs are very interested in the conclusion of the Korea-US FTA.

Similar survey results can be seen in the report of Korea Small Business Institute (2007). According to the survey, an absolute majority of SMEs evaluated the Korea-US FTA positively. The business types that gave the response "positive effects" are the textile, image/sound/communication equipment, transportation equipment, other machinery and equipment, and furniture manufacturing. As for the grounds on which the response "positive effects" is based, "expansion of exports to/easy advance into the US" was most cited. Furthermore, the respondent enterprises recognize "enhancement of price competitiveness through imports from the US" (23.8%) and "active inducement of investment from nonmember countries" as the major reasons for the "positive effects."[25] The enterprises that cited "negative effects" responded that they fear the impaired competitiveness of products the most.

In the meantime, Korean enterprises have not sufficiently appreciated the effects of the FTAs with Chile, EFTA, and the ASEAN. The FTA with the US has yet to be ratified, the FTA negotiations with the EU, Canada, and India have been delayed, and the FTAs with Japan and the PRC are feared to harm the Korean industries. Thus, although the effects of the FTAs that have already been concluded are not fully appreciated, and although it is feared that the driving force to promote new FTAs may weaken due to the burden of restructuring, the promotion of FTAs is still an important trade policy.[26]

The fact that Korean enterprises are preparing to utilize the existing FTAs is partly reflected by the results of the survey on the recognition of the rules of origin. When asked whether

[25] Depending on the contents of FTAs, substantial impact on the inflow of investment can be drawn from the conclusion of FTAs. Refer to Donnenfeld (2003) and Raff (2004).

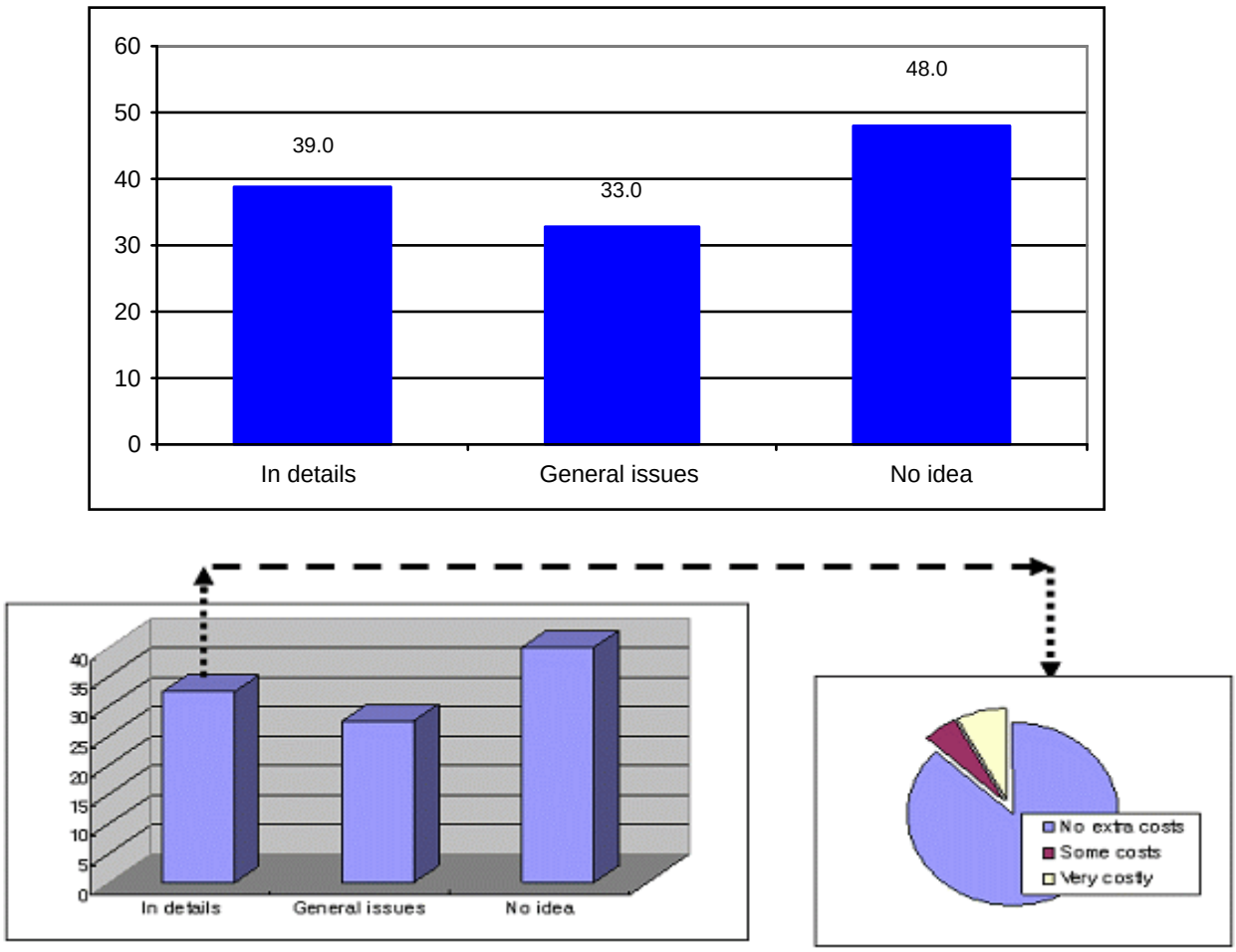
[26] For further discussions, refer to International Trade Institute (2008).

they grasp the ROO of the FTAs that the Korean government has implemented, 72 of the 120 enterprises that had been surveyed responded that they were well aware of them. Of these 72 enterprises, 39 responded that they understand the ROO in detail, including those of their own products, and 33 of these 39 enterprises were found to have no need to bear additional burdens due to the FTA ROO. On the other hand, 40% of the enterprises that had been surveyed were unaware of the rules of origin, and it may be thought that there are big differences in the recognition of the ROO among the enterprises, but this can be interpreted differently. First, it can be pointed out that the SMEs' recognition of the Korean government's FTA policies tends to become polarized. Many enterprises still do not know the ROO, and most of the enterprises that are well aware of them are estimating the costs of meeting such rules. Next, many SMEs in Korea are expecting the coming into effect of FTAs with the big economic blocs. Although Korean enterprises do not feel any urge to utilize the FTAs that the Korean government has implemented so far, they deem it useful to utilize such FTAs to advance into the big domestic market or to expand their exports. In particular, since the Korea-US FTA is a comprehensive agreement and the tariffs on most of the items that Korea exports are to be abolished within three years from the time the agreement comes into effect, the manufacturing industries in Korea are very much interested in it. Since the FTA with the EU is being promoted based on the Korea-US FTA, it can help expand Korea's exports to the EU.

4.5 Perceptions of Rules of Origin

Thirty-nine enterprises that are well acquainted with the FTA rules of origin were asked about whether they find it easy to meet the ROO of the FTAs that the Korean government is promoting. Thirty-three enterprises responded that they find it easy to meet the ROO, two responded that they find it difficult to do so, and four responded that they couldn't do so at all considering their present circumstances.

Figure 13: Awareness of ROOs
(unit: %)



Source: Authors' calculations based on 120 firm samples.

Table 17: Perception of ROO Compliance by Industry
(unit: number of firms)

Industry	Easy	Difficult	Impossible	Subtotal
Auto, parts	3	0	0	3
Electrical goods	2	0	1	3
Machinery	5	0	2	7
Chemicals	5	0	0	5
Textiles	5	0	1	6
Metal, products	5	1	0	6
Sundries	8	1	0	9
Total	**33**	**2**	**4**	**39**

Source: Authors' calculations based on 120 firm samples.

The industries in which the ROO are highly recognized are the sundry, textiles, electricity and electronics, automobile, and machinery industries. The sundry business is the typical business of SMEs; the degree of its recognition of FTAs on the whole is high, and the degree of its recognition of the ROO is the highest, which is regarded as an unexpected result of the survey. The steel and petrochemical industries were found to have a low degree of recognition of the rules of origin, as is the case with the degree of their recognition of

FTAs and of their plans to utilize the existing FTAs. As with the steel industry, the tariff rates on the petrochemical industry are rather low. Since most petrochemical products are interim-inputted goods, many countries, including Korea, impose very low tariffs on them.

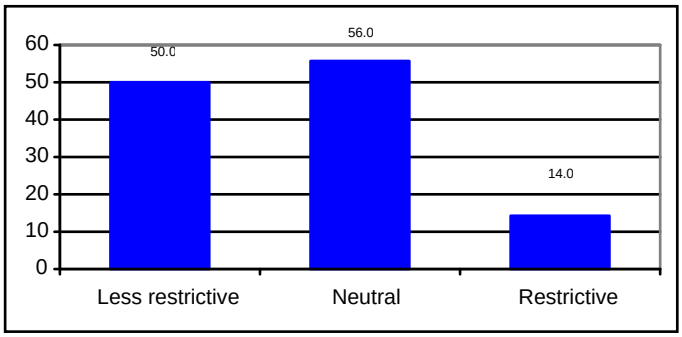
Table 18: Awareness of ROOs by Industry

Industry	In Detail (A)	General (B)	Don't Know	Subtotal (C)	Share ([A+B]/C)
Auto, parts	5	5	7	17	58.82%
Electrical goods	5	6	6	17	64.71%
Machinery	6	3	8	17	52.94%
Chemicals	5	2	11	18	38.89%
Textiles	6	9	2	17	88.24%
Metal, products	4	0	13	17	23.53%
Sundries	8	8	1	17	94.12%
Total	**39**	**33**	**48**	**120**	**60.00%**

Source: Authors' calculations based on 120 firm samples.

Asked how the ROO to be adopted by the Korean government's FTAs could be improved in comparison with the existing ROO, majority of the enterprises responded that it is necessary to adopt a more lenient form of the rules of origin. On the other hand, 14 (12%) of the enterprises surveyed maintained that a more reinforced form of the ROO should be adopted. These enterprises were found to be mainly manufacturing products that are severely competing with imported goods in the domestic market.

Figure 14: ROO Type Preference in Future FTAs (unit: %)



Source: Authors' calculations based on 120 firm samples.

5. CONCLUSION AND POLICY RECOMMENDATIONS

Most of the FTAs that Korea is currently implementing have been concluded with small and medium-sized developing countries. Moreover, in these FTAs, the range of preferential tariffs is not big; as such, only one out of five enterprises was found to be utilizing them. On the other hand, half of the enterprises that had been surveyed responded that they intend to utilize the existing FTAs. These enterprises are thought to have responded so with the implementation of the Korea-US FTA in mind, and most of the enterprises are expecting an early implementation of the Korea-US FTA.

Accordingly, the Korean government should complete the internal ratification of the Korea-US FTA so that it could be implemented early. Owing to the US presidential election, it was difficult for the FTA to be ratified by the US Congress, but Korea should closely consult with the new US administration so that the ratification procedures can be completed in 2009. Moreover, the Korean government should implement the agreement that it concluded with India this year and should also conclude its FTA negotiations with the EU. Further, the Korean government should promote FTAs with the East Asian countries, such as Japan and the PRC.

Lee Myung-bak's government is now promoting strategic FTAs aiming at forming a "global FTA network," but the government should improve its mechanism of coordinating the internal interests. The government intends to secure the world's largest advanced markets through the promotion of FTAs with the big economic blocs (the US and EU), to adopt the economic system of the advanced economies, to establish a national opening-up mindset, and to pave the way for the revamping of less competitive enterprises. The government is also constructing Korea's strongholds by continent by concluding FTAs with Central America (Chile, Mercosur), Southeast Asia (ASEAN), Europe (EFTA, EU), and North America (US, Mexico and Canada). It aims at securing the prior occupation of the emerging big markets through bilateral FTAs with India, PRC, Russia, and GCC.

The promotion of FTAs with Korea's major trading countries is necessary, and the schemes for raising the degree of FTA utilization should also be actively examined. The organization and channel through which FTA-related information that is useful to enterprises can be provided, rather than the unilateral promotion of FTAs, stressing its advantages to the people, should be reinforced. In particular, SMEs cannot grasp not only the contents of the existing FTAs but also the rules of origin for their own products due to their manpower limitations. The system of supporting FTAs for SMEs should be reinforced. Some SMEs utilize FTAs widely, but the rest are virtually indifferent to them. While the current structure used by many SMEs for supplying goods to the big domestic corporations should be taken into account, the FTAs are useful not only for their exports but also for procuring the parts that are necessary for production. In the FTAs that had been concluded by Korea, the rules of origin are strict and complicated. In future FTAs, a more neutral and lenient form of the rules of origin should be adopted.

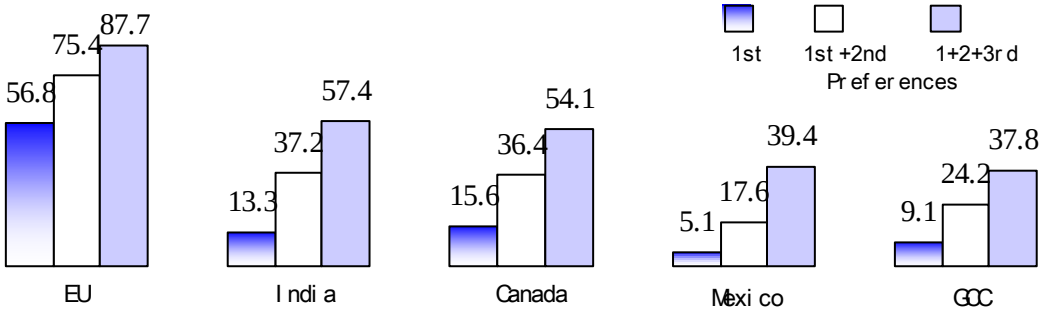
In addition, future FTAs should be approached more elaborately and strategically. The government's procedures for promoting FTAs have been systematized, but the procedures for collecting opinions within the country leave much to be desired. As a result of the top-down approach to the promotion of FTAs that has been employed so far, the matters in which the enterprises are interested have not been properly reflected in the agreements. In advanced countries, bottom-up trade policies are generalized, so the matters that the enterprises are interested in are first put in order, and then the FTAs are promoted to realize these interests. Now, Korea, having concluded FTAs with many countries, should establish the advanced-country-type trade policy structure.

Since the conclusion of the Korea-US FTA, the Korean people have become highly interested in the economic effects of FTAs, but basically, it became difficult to form internal consensus among people on the promotion of FTAs with other countries, even with clear validation of economic feasibility. Moreover, in the course of FTA negotiations, there are limitations to the government's role in maintaining its position in order to reflect opinions of its people. As such, the interested groups, including the industrial circles, should be widely utilized in the course of establishing strategies and collecting relevant data. FTA negotiations that are undertaken without collecting public opinion are much likely to cause conflicts due to the lack of internal understanding of such FTAs and may lead to enormous social costs, as was seen in the candlelight street demonstrations related to American beef imports.

APPENDIX: 2008 KOTRA SURVEY FINDINGS

According to the 2008 KOTRA survey of 505 firms, of the countries with which Korea is currently negotiating an FTA, most Korean enterprises want to conclude an FTA with the EU soon (87.7%), and most Korean enterprises want the government to resume or initiate FTA negotiations with the PRC (74.1%).[27] Of the countries with which FTA negotiations are underway, the EU was cited by most of the respondents (the sum of ranks 1, 2, and 3 make up 87.7%) as the country with which they want an early conclusion of FTA negotiations, followed by India (57.4%), Canada (54.1%), Mexico (39.4%), and GCC (37.8%).

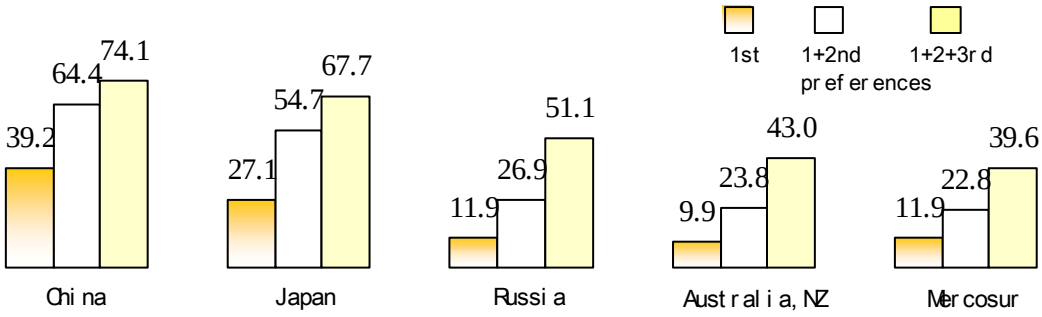
Figure A.1: FTA Preference of Early Conclusion
(unit: %)



Source: KOTRA (2008)

The majority of the respondents want FTA negotiations to be resumed or initiated for the PRC (74.1%), followed by Japan (67.7%), Russia (51.1%), Australia and New Zealand (43.0%), and Mercosur (39.6%).

Figure A.2: FTA Preference for Early Start of Negotiation
(unit: %)

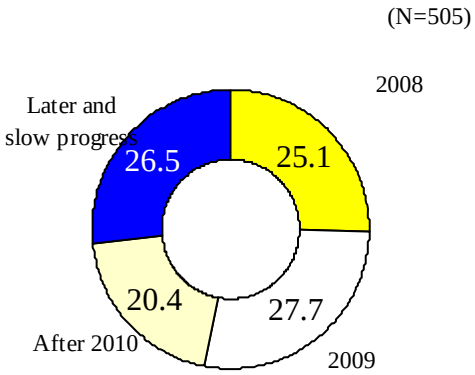


Source: KOTRA (2008)

Meanwhile, many enterprises are highly interested in the early implementation of the Korea-US FTA. According to the 2008 KOTRA survey, seven out of 10 respondents (69.1%) indicated that the Korea-US FTA should be ratified in 2008. About half of the respondent companies indicated that the promotion of a Korea-Japan FTA and a Korea-PRC FTA should begin in 2009, but a considerable number of respondents opined that, considering the long-term effects of such FTAs, their promotion should begin after 2010.

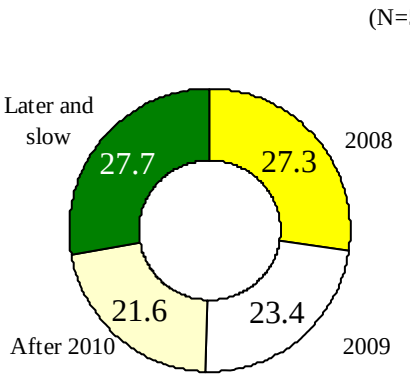
[27] KOTRA's survey reported the sum of those ranking 1st-2nd-3rd in the priority order and the total sums come to 300%.

Figure A.3: Preferred Time for Resuming Negotiation for a FTA with Japan (unit: %)



Source: KOTRA (2008)

Figure A.4: Preferred Time for Resuming Negotiation for a FTA with the PRC (unit: %)



Source: KOTRA (2008)

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