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Policy Brief

Korea's Tariff Rate Quota System: Impact of the Doha Development Agenda Proposals

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February 15, 2011

IATRC Policy Brief #PB2011-06

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The quota under-fill mechanism currently proposed under the Doha Round of trade negotiations is likely to increase Korea's tariff rate quota (TRQ) imports of agricultural products by 30 percent. If Korea wishes to pursue the objective of minimizing import competition, it may be preferable to implement the proposed reduction in tariffs in full for some products, rather than adopting smaller tariff reductions and higher TRQs.

One of the achievements of the Uruguay Round of trade negotiations (1986-1994) was that agricultural trade was finally covered under the General Agreement on Tariffs and Trade (GATT). Non-tariff barriers were converted into tariffs; limits were imposed on the most trade-distorting government subsidies; and restrictions were placed on the volume and value of subsidized exports. However, tariffs for many commodities remained at high levels. Thus, to guarantee exporters at least some access to markets for highly-protected commodities as well as to increase the transparency of trade policies, the Uruguay Round also created a tariff rate quota (TRQ) system that allows a certain volume of imports to enter a country at a lower in-quota tariff, while imports that exceed the quota face a higher out-of-quota tariff.

The current negotiations under the Doha Development Agenda (DDA) of the World Trade Organization (WTO) include proposals that are likely to affect the ways that TRQs are administered and create greater competition from imports. A particular challenge for TRQ administration has been the issue of under-filled quotas (or low fill rates), which occurs when the volume of imports is below the quota. Thus, a quota under-fill mechanism has been proposed that requires an importing country to modify or correct its administration methods if the quota fill rate falls below 65 percent (WTO, 2008).¹ To address the resulting increase in competition from imports, the DDA proposals also include a provision allowing countries to make a tradeoff between tariff reductions and TRQ expansion. Under this provision, a country would have the option of declaring a certain number of tariff lines (to be determined) as "sensitive products" (i.e., those most susceptible to competition from imports), which would then be subject to smaller tariff reductions than other products. However, if these sensitive products are subject to TRQs, their quotas would be increased instead.

The current TRQ system is very important to Korea, providing protection for a range of Korean commodities. TRQ imports accounted for an average of 22 percent of Korea's total agricultural imports during the 1995-2006 period and 48 percent of the total value of agricultural production between 2002 and 2007. Korea has a relatively complicated TRQ system that uses a range of administration methods. In particular, imports of the most sensitive products (e.g., rice, garlic, red pepper, potatoes, sesame seed) are handled by state trading entities. These sensitive products accounted for 32 percent of the value of Korea's agricultural production and 2 percent of the value of agricultural imports over the 2002-05 period. A unique feature of Korea's TRQ system is that producer groups handle imports of certain products, including pine nuts and mandarins (Korean citrus).

Given the importance of the TRQ system to Korea and the nature and extent of the changes proposed under the DDA, an empirical study was conducted to analyze the operation of Korea's TRQ system and to assess the potential impacts of the proposed changes concerning TRQ administration and sensitive products (Lim and Blandford 2009).



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The results of the analysis confirm that the method used to administer quotas has a significant impact on Korea's imports under the TRQ system. In particular, state trading was found to have a large, positive effect on fill rates, while auctioning (under which the government sells the right to import the amount determined by the quota) and the administration of quotas by producer groups were both found to have large negative effects on fill rates. The fill rate for TRQs administered by producer groups averaged only 42 percent between 1995 and 2004, compared to a fill rate of 184 percent for TRQs administered under a state trading method over the same period. This low fill rate was expected since producers generally seek to protect domestic markets. Thus the results suggest that there is room for improvement in the administration of quotas, particularly by producer groups.

The study finds that the proposed quota under-fill mechanism would have a substantial impact on Korea. In order to achieve the benchmark fill rate of 65 percent, imports of Korea's current TRQ products would have to increase by approximately 30 percent. It would be difficult for Korea to achieve the benchmark for products that face weak domestic demand. Thus, from a trade policy perspective, the proposed quota under-fill mechanism may be a double-edged sword. That is, while it may reduce inefficiencies in quota administration, the risk of importing unwanted products would also increase. If a country has to import a good regardless of market conditions, the policy could add to inefficiencies and create distortions.

The study also conducted a tariff-quota equivalency test to assess whether it would be in Korea's interest to use the proposed sensitive products provisions. The analysis suggests that if Korea wishes to minimize the increased import competition that would result from the DDA proposals, it needs to carefully consider its choice of sensitive products. The study finds that for some products it may be preferable to implement the proposed reduction in tariffs in full, rather than adopting smaller tariff reductions and higher TRQs, especially given the greater scrutiny quota fill rates would receive under the proposed under-fill mechanism. More specifically, the analysis indicates that for beef, pork, poultry, skim milk powder, whole milk powder, soybeans, jujube, mandarin, potatoes, sweet potatoes, red pepper, garlic, onion, ginseng, pine nuts, chestnuts, and natural honey, the increase in imports would be smaller if the tariff reductions are implemented in full. However, for groundnuts, buckwheat, barley, ginger, sesame seed, and red bean, the sensitive product designation would likely result in smaller increases in imports. It is important to note that other issues may be relevant when assessing the tradeoff between reducing tariffs and increasing quotas. For example, the quantity of imports is more predictable under a quota system than under a tariff-only scheme. Such stability may be a priority for policy makers and domestic interest groups, particularly agricultural producers.

In summary, Korea is likely to face difficult choices in implementing any Doha Round proposals that involve a significant increase in market access for agricultural products. Since it appears unlikely that an agreement can be reached without concessions on market access, Korean producers may require assistance to adjust to these changes and to adapt to the resulting increased competition from imports.

References

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This research was supported by the William and Flora Hewlett Foundation through their generous support of the Hewlett/IATRC Capacity Building Program.

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