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# **In Search of a Breakthrough for the Korea-EU FTA Negotiations**

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# **In Search of a Breakthrough for the Korea-EU FTA Negotiations**

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*Abstract* : The purpose of this paper is to seek a breakthrough for the Korea-EU FTA negotiation in agriculture which started last year, but has not made much progress yet. The EU has been asking Korea to open its agricultural market to the same extent that was agreed upon in Korea's free trade agreement with the U.S. while the Korean government firmly opposes the EU's request, saying that FTA negotiations differ from multilateral trade talks as in the WTO. An examination of agricultural trade among Korea, the EU, and the U.S. shows that there may be many niche markets of which the EU can take advantage over other agricultural exporting countries including the U.S. Also, it is expected that the EU could gain much from its agricultural trade with Korea through an FTA, even without a market access level equal to one stipulated in the Korea-U.S. FTA accord. As far as agriculture is concerned, the slower does the talk proceed, the better to Korea, with the EU losing huge expected trade gains. It is suggested that the EU needs to be more flexible in the talks by focusing on a new strategy that can maximize trade diversion effects stemming not only from price but from non-price factors, rather than simply asking for the same level of market opening as in Korea-U.S. FTA. This would be the better way for the EU to become a winner in the battle for Korean agricultural market.

*Key words* : Korea-EU FTA, Agricultural Trade, Trade Diversion Effects

## **I. INTRODUCTION**

The negotiations for the Korea-EU free trade agreement started last year, but they have not made much progress yet although it is widely believed that the economic gains as a whole from the accord will be substantial for both sides. Agriculture lies at the center of the lingering talks as it holds the key to striking the deal.

The EU has been asking Korea to open its agricultural market to the same extent that was agreed upon in Korea's free trade agreement with the U.S. In other words, the EU claims that the Korea-U.S. FTA (hereinafter KORUS) should serve as a guideline in determining the level of agricultural market access in the Korea-EU FTA. The Korean government, however, firmly opposes the EU's request, saying that FTA negotiations differ from multilateral trade talks as in the WTO (world trade organization), and that the Korea-EU FTA must proceed on an individual basis, independently of the result of KORUS. The big gap between the two sides' stances over the EU's access to Korean agricultural market does not seem to be easily narrowed unless each side's current positions are changed.

The purpose of this paper (poster) is, therefore, to seek a breakthrough for the Korea-EU FTA negotiations in agriculture by providing new directions to resolve the controversy described above. First, we will briefly look at the Korea's overall tariff structure for agricultural products, followed by the KORUS results. Then, the agricultural trade among Korea, the EU, and the U.S. will be examined. Finally, an attempt will be made to seek new strategies to break the deadlock, and successfully reach an agreement in the negotiation process for the Korea-EU FTA.

## II. KOREA'S TARIFF STRUCTURE FOR AGRICULTURAL PRODUCTS

It is well known that Korea is one of the world's most protective countries in agriculture, with the average tariff rate for agricultural products being as high as 60%. According to the H.S. 10 digit classification, the share of agricultural products with extremely high tariff rates of over 500% accounts for 3.2 percent as shown in table 1. Sesame, ginseng, and barley for beer are those items falling into this category. The number of agricultural products with tariff rates higher than 100% reaches 126, or 8.8% of the total.

But most agricultural products, say 77.1%, come into the categories with their tariff rates of less than 50%. The tariff rates for most fruit and vegetables, and beef range from 40% to 50% something. Dairy products are included in the category with 30-39% tariff rates, chicken and pork 20-29%, and grains less than 20%, respectively.

[Table 1] Korea's Import Tariffs for Agricultural Products

Import Tariff Rates (%)	Number of Items (H.S. 10 digits)	Major Products
Over 500	46 (3.2 %)	Sesame, Ginseng, Barley for Beer
200 – 499	62 (4.3 %)	Soybean, Potato, Sweet Potato, Garlic, Pepper,
100 – 199	18 (1.3 %)	Milk Powder, Citrus, Barley Powder, Onion
50 – 99	189 (13.0 %)	Orange, Fruit Mixed Juice
40 – 49	132 (9.1 %)	Fruits, Beef, Mushroom, Watermelon, Cucumber, Carrot
30 – 39	147 (10.1 %)	Cheese, Milk Products, Fruit Beverage
20 – 29	249 (17.1 %)	Chicken, Pork, Frozen Vegetables
10 – 19	381 (26.2 %)	Grain Products, Water
0 – 9.9	212 (14.6 %)	Wheat, Seeds

Source: Ministry of Agriculture, *DDA Trade Negotiations on Agriculture*, 2007.

## III. RESULTS OF KOREA-U.S. FTA NEGOTIATIONS

According to the Korea's tariff elimination schedule for agricultural products agreed upon in the KORUS, the import tariffs for 578 (37.9%) items out of 1,531 are to be eliminated at the time of the agreement taking effect. These include grape juice, wine, flowers, and wheat. This figure accounts for 55.8 percent of total import value. 86.6 percent of total agricultural products will completely lose their protective border measure of tariff within ten years after the accord comes into effect. The agricultural products for which import tariffs are to be cut down to zero within eleven to fifteen years account for 8.7 percent, including beef, chicken, egg, and some fruit and vegetables. Some products such as apple (Fuji), pear, and sugar have much longer grace periods in tariff elimination for up to 20 years, considering their importance in Korea's agriculture.

For some agricultural products, it has been agreed upon to use other measures like seasonal variable rates and TRQ (tariff rate quota) along with tariff elimination to open their import markets. Cheese, butter, and barley are those examples to which the TRQ rule will be applied along with tariff elimination for 10-18 years as well. There is one exception to market opening with the U.S., i.e. rice, which is exempted from any import concessions.

#### IV. AGRICULTURAL TRADE AMONG KOREA, EU, AND US

The EU is increasingly becoming an important partner for Korea in agricultural trade, especially in import. In 2006, for example, Korea imported a total of 13.3 billion dollars worth of agricultural products, of which 1.4 billion dollars (10.9%) flowed in from the EU, whereas agricultural export to the EU was only 46 million dollars that amounted to 2.0% of the total agricultural exports of 2,304 million dollars. Table 2 indicates that Korea's agricultural import from EU has significantly increased for the past four years, with export remaining unchanged or even decreasing. As a result, Korea's trade deficit against EU in agricultural sector reached over 1.4 billion dollars in 2006. The deficit is predicted to continue to widen considering the recent export and import trends as shown in table 2.

[Table 2] Korea's Agricultural Trade with EU (thousand US\$)

	2002	2003	2004	2005	2006
Export	35,440	44,202	51,150	51,642	46,194
Import	1,032,091	947,513	1,121,927	1,351,985	1,454,472
Trade Surplus	-996,651	-903,311	-1,070,777	-1,300,343	-1,408,278

Source: Korea Rural Economic Institute, *World Agriculture News*, No. 87, 2007.

Table 3 shows the agricultural import values from the EU by product, and compares them with those from the U.S. Korea imports more pork, milk powder, barley, starch, wine and whiskey from EU than from the U.S. The beef and chicken trade was directly affected by the occurrences of livestock diseases and showed a sharp fluctuation in trade volume each year.

[Table 3] Korea's Agricultural Imports from EU and U.S. (2005 – 2007 average)

Items	Import Value ( thousands US\$ )			Unit Import Prices (\$/ton)	
	EU	U.S.	World	EU	U.S.
Beef	157 (0.02)	32,684 (3.7)	883,724	2,661	6,590
Pork	373,755 (48.7)	184,986 (24.1)	767,229	2,697	2,293
Chicken	19,606 (16.8)	30,475 (26.1)	116,972	1,921	1,128
Cheese	23,518 (15.1)	27,552 (17.6)	156,275	5,418	3,979
Skim milk Powder	2,684 (17.0)	179 (1.1)	15,758	3,092	4,475
Mixed Powder	50,253 (50.4)	4,142 (4.2)	99,663	2,766	2,919
Soybean	0 (0.0)	186,994 (48.3)	387,130	-	308
Barley	2,650 (4.3)	2,075 (3.4)	62,012	434	537
Potato	1,089 (2.3)	33,574 (70.1)	47,926	1,360	888
Corn (food)	2,576 (0.8)	51,475 (15.4)	333,464	393	188
Corn (feed)	278 (0.03)	663,095 (59.9)	1,107,800	167	172
Grape	8,509 (12.9)	21,352 (32.3)	66,037	1,287	1,810
Orange	1,430 (0.8)	124,196 (73.1)	169,924	1,172	1,131
Starch	20,952 (38.0)	125 (0.2)	55,128	659	3,289
Wine	59,791 (58.5)	12,903 (12.6)	102,209	4,684	3,068
Whiskey	237,779 (98.4)	3,212 (1.3)	241,735	11,466	5,082

Notes: Numbers in parentheses are the import shares of world total (%). Unit import prices have been calculated by dividing imported value by quantity imported for each product, indicating average import prices in terms of c.i.f.

## V. SUGGESTIONS FOR SUCCESSFUL CONCLUSION OF THE TALKS

The EU's strategy needs to be changed to push the talk toward a successful conclusion, which will bring them significant agricultural trade gains. First of all, the EU might want to look at trade diversion effect between the EU and other exporting countries including the U.S. The EU needs to search for niche markets where they are more competitive than the U.S. They will be able to increase agricultural export to Korea without much expansion of Korea's total import by taking advantage of the trade diversion effect so that they can maximize the gains from FTA with Korea.

Table 3 shows that the EU may have many products that are more cost efficient compared to the U.S., such as skim milk powder, grape, starch, etc. The starch from the EU, for example, is much cheaper than the US's, implying that the EU starch even with smaller tariff cut could have more price competitiveness in Korean market compared to the US's.

Trade diversion effect can also occur from non-price factors such as quality variety, brand loyalty, geographical character, etc. The import values for pork, wine, and whisky from the EU are much more than those from the U.S., while their unit import prices are much higher than those from the U.S. as in table 3. In particular, the average price for whisky imported from the EU more than doubles the price from the U.S., whereas its import value from the EU accounts for 98.4 percent of the total. This implies that non-price factors are very important in determining the import flows of agricultural products into Korean market. There may be many agricultural products, such as pork, wine, and whisky, in which the EU has strong competitiveness in non-price factors against the U.S. in Korean market. Import tariffs on these items are 25%, 15%, 20%, respectively. The effect of tariff cut on these products might not be so substantial.

Another important point to be noted is that there may be many products for which the combined shares of the EU and the U.S. are very small compared to the world total, including barley, corn (food), and beef as in table 3. By concluding the Korea-EU FTA, the EU could gain much in these markets. In such markets, the EU could increase export to Korea without keenly competing with the U.S.

To what extent the tariff for agricultural products should be cut needs to be judged on an individual product basis considering not only price-related factors but also various non-price aspects discussed above. The EU should not stick to price aspect alone by requesting the same market opening as in KORUS. Korean government's counter argument that an FTA deal differs from multilateral trade talks does not seem to be unreasonable. Rather, the better strategy for EU is to conclude the FTA with Korea as quickly as possible even though the level of tariff cut is not the same as that of KORUS. Once the deal is signed and implemented, the EU will definitely gain in agricultural sector.

## VI. CONCLUSIONS

The Korea-EU FTA is expected to have significant adverse impacts on Korean agriculture, assuming that the EU's request will be realized. This is why many people in Korea believe that the FTA talks underway may fail if Korean farmers face the same market opening as in KORUS for all agricultural products. Under this circumstance, it is highly unlikely that Korean government accepts the EU's request at the risk of being criticized by local farmers and the public as well.

The EU could definitely gain from its agricultural trade with Korea through an FTA, even without a market access equal to one stipulated in KORUS. There may be many niche markets of which the EU can take advantage over other agricultural exporting countries including the U.S. As far as agriculture is concerned, the slower does the talk proceed, the better to Korea, with the EU losing huge expected trade gains.

The EU needs to show more flexibility in the talks to increase agricultural exports to the Korean market. They should focus on a new strategy that can maximize trade diversion effects stemming not only from price but from non-price factors, rather than simply ask for the same level of market opening seen in KORUS. This would be the better way for the EU to become a big winner not a loser in the battle for the Korean agricultural market.

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