

# Chapter 3

## To Improve the Use of FTA: Lessons learned from Korea

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## Chapter 3

### To Improve the Use of FTA: Lessons learned from Korea

Inkyo Cheong

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*Although Korea has been successful in concluding free trade agreements (FTAs), it has faced difficulties in increasing FTA utilisation by small and medium enterprises. Since there has been substantial progress in building institutional infrastructure as part of the Korean government's active policy of FTA utilisation assistance, FTA utilisation ratios are as high as those of advanced countries. Several policy implications can be drawn from Korea's experience in assisting businesses with FTA utilisation. (i) One of the most urgent and important tasks in assisting FTA utilisation is to identify the barriers that prevent companies from utilising FTAs. Critical barriers may differ from country to country. (ii) Coordination amongst national agencies is critical in increasing the efficiency of the infrastructure assisting FTA utilisation. (iii) Governments should promote FTAs with large economies, which are expected to bring big economic gains. (iv) Authorities of trade and industry should understand the importance of the quality of FTAs. (v) FTA member countries should take advantage of various levels of committees institutionalised in FTAs.*

## 1. Background

Korea has established a very wide free trade agreement (FTA) network by implementing 15 FTAs with 50 countries, and the utilisation ratios of these FTAs are fairly high, ranging from 40 percent to 80 percent as of December 2013, although the rates differ depending on the method of measurement, and some FTAs record poor performance in terms of FTA utilisation. Korean companies' utilisation ratios of FTAs were quite low five years ago, and some suspicions regarding the benefits of FTAs were raised, despite their active promotion by the government.

Today's good performance has been achieved thanks to the strategic approach and diverse support mechanisms initiated by the government of Korea since 2010. This goes back to the period of 2007–2009. When the Association of Southeast Asian Nations (ASEAN)–Korea FTA was implemented in June 2007, Korean companies had high concerns over the FTA with ASEAN, which is geographically close and Korea's fifth to sixth largest trading partner. However, it was reported that only few companies were utilising the FTA in exporting their products to ASEAN countries. Despite the official announcement by the government of Korea on the implementation of the ASEAN–Korea FTA, only five ASEAN member countries officially effectuated the ASEAN–Korea FTA, and some countries were not ready to implement the agreement.<sup>1</sup> Moreover, the tariff rates were only partially liberalised, and the tariff schedules of the FTA were fairly complex. It was difficult for Korean businessmen to comprehend the tariff schedules given in the FTA without a high level of knowledge of FTAs.

Surveys revealed that utilisation rates for Korea and Japan were 21 percent and 29 percent, respectively. The surveys by KOTRA (2008), KITA (2009), and Cheong (2008, 2009) had similar findings. Most of the FTAs that Korea implemented this time were concluded with small and medium-sized developing countries. Moreover, in these FTAs, the preferential margin of tariffs is not big; as such, only one out of five enterprises was found to be utilising FTAs in Korea. On the other hand, half of the enterprises that had been surveyed responded that they intended to utilise FTAs in the future. These Korean enterprises are thought to have responded with the implementation of the Korea–US FTA

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<sup>1</sup> Those five ASEAN countries were Indonesia, Malaysia, Myanmar, Singapore, and Viet Nam.

in mind, and most of the enterprises were expecting its early implementation.

Korea was embroiled in a controversy over the negotiation of the Korea–US FTA when the ASEAN–Korea FTA became effective. Anti-FTA groups advocated the cancellation of the FTA with the US, and the government of Korea was criticised for its handling of various aspects of the deal. The poor utilisation rates of the FTA with ASEAN were used as one of the arguments against the Korea–US FTA. That is, even though the government promoted the economic gains of FTAs to the general public, low utilisation rates meant a contrary outcome; a similar argument could apply regarding the Korea–US FTA. The controversy over the Korea–US FTA continued in 2008 and 2009 – more sensitive issues were raised over various areas such as the investor–state dispute settlement mechanism (ISD) and mistranslations of the agreement into Korean.

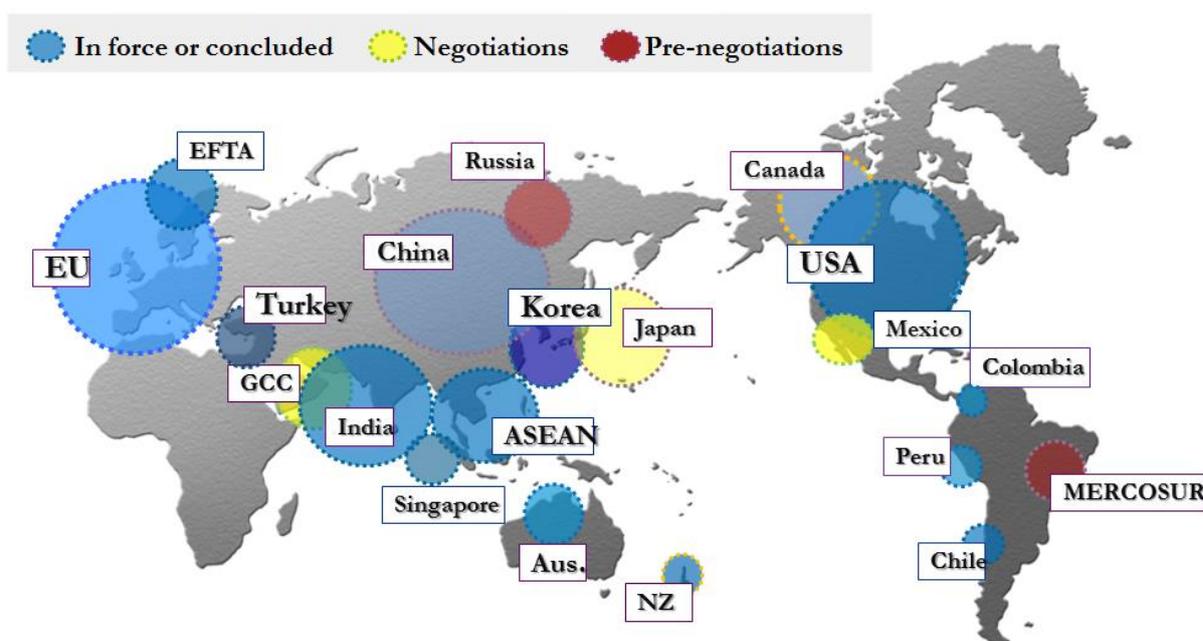
For the FTA with the US to be implemented, it had to be ratified by the National Assembly (congress), and the government planned to ratify the FTA in 2009. However, with the exception of the FTA with Chile, Korea's low utilisation of its FTAs did not improve, and along with other issues could be regarded as a critical pretext for rejecting the agreement. Therefore, improving the utilisation rates of existing FTAs became one of the most urgent tasks for the trade authority in 2009–2010. A more serious issue was the fact that most small and medium enterprises (SMEs) did not utilise FTAs, and were losing interest in the government's FTA policy, as it seemed FTAs are beneficial to large companies, whereas most of SMEs suffer as a result of trade liberalisation under FTAs.

The Korean enterprises, on the whole, consist of a small number of big corporations (one percent of the total number of companies in Korea) and a large number of SMEs. Most of the 30 largest Korean corporations are classified as multinational corporations, whose exports account for roughly 70 percent of Korea's total exports. These corporations are not only favourably inclined towards the government's FTA policies, but are also actively utilising the existing FTAs for their respective businesses. It is not difficult for them to utilise the existing FTAs as they have considerable manpower that can be dedicated to the task. However, most SMEs did not fully recognise the roles of FTAs in expanding their international businesses, and have not secured the dedicated manpower for international trade in utilising FTAs (Cheong and Cho 2009b).

## 2. Korea's FTA Performance

Korea's participation in the global trend of regionalism started with the implementation of its FTA with Chile in April 2004. Ten years later, Korea had established one of the widest FTA networks in the world. Korea's FTA partners are the US, the European Union (EU), China, Canada, Australia, India, ASEAN, Turkey, Colombia, Peru, and Chile. Korea has established free trade infrastructure with 50 countries through the conclusion of 12 FTAs, covering about 60 percent of world economy.

Figure 3.1: Korea's FTA Network



Source: Prepared by the author based on Cheong (2013).

Korea signed an FTA with China in February 2015, expecting the implementation of the FTA in 2016. It also started negotiations on a China–Japan–Korea (CJK) FTA and the Regional Comprehensive Economic Partnership (RCEP) agreement in the first half of 2013. FTAs with Japan, Mexico, and the Gulf Cooperation Council (GCC) are progressing slowly, compared with currently effective (concluded) FTAs. Korea is in discussions about FTAs with the Russian Federation, the Trans–Pacific Partnership (TPP), and the South American Common Market (MERCOSUR).

**Table 3.1: Korea's FTA Performance**

	<b>Country and Region (Key time)</b>
FTAs implemented (concluded)	Chile (implemented in April 2004) Singapore (March 2006) EFTA (September 2006) ASEAN (June 2007) India (January 2007) EU (July 2009) US (March 2007) Turkey (May 2013) Colombia (to be implemented in 2015 after ratification) Australia (December 2014) Canada (January 2015) China (to be implemented in 2016)
FTA partners under official negotiation	Japan, China–Japan–Korea Regional Comprehensive Economic Partnership (RCEP) Mexico, Gulf Cooperation Council (GCC), New Zealand
FTAs under consideration	Trans-Pacific Partnership (TPP), Russian Federation, South American Common Market (MERCOSUR)

Source: Compiled from various sources.

It can be said that Korea has been one of most successful countries in concluding FTAs with major trading partners in the world during the last decade. In addition to the high number of FTAs Korea implemented and concluded, Korea's FTA policy has been developed step by step in terms of quality, and its recent FTAs with developed economies are very broad in terms of market access and comprehensive in coverage. That is, Korea has concluded 'deep and comprehensive' FTAs. Especially, the Korea–US (KORUS) FTA is likely to be the world's most exemplary, the most advanced FTA in existence today.

In spite of establishing a wide FTA network, the government of Korea has been criticised because of low FTA utilisation ratios. Although the country has provided several FTA support programmes for companies since 2007, most companies had difficulties in utilising FTAs. In 2009–2010, Korea introduced a comprehensive package for supporting companies in terms of FTA business information, various programmes for staffs of trade companies, graduate courses for FTA experts, FTA business models for beginners, and a 'toll-free' phone number for free consulting on how to use FTAs. Korea has also been trying to improve the efficiency of the package from a company perspective. FTAs have become a basic part of the infrastructure for most trading companies.

### 3. Barriers against FTA Utilisation

The Korean trade authority reviewed the status of FTA utilisation and made a commitment to prepare a government-level policy package for FTA utilisation by private companies in 2010. At this time, the pros and cons of the US–Korea FTA were being fiercely debated in Korea, and the government at the time needed to increase the level of support for the FTA in the business sector. The low utilisation ratio of existing FTAs was an appealing logic against the ratification of the US–Korea FTA, as it suggested that the economic gains from the implementation of the FTA would be smaller than the government's estimates.

Low utilisation of FTAs was reproved in governmental survey for manufacturing companies and trading ones. Before the policy package for FTA utilisation was created, extensive research on the FTA utilisation ratios for each FTA, and major factors discouraging the utilisation of FTAs were identified. It became apparent that most companies were in the misunderstanding that the implementation of FTAs would automatically bring them economic gains, without the need for any action on their part. Private companies argued that the government had promoted a similar message to gain the support of the Korean people.

Korea was able to conclude negotiations for bilateral FTAs with Singapore, the European Free Trade Association (EFTA), ASEAN, India, the US, and the EU in the five-year period from 2004 to 2008 due to the high trade performance of its first FTA with Chile, which had been implemented in April 2004. However, similar performances failed to materialise for subsequent FTAs. Several surveys at that time showed that most companies did not take advantage of the FTAs being implemented. The finding that most of the companies surveyed were not properly utilising the FTA preferential tariffs was also substantiated by the results of the KOTRA (2008) survey, which showed that only 19 percent of all respondent firms were utilising FTA preferential tariffs. A survey by Cheong (2008) provided a similar result – only 21 percent of firms utilised FTAs in their business in applying preferential tariffs.

Cheong (2009) reported that the majority of Korean businessmen were unaware of the implementation of FTAs, and their perception was not very favourable regarding FTAs, despite the government of Korea promoting the message that FTAs would provide

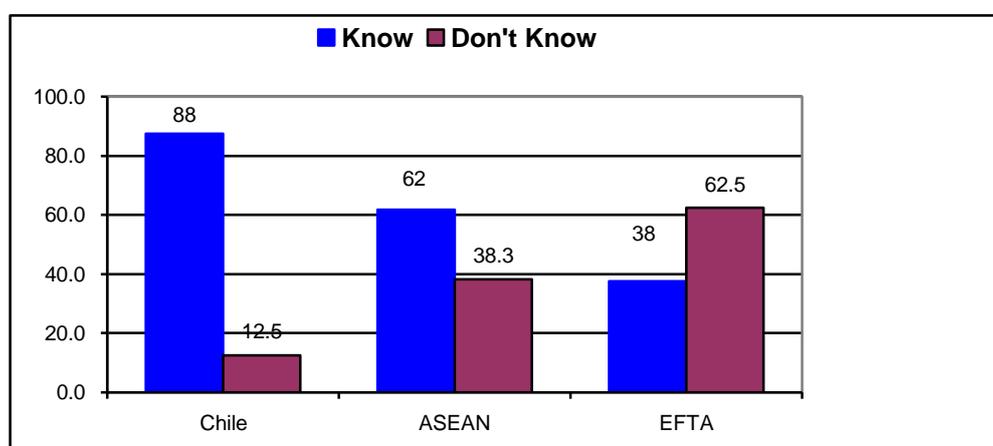
lucrative business opportunities for Korean companies. Over the past several years, Korea's foreign-trade authorities have extensively publicised the promotion of FTAs amongst the Korean people, with the aim of increasing political support for its FTA policy and enhancing the policy environment for more active promotion of FTAs.

### Survey results of 2008–2010

The survey was carried out in relation to three FTAs – with Chile, ASEAN, and the European Free Trade Association (EFTA) – which were implemented in 2009.<sup>2</sup> The enterprises that responded to the survey included 221 SMEs that manufacture automotive parts, electrical goods and parts, machinery, petrochemicals, textiles, steel and metal products, and sundries. These companies were selected from across the country to minimise bias resulting from data selection.

The survey result showed wide differences in the perception that the Korean enterprises recognise the implementation of FTAs. The enterprises' degree of recognition of the countries in which FTAs have become effective was highest for the FTA with Chile – 88 percent of responding companies knew of the implementation of the FTA with Chile, followed by the FTA with ASEAN (62 percent), and that with EFTA (38 percent), according to the survey by Cheong and Cho (2009a).

**Figure 3.2: Perception of Implemented FTAs (%)**

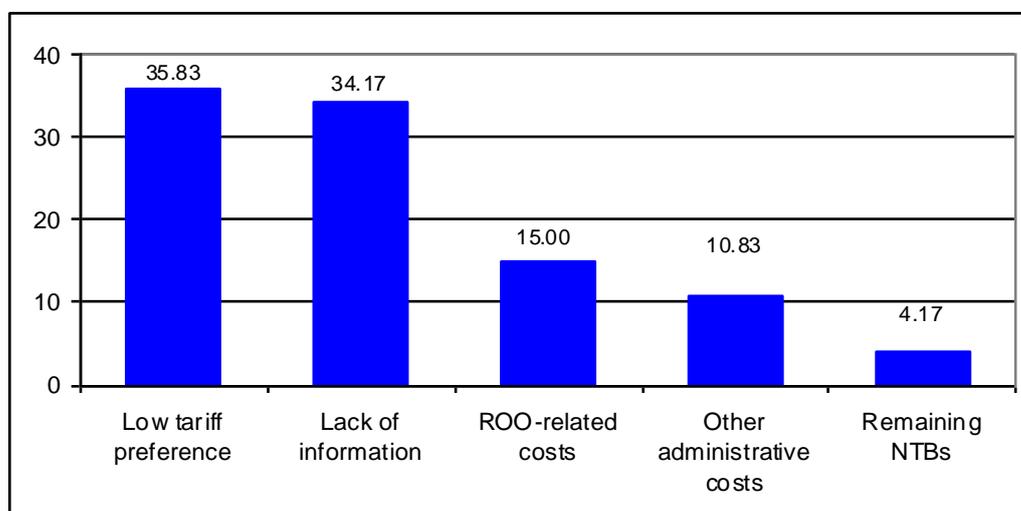


Source: Cheong and Cho (2009), 'Barriers in Korean Businesses' FTA Utilization'.

<sup>2</sup> The Korea–Singapore FTA was under implementation at the time of the survey, but this was not included in the survey since its most-favoured nation (MFN) tariff rate is low or near zero.

Several impediments were identified by the survey. Contrary to initial expectations, small tariff preference, that is, low incentive for utilising FTAs, was the most frequently cited reason for not utilising FTAs, followed by lack of information, difficulties related to rules of origin (ROO), and other administrative costs.

**Figure 3.3: Impediments to FTA Use (%)**



Source: Cheong and Cho (2009), ‘Barriers to Korean businesses’ FTA utilization’.

**Table 3.2: Barriers to Korean Businesses’ FTA Utilisation**

		1 <sup>st</sup>	2nd	3rd	4th
Imports		Lack of FTA information	Problems with ROO	Low tariff margins	Other
Exports	Survey 1	Lack of FTA information	Problems with ROO	Importers’ intention for using FTAs	Other institutional barriers
	Survey 2	Low tariff margins	Lack of FTA information	Importers’ business mind	Customs clearance

Source: Cheong and Cho (2010), ‘Barriers in Korean businesses’ FTA utilisation’.

Whilst the barriers to Korean businesses’ FTA utilisation that had been identified were slightly different for imports and exports, the most significant barriers were a lack of

FTA business information, difficulties in satisfying ROO, low tariff preferential margins, and a lack of importers' business mind in utilising FTAs in partner countries. These barriers could not be alleviated within a short period of time, as it requires a lot of resources and efforts to institutionalise an infrastructure for providing FTA business information. Some tasks such as raising low tariff margins and improving importers' FTA business mind could not be achieved without co-operating with the governments of FTA partner countries.

Low tariff preference was closely related to the FTA with ASEAN, which was implemented in June 2007. During the negotiation period of the ASEAN–Korea FTA, its effects were expected to be great since ASEAN is not only geographically close to Korea but is also Korea's fifth or sixth-largest trading partner in 2006. But the ASEAN–Korea FTA has not yet produced substantial trade effects. According to the FTA's market access provisions, both parties were supposed to abolish tariffs on 90 percent of their mutual imports (based on tariff lines) by 2010, and should lower tariffs on 7 percent of imports of sensitive items from 0 to 5 percent by 2016. For the remaining three percent of imports, which are ultra-sensitive items, various protective measures such as import permits, 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 three percent ultra-sensitive items category. Consequently, ASEAN's tariffs on such items, exports of which Korea had expected to increase sharply at the time of the FTA negotiations, were not lowered.<sup>3</sup>

In particular, the difference between the Korea–ASEAN preferential tariff and the MFN tariff is close to 1 percent, and the FTA preferential level felt by the enterprises is low. Moreover, the expenses that must be incurred to meet the ROO are also burdens on the companies that utilise FTAs. As Korean companies did not see enough economic incentives to utilise the then-effective FTAs, they were certainly not willing to bear the burdens associated with the ROO. This implied that companies were losing opportunities to prepare themselves for organising FTA utilisation. Depending on the survey, a majority

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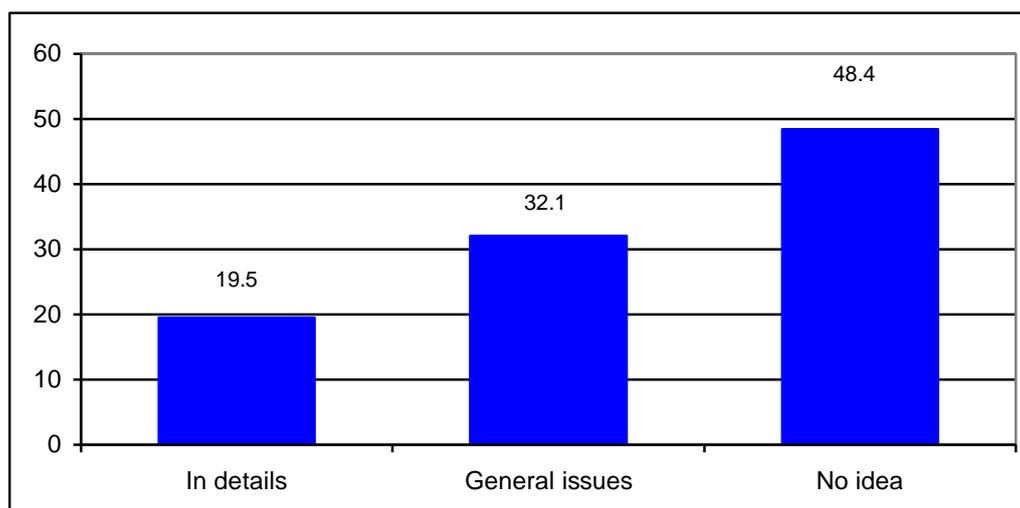
<sup>3</sup> A number of ASEAN member countries – Singapore, Indonesia, Malaysia, Myanmar, and Viet Nam – effectuated their FTAs with Korea only in June 2007. Korea's regional FTA with the Philippines came into effect only in January 2008, and its FTAs with Brunei Darussalam, Lao People's Democratic Republic, and Cambodia came into effect only in July, October, and November 2008, respectively. Thailand only acceded to the ASEAN–Korea FTA in February 2009.

of respondents identified the biggest barrier to utilising FTAs as 'Korean FTA has no substantial tariff preference or no actual benefits from FTA utilisation' and 'lack of information about the business factors of the existing FTAs or about how to utilise them'. Since the trade authorities and related agencies had tried to provide the information on FTAs via websites and various publications, this result was another surprise for the Korean trade authority. This was interpreted to imply that Korean companies wanted manuals for utilising FTAs and descriptive summaries that were suitable for entrepreneurs, rather than simply providing the texts of FTAs, which were available on the websites. The texts of FTAs are written in legal format, rather than in a descriptive style. This also highlighted the need for training courses for education about utilising FTAs and interpreting the texts of FTAs.

Of the many parts of FTAs, ROO were cited as the most burdensome element in terms of utilising FTAs. Although non-preferential ROO have been applied to Korean products regardless of FTAs, preferential ROO was a new concept for Korean companies in the early days of FTA implementation. Korean companies were not willing to change production processes to satisfy the product-specific preferential ROO of FTAs under implementation. According to the survey by Cheong and Cho (2009), only 19.5 percent of respondents replied that they understood the concept of the ROO in detail, and 32.1 percent understood the general issues surrounding ROO. About half of respondents did not know that satisfaction of the ROO is a requirement for applying for the preferential tariff margins provided for in the FTAs. Korea Customs Services (2009) reported that 89 percent of domestic companies did not know the ROO for their products, and in local areas the share of SMEs/companies that did not know was even higher.

**Figure 3.4: Awareness of Rules of Origin**

(unit: %)



Source: Cheong and Cho (2009).

#### **4. Governmental Package for Enhancing FTA Utilisation**

##### **4.1. The FTA Promotion and Policy Adjustment Authority (FTAPPAA)**

In June 2007, the government of Korea established the FTA Committee for Domestic Measures (FTA Committee hereafter). When the Korea–US FTA was supposed to be signed by both parties, the FTA Committee was organised as a governing institution for the Support Committee for the Negotiation of the Korea–US FTA, which was formed in early 2006, when Korea was about to start negotiations on the FTA. One purpose of establishing the FTA Committee was to support the utilisation of FTAs, particularly for SMEs. At the same time, trade-related governmental agencies began to provide several programmes to support FTA utilisation by SMEs.

Although the committee established several programmes to support FTA utilisation, such as providing FTA information and education for the private sector, the role of the committee shifted to publicising the Korea–US FTA to attract public support for it. One mistake made by the committee was that it exaggerated the benefits of FTA implementation. That is, rather than making it clear companies should understand how to utilise the FTA once it had been implemented, and how to satisfy the ROO for their products as specified in the FTA, the committee gave the impression that companies'

exports to partner countries would naturally increase following the implementation of FTAs. Although the government was able to gather support for the Korea–US FTA, companies did not realise the importance of strengthening their capacity and make structural adjustments to be able to benefit from FTAs.

The supporting programmes for businesses included education courses for companies and consulting workshops to explain the FTAs and provide information on FTAs, build FTA portals, and organise FTA expos in foreign countries. Although these programmes seemed to be helpful to the business sector, their contents were very poor, and many were implemented as part of efforts to improve the sentiment towards FTAs of the general public in Korea. As a result, the strengthening of companies' capacity to utilise FTAs was very limited, and a 'FTA fatigue' phenomenon emerged, referring to a perception that FTAs were useless. Some companies complained that they suffered an extra burden as a consequence of the implementation of FTAs, without receiving any economic gain, and businesses that had previously been supporters of FTA policy changed their position regarding FTAs.

#### **4.2. Evaluation of the mechanism for supporting FTA utilisation (2010)**

When it adopted a comprehensive package supporting FTA utilisation in 2010, the government of Korea set the goal of achieving a 60 percent FTA utilisation ratio over the next three years. As a first step toward achieving that goal, the government decided to review the effectiveness of existing FTA support programmes in detail, recognising that establishing a national infrastructure for utilising FTAs would be key to a successful FTA policy. Without such infrastructure, the economic gains from FTAs would be small – even though Korea implemented many FTAs with major trading partners – and the political environment for promoting FTAs would worsen in the short term. A series of trilateral meetings of trade experts, industrial representatives, and policy makers was held in first half of 2010 to check the ongoing support programmes at that time and evaluate their effectiveness. Numerous criticisms were made, including the following:

- Support programmes were designed from the perspective of governmental authorities, and failed to consider the needs of business sectors.

- The positive points of FTAs were emphasised, but the basic conditions for utilising FTAs, such as satisfaction of ROO, were ignored.
- Major portions of information on FTAs were for public advertisement for FTA promotion, to attract political support for FTA policy. That is, general information on FTAs, not useful for the business sector, was provided.
- Several governmental agencies implemented almost the same programmes with similar contents and lacking a coordinated approach, without sectoral specific contents, leading to low efficiency and waste of administrative capacity.
- The necessity of setting up a 'control tower' and providing a comprehensive package to improve the efficiency of FTA programmes was recognised. All public programmes for FTA utilisation should be completely substantiated, coordinated, and systemically managed by the FTA Committee to improve their efficiency in terms of budget spending, contents, and the satisfaction of business sectors.

#### **4.3. Major structure of Comprehensive Package for Supporting FTA Utilisation**

Based on various surveys about the problems of and institutional barriers to Korean companies' FTA utilisation, the government of Korea, led by the Ministry of Strategy and Finance (MOSF), prepared a comprehensive business support mechanism titled 'Plan for Enhancing FTA Utilization'. Governmental concerns about increasing the FTA utilisation ratio and supporting business sectors were first addressed by introducing the FTA Promotion and Policy Adjustment Authority (FTAPPAA) in June 2007. Korea assigned the FTAPPAA to the MOSF for more efficient allocation of resources across all ministries in Korea. In early 2010, Korea adjusted the main role of the FTAPPAA from dealing with domestic issues to supporting the business sector in utilising FTAs. The FTAPPAA and the MOSF, a leading ministry regarding trade and industrial policies, arranged a national package of FTA information on policy, preferential tariffs, and ROO, FTA experts, FTA consulting, local FTA assistance centres, and an FTA call centre, as summarised in Table 3.3.

**Table 3.3: Major Components of Korea's FTA Support**

	Business Demand Survey	FTA Business Information	FTA Expert, Consulting	Direct Assistance for Business	FTA System Maintenance
Major Contents	Regular and special meetings and surveys for industrial agencies, representative companies	<ul style="list-style-type: none"> <li>- FTA homepages for tariffs, ROO</li> <li>- Seminars, workshops</li> <li>- Guide books, pocket books, brochures</li> </ul>	<ul style="list-style-type: none"> <li>- Cyber-learning system on FTAs</li> <li>- FTA class in universities and graduate schools</li> <li>- Courses for FTA consultants and experts</li> </ul>	<ul style="list-style-type: none"> <li>- FTA business consulting</li> <li>- FTA call centre</li> <li>- Local FTA assistance centres</li> </ul>	<ul style="list-style-type: none"> <li>- Integrated Business ROO centre</li> <li>- Integrated FTA info centre</li> </ul>
Government Agency	FTAPPAA and national related agencies New: National FTA Utilisation Center	FTAPPAA and related agencies	FTAPPAA and related agencies, universities, business forum, academic associations	Related national agencies, customs brokers, FTAPPAA	Korea Customs Services, centre for ROO, Chamber of Commerce, KITA, etc.

Source: Author's summary.

Officials and staff of the FTAPPAA were reinforced in terms of numbers and FTA expertise in dealing with FTA business support issues early 2010. Also, the FTAPPAA was given the authority to promote all FTA assistance tools and related resources in the comprehensive package, and the National FTA Utilization Center (FTAUC) was newly organised in the FTAPPAA and regional (local) FTA assistance centres. That is, the FTAPPAA plans major policies, sets goals, and designs roadmaps on a yearly basis and the National FTAUC implements related details for achieving policy goals set by the FTAPPAA.

**Table 3.4: Major Roles of National FTAUC**

Major Role	Details for Business Assistance
Cooperation, coordination	✓ Coordination of roles on FTA assistance by ministries, agencies, and organisations (across, between)
Survey, Management	✓ FTA utilisation ratios, barriers to utilising FTAs ✓ Managing FTA business assistance programmes, etc.
FTA info	✓ Internet portals, books, brochures, booklets, etc.
Consulting	✓ Consulting on tariffs, ROO, overseas marketing by experts
Education, training	✓ Cyber-learning system on FTA info ✓ FTA class in universities and graduate schools ✓ Courses for FTA consultants and experts
Seminar, workshop	✓ Various events for educating business sector (national, local, FTA partner countries)

Source: Author's summary.

#### **4.4. Examples of Comprehensive Package for Supporting FTA Utilisation**

One of the programmes initiated by the FTAUC was to provide FTA consulting to approximately 10,000 companies over four years starting in 2010. At this time, consulting was considered to be the most efficient means of enhancing FTA utilisation. Financial support was given to trade agencies such as the Small & Medium Business Corporation (SBC), Korea International Trade Association (KITA), and Korea Trade-Investment Promotion Agency (KOTRA) to cover their FTA business consulting costs. The companies that received FTA consulting were targeted to be those that trade with FTA partners. As of 2009, there were about 80,000 trading SMEs, and 37,000 companies were trading with Korea's FTA partner countries. The FTAUC has reached most of the FTA consulting targets so far.

**Table 3.5: Targets for Providing FTA Business Consulting**

	‘10	‘11	‘12	‘13	Total
No. of SMEs	600	2,000	3,000	5,000	10,600

Source: Internal report prepared by Ministry of Strategy and Finance (MOSF).

FTAPPAA opened the FTA Business Portal, which provides important information for FTA business utilisation in 2011. FTA information was organised in such a way that it can be updated on a daily basis, and the portal has been upgraded several times to make the format more user-friendly. The site was designed to provide a single-window portal, consolidating the various FTA information provided by trade ministries and agencies. Recently, areas such as FTA business models and success cases of FTA utilisation were added into the FTA portal, and more systematic analysis mechanisms for searching tariffs and product-specific ROO were installed into the portal.

**Figure 3.5: FTA Business Portal by the FTAPPAA**

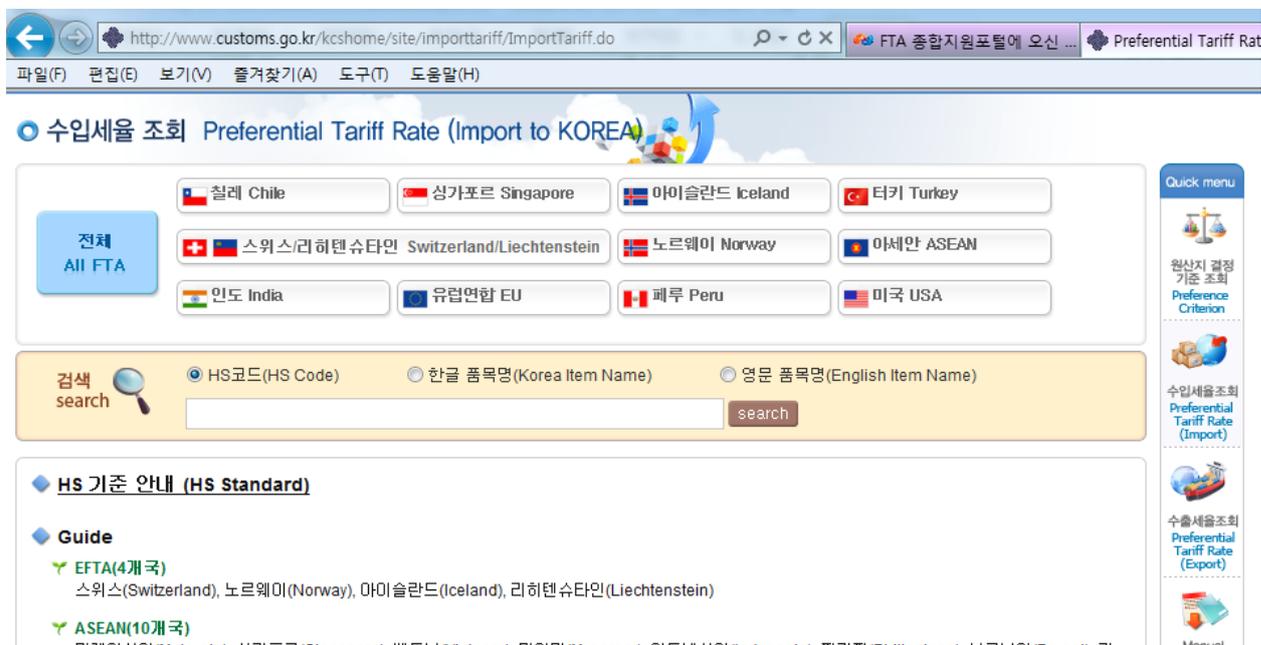


Source: [www.ftahub.go.kr](http://www.ftahub.go.kr)

Since preferential tariff rates and product-specific ROO are basic elements in utilising FTAs, Korea Customs Service installed integrated portals on preferential tariff

rates and FTA ROO. The FTAPPAA linked these portals in its portal for Korean SMEs. FTA tariffs and related ROO can be viewed by HS digit and by FTA partner. This system allows Korean companies to check relevant information without referring to the Appendix or Annex of FTA agreements. FTAPPAA also offered a series of seminars and workshops for businesses regarding this system.

Figure 3.6: Integrated Portal for Preferential Tariff Rates under Korean FTAs



Source: <http://www.customs.go.kr/>

Figure 3.7: Integrated Portal for FTA Rules of Origin



Source: <http://www.customs.go.kr/>

The FTA call centre was established in June 2014, and provides consulting services to callers seven days a week. This centre was not easy to establish and it took two years to arrange professional FTA consultants. It received more than 1,000 calls per month in the five months after it opened. Immediate consulting is provided based on the questions raised by callers, and then follow-up on-site consulting is provided for the companies in question.

Figure 3.8: FTA Call Centre

<p style="text-align: center;"><b>FTA 활용, 무엇이든 물어보세요!</b></p>  <p style="text-align: center;"><b>전국 어디서나 FTA 콜센터 1 3 8 0</b></p> <p style="font-size: small; text-align: center;">FTA 콜센터 13800시는 중소기업의 FTA 활용 능력 향상과 경쟁력 강화를 위하여 전문기관 컨설팅, 정보제공, 교육 등의 다양한 서비스를 보다 빠르고 보다 편리하게 제공하고 있습니다.</p>	<p>Ask whatever on FTA utilisation</p>  <p>FTA call centre Number 1380 anywhere in Korea</p>
-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------	---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------

Source: [www.ftahub.go.kr](http://www.ftahub.go.kr)

Various issues related to satisfying ROO have been identified as barriers to FTA utilisation in most of the surveys since establishment of the FTAPPAA. That is, satisfying ROO requires that many elements of a company are reviewed, such as cost structure, production procedure and specification, sourcing structure, and account books. This process may necessarily involve accessing classified business information including technology and unit cost of products, which made most companies unwilling to receive consulting for FTA utilisation. Although professional consulting companies mention their obligation to handle their clients' information confidentially, it was difficult for Korean SMEs to trust the consulting companies and consultants. Therefore, the FTAPPAA had self-test software developed to enable companies to determine whether they could satisfy ROO without providing internal information on production and costs. As companies practiced testing ROO, they gradually came to trust the consulting companies and consultants.

## 5. Recent FTA Utilisation

In spite of the delayed recovery of the global economy and the slump in global trade volumes, Korea's trade with most of its FTA partners has continuously expanded. FTA utilisation ratios are recorded to be higher than 60 percent in Korea's bilateral trade with many of its FTA partners, which was the goal that had been set by the government of Korea in 2010. Korea recorded FTA utilisation ratios above 70 percent for the Korea–US FTA and the EU–Korea FTA, whereas the utilisation ratios for the FTAs with ASEAN and India remained low despite national efforts to improve FTA utilisation ratios.<sup>4</sup>

Although the importance of government support for businesses in utilising FTAs should be recognised, the quality of FTAs in terms of improving market access is a key determinant for the extent of FTA utilisation. That is, one of the major reasons for the slow increase in FTA utilisation in FTAs with ASEAN and India is that Korean businesses do not consider tariff margins to be high enough to pay the cost of allocating personal and physical resources. But utilisation ratios for these FTAs have slowly increased due to various forms of governmental support for businesses. As of 2013, the FTA utilisation ratio for the bilateral FTA with ASEAN was 38 percent and that with India 43 percent.

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<sup>4</sup> FTA utilisation ratio is measured by dividing exports/imports using FTA tariff preference margins with total exports/imports into/from FTA partner country. Denominators can be discretely chosen total exports/imports depending on the consideration of tariff preference margins.

**Table 3.6: Trend of FTA Utilisation Ratios**

(unit: percent)

FTA partner	As of End-2012		As of November 2013	
	Exports	Imports	Exports	Imports
Chile	75.2	97.9	78.4	98.3
EFTA	79.8	61.9	80.5	42.0
ASEAN	37.7	73.8	38.5	80.1
India	36.2	52.7	43.0	62.3
EU	81.4	66.8	80.9	67.6
Peru	78.0	92.0	92.0	98.4
US	68.9	61.0	76.4	67.3
Simple average	65.31	72.30	69.96	73.71

Source: Korea Customs Service (2013) 'FTA Utilisation Ratios for Korea' Trade'.

Based on the FTA utilisation performance summarised in Table 3.5, Korea's FTA support policy can be considered a success in terms of achieving policy goals and improving FTA utilisation ratios. When the government of Korea was considering a national FTA support policy in 2010, the average FTA utilisation ratio was about 20 percent, and as low as 4–5 percent in exports for some FTAs. The original goal was to achieve a 40 percent FTA utilisation ratio in 2012, a 60 percent FTA utilisation ratio in 2013, and to increase those to about 80 percent, which is as high as the FTA utilisation ratio in advanced economies such as the EU and the US.

Several observations from Korea's FTA support experience to raise FTA utilisation merit highlighting. One is that the FTA utilisation ratios in Korea's exports increased substantially during the last three years of the FTA support policy, although they were lower than for imports. Utilising FTAs for importing goods from FTA partners is relatively easy, compared with exporting, since exporting requires marketing by FTA partners. Another observation is the gradual improvement of Korean SMEs' FTA utilisation ratios, although those ratios remained lower than the ratios achieved by large companies. The initial motivation behind Korea's FTA support policy was poor FTA utilisation by SMEs. For the EU–Korea FTA, large companies' FTA utilisation ratio was 84.3 percent and that for SMEs 76.4 percent in 2013 (in terms of value). And 69.2 percent of Korean SMEs' exports used FTA tariff preference provided by the Korea–US FTA.

FTAs are widely utilised in most industrial sectors, and there has been progress in sectoral FTA utilisation in 2013. A utilisation ratio above 80 percent has been recorded in several sectors, such as mining, machinery, and the plastic/rubber industry. And a substantial increase in Korea–US FTA utilisation was achieved in mining, home items, electrical goods, and steel products from 2012 to 2013.

**Table 3.7: FTA Utilisation Ratio by Industry (Korea–US FTA)**

(unit: %)

<b>Korea–US FTA</b>				
	As of the end of 2012	As of November 2013	Yearly change (%)	
Mining	66.4	80.2	13.8	
Machinery	74.4	81.1	6.7	
Agriculture	45.4	52.1	6.8	
Household goods	52.5	66.9	14.4	
Textiles	69.6	71.5	2.0	
Electrical goods	49.4	61.1	11.7	
Steel, products	68.0	78.4	10.4	
Plastic, rubber	82.9	83.2	0.3	
Chemicals	66.0	70.7	4.6	
Other goods	66.0	68.4	2.4	
<b>EU–Korea FTA</b>				
Mining	69.3	53.4	Δ15.9	
Machinery	88.2	89.6	1.5	
Agriculture	47.4	52.1	4.7	
Household goods	67.8	84.9	17.1	
Textiles	82.7	86.5	3.8	
Electrical goods	71.3	77.0	5.7	
Steel products	67.4	72.3	4.9	
Plastic, rubber	88.4	90.6	2.2	
Chemicals	78.7	74.3	Δ4.3	
Other goods	56.9	77.9	21.0	

Source: Korea Customs Services (2013).

Finally, the FTA utilisation ratio of small exporting companies (in terms of export value) remained low, although the overall utilisation ratio increased substantially. However, as the scale of exports increases, the FTA utilisation ratio rises. This seems reasonable, in that large companies have a better internal infrastructure for utilising FTAs with higher incentives. Table 3.8 shows that only 4,340 small companies applied preferential tariffs out of 28,762 companies that had exports worth less than 0.1 million

dollars a year. The FTA utilisation ratio for these companies was about 15 percent. This is a significant contrast with the 64 percent utilisation ratio for companies with exports of over one million dollars. This implies that the government of Korea needs to strengthen FTA utilisation for small companies.

**Table 3.8: SMEs with FTA Utilisation and Non-utilisation by Scale of Exports**

(unit: number of SMEs)

		Scale of Exports (million \$)					Total
		(A) <0.1	0.1M< (B) <0.5	0.5< (C) < 1	(D) > 1	(B+C+D) >0.1	
Number of Companies	No FTA utilisation	24,422	6,702	1,799	2,637	11,138	35,560
	FTA utilisation (F)	4,340	3,812	1,700	4,656	10,168	14,508
	Total (T)	28,762	10,514	3,499	7,293	21,306	50,068
	Ratio (F/T, percent)	15.09	36.26	48.59	63.84	47.72	28.98

Source: Calculated based on data from KCS.

## 6. Conclusion and Implications

Although countries promote FTAs to achieve various policy goals, achieving economic gains is one of the most important. FTAs are concluded by governments, but private companies utilise FTAs to realise economic gains. When companies make decisions related to FTA utilisation, they will compare the economic incentives with the various costs related to satisfying ROO and collecting information on FTA tariffs and ROO. It is important the perception of CEOs of SMEs on FTA utilisation is changed. Unlike large companies, SMEs do not have enough staff to handle FTA business, and lack the professional expertise in trade practice and business activities. Unless CEOs have a strong intention to utilise FTAs, staff of SMEs are unlikely to allocate their time to explore the possibility of new businesses based on FTA contents.

Due to substantial progress in building institutional infrastructure as a result of the Korean government's active policy on FTA utilisation assistance, FTA utilisation ratios are now as high as those of advanced countries. For more companies to use the FTAs,

companies need to comprehend the contents of the FTAs and be inclined to use them. FTA utilisation is possible when exporters (manufacturers) issue the certificate of ROO and importers submit it to the customs authority of the importing country. Otherwise, importers face a serious problem regarding the origin verification by the customs authority. This implies that exporters and importers must share the intention and information related to FTA utilisation.

Several policy implications can be drawn from Korea's experience in assisting businesses with FTA utilisation. First of all, one of the most urgent and important tasks in assisting FTA utilisation is to identify the barriers that prevent companies from utilising FTAs. Critical barriers may differ from country to country. Based on the significance of the barriers and the possibility for improvement through governmental actions, the government should make a road map for building infrastructure and assisting businesses in utilising FTAs.

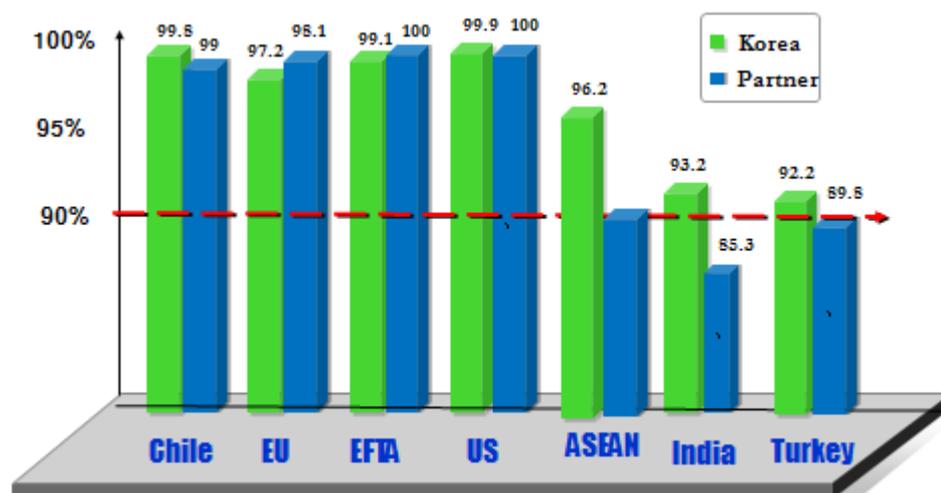
Second, coordination amongst national agencies is critical in increasing the efficiency of the infrastructure assisting FTA utilisation. In the absence of such coordination, several agencies tend to provide similar services with poor contents to business sectors. Korea had this experience in 2008–2009, and companies evaluated this to be 'not useful' in designing business plans for utilising FTAs.

Third, governments should promote FTAs with large economies, which can be expected to bring high overall economic gains. This will give businesses large incentives to look for opportunities to utilise FTAs. In this regard, special considerations must be given to small exporting companies that lack the staff and expertise for international trading and marketing. Assistance in marketing, branding, and logistics will be useful for small companies in utilising FTAs. In the case of Korea, there is room for improving the FTA utilisation ratio for small companies, and the government must make this a priority for domestic FTA policy.

Fourth, authorities of trade and industry should understand the importance of the quality of FTAs. When tariffs are eliminated in a short period of time and the agreement is comprehensive in its coverage, companies will have an incentive to utilise the FTA in their business activities. As seen in Figure 3.9, Korea achieved 97–100 percent ratios for tariff elimination in its many FTAs, but the Korea–Turkey FTA has 92.2 percent of tariff elimination for Korea and 89.5 percent for Turkey. This becomes a serious problem for

businessmen, since the EU–Korea FTA offers more favourable treatment than the Korea–Turkey FTA. Both countries need to upgrade existing market access in the FTA in addition to finishing their negotiations on services and investment to provide greater incentives for FTA utilisation by businesses and to have a more comprehensive FTA.

**Figure 3.9: Tariff Elimination Ratios in Korea's Major FTAs**



Source: Authors' calculation based on the tariff schedules of Korea's FTAs.

Fifth, FTA member countries should take advantage of various levels of committees institutionalised in FTAs. Most FTAs install trade ministers' meetings, FTA committees, and several subcommittees for customs clearance, ROO, Sanitary and Phytosanitary Measures (SPS), and Technical Barriers to Trade (TBT). Even though FTAs are implemented, many non-tariff barriers (NTBs) continue to distort bilateral trade. Depending on the position of member countries, these NTBs could be eased and/or eliminated. Complicated ROO are amongst the most serious hurdles in utilising FTAs, hence member countries should discuss the simplification of ROO.

Last, FTA member countries need to co-operate on implementing FTAs properly and providing information related to FTA utilisation. FTAs establish several committees to facilitate the implementation of FTAs. Since FTA implementation means the adoption of common trade and economic systems defined in the agreement, problems due to institutional differences between member countries arise, which in many cases become

barriers to FTA utilisation. Also, member countries should discuss the tasks set in the agreements such as the acceleration of tariff elimination. Harmonisation of FTAs should be pursued. As the number of FTAs increases, the differences across FTAs become an issue for trade policy makers. From the viewpoint of business sectors, the contents should be harmonised across FTAs, and should be upgraded for easy utilisation of FTAs.

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