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TRADE AND ECONOMIC RELATIONS BETWEEN THE EUROPEAN UNION AND THE REPUBLIC OF KOREA

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Abstract

The objective of the research is to outline the main trends in the economic relations between the European Union and the Republic of Korea. The research methods used in the study involve retrospective, comparative and content analysis, as well as table presentation of empirical data for the relations between the two countries. The paper is of conceptual character. The thesis of the research is that the Free trade agreement (FTA) between the two countries is beneficial to both parties but changes in trade flows trends are difficult to attribute clearly, as other macroeconomic factors are also in place. The results of the research involve several major findings. The slow GDP growth of the EU and the depreciation of the euro against the South Korean won over the past five years are obvious. Korea's exporters have a higher rate of utilization of preferences than European companies (there are also large differences between the EU Member States). Two key reasons are at the heart of this observation – first, Korea's exporters, which are often large export family conglomerates, are experienced and resourceful when it comes to administrative customs procedures, while the EU industry is more fragmented. Second, the "direct transport clause" of the agreement does not allow some EU exporters to use their regional centers in Asia to benefit from FTA preferences. The conclusion of the research is that despite the overall positive assessment of the bilateral economic relations, specific concerns remain on both sides.

Key words: Republic of Korea – European Union, economic relations, ROK-EU FTA

JEL: F13, F15

Introduction

Identified as one of the Four Asian Tigers, the Republic of Korea, along with Singapore, Taiwan and Hong Kong, has been depicted as an example of a *developmental state.* In the model of developmental state, the state has an influence on macro-economic policy and develops strategies for the private sector development.

Recent academic research has attributed significant importance to the effect of the state and state-society relations on economic development (Boneva, 2014) and many of them give the Republic of Korea (ROK) as an example (Lin,

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Chang, 2009). The steady economic growth of the country is exemplified by its impressive increase in GDP per capita. The country has grown in influence in the international limelight, due to its export-oriented economic growth, setting numerous trade partners. Since the last two decades, trade in ROK has increased from 50% to 90% of its GDP, with the trade threshold surpassing 1 trillion USD in 2011. Consequently, Korea became one of EU's ten strategic partners. Although the definition of a strategic partnership remained unclear (Boneva, 2013), strategic partnerships are currently a conceptual framework for the EU's relations with the leading powers and take place on an international level, characterised by new forms of bilateral network governance.

Economic relations between the EU and the Republic of Korea

The EU and Korea are strategic partners which marked the 55-th anniversary of the establishment of diplomatic relations in 2018. Bilateral relations are governed by three key agreements, namely the Political Framework Agreement, the Free Trade Agreement and the Framework Agreement for Participation. Numerous bilateral consultations are held annually.

The EU-Korea Free Trade Agreement (EU-Korea Free Trade Agreement, 2011) is the first of a new generation of EU Free Trade Agreements launched in 2007 as part of the Global Europe initiative, which called on the EU to renew its commitment in Asia. It was the first EU agreement concluded in a wave of deep and comprehensive free trade agreements, which Brussels started after the abolition of the self-imposed moratorium on such agreements in favour of the multilateral circle at the end of the 20th century. The European Union has strong economic and political relations with the Republic of Korea. Education, science and technology as well as climate change are important areas of cooperation between the two parties. As Korea is one of the 10 EU strategic partners (four in Asia – Korea, China, Japan and India), the country is of high importance to the EU, which regards Korea as a country with political and economic influence, capable of contributing to the resolution of international crises and of addressing the key challenges of the 21st century.

The agreement is part of a new generation of FTAs with a broad scope, incorporating the following aspects: liberalisation of trade in goods and services (telecommunications, legal, financial and maritime and environmental services), investment in the industrial sector and services, protection of intellectual property, competition, public procurement, transparency of the regulatory framework and sustainable development. This was the most ambitious trade deal ever made by the EU by then.

A number of bilateral bodies have been set up that come with the signature of the FTA to ensure smooth adjustments and make improvements to the text when such needs arise. The Ministerial Trade Committee meets annually to discuss and review the overall implementation of the Agreement. In addition, six specialised committees (focused on trade in goods; sanitary and phytosanitary measures (SPS); customs, services, establishment and e-commerce; trade and sustainable development; and the Korean Peninsula outward processing zones), seven working groups (focused on motor vehicles and parts; pharmaceuticals and medical devices; chemicals; cooperation in the field of trade in medicines; agreements on mutual recognition of services; government procurement and geographical indications); three dialogues (focused on intellectual property; cultural cooperation; electrical and electronic products); as well as a civil society forum, are established to address issues in their respective areas of responsibility (Lim and Lee, 2018).

The agreement is a comprehensive pact covering a wide range of economic activities. It includes fifteen chapters, annexes, three minutes and four understandings. Import duties have been abolished on almost all products and there is widespread liberalization in the services sector covering all types of supplies. Five years after the agreement was signed, 98.7% of customs duties on trade were eliminated, with some exceptions for agricultural products (Flew, 2016). The agreement also includes investment provisions and covers important areas such as the protection of intellectual property rights (including geographical indications), public procurement, competition rules, regulatory transparency and sustainable development. Specific commitments have been made to remove and prevent the emergence of non-tariff barriers in critical sectors such as automobiles, pharmaceuticals, medical devices and electronics. Lastly, a Protocol on cultural cooperation based on the commitment of both parties to promote cultural diversity in accordance with the UNESCO Convention is included.

Trade between the EU and the Republic of Korea

Among foreign investors in the ROK, the EU is the largest investor. EU foreign direct investment in the ROK accounts for more than one third of total FDI in Korea. In addition, Korean investments in the EU increased by 19% between 2014 and 2015, representing totally around 20.9 billion EUR.

The EU Gateway to Korea (https://www.eu-gateway.eu/korea) is an EU-funded initiative that helps companies in the 28 EU Member States establish long-term business partnerships in Korea. During the period 2016 – 2020, the EU aims to organise up to 20 EU business mission portals in Korea. They operate in certain industrial sectors where there is potential for enhanced cooperation between European and Korean companies with a budget of 15.4 million EUR. The European Portal is an initiative funded by the European Union that helps European companies establish long-term business cooperation in Asia. Selected

European companies are eligible to participate in a one-week, sector-specific business mission in Korea, Southeast Asia, China and Japan. Companies benefit from a range of business support services, which include coaching, logistics and financial support.

Trade between the EU and Korea is dominated by electrical/non-electrical machinery and equipment, transport equipment, optical and photo equipment as well as plastics. Trade in services also boomed with a stock of 19 billion EUR in 2014.

On the other hand, Korea promotes trade and investment in Korea through its government organisation KOTRA (Korea Trade-Investment Promotion Agency), established in 1962 as a national trade promotion organisation (http://www.kotra.or.kr). Its main purpose is to promote SME export, give trade services, government-to-government export foreign investment in Korea, as well as B2B matchmaking.

In addition, KOTRA operates the national investment promotion agency, called Invest Korea, which supports foreign investors with an expanded provision of services. In the age of e commerce since the early 2000's, the organisation developed an interactive portal site of Invest Korea Online and BuyKorea, in 2003 and 2004 respectively.

To bolster young talents, a professional learning centre for international business was launched, called KOTRA Academy, with the intention of fostering the investment infrastructure and the national trade. As of late 2018, there are a total of 126 overseas liaison offices in over 86 countries for trade-related information and promotion, with more than 1000 employees. Ultimately, KOTRA has prospects in placing Korea as a main economic and business hub of East Asia (Hong, 2014).

At the same time, the Korea International Trade Association (KITA), established in 1946, is the largest business organisation in Korea with over 70 000 companies as members. KITA (http://www.kita.org/about/kitaProfile.do) provides multiple services in trade, namely initiating trade strategies and proposals for policy improvement to the government, bolstering trade professionals, creating trade infrastructure for the private sector, providing research assistance to SMEs for export, organising world-class exhibitions. There are over 13 domestic offices and 11 branches in major cities around the world. The organisation has delivered a total of 1 trillion USD in trade volume towards Korea.

Bilateral relations between the EU and Korea are based on a material and ideological basis. Both parties have the necessary economic and human resources to put their agreements into practice. They can cooperate at the bilateral level as well as within multilateral governance structures. In addition, both sides share the values of democracy, human rights and the rule of law. They also share their confidence in the market economy. In other words, relations between the EU and Korea go beyond economic and political interests and are based on shared values.

The Free trade agreement between the EU and the ROK was signed in 2010, and in 2011 it entered into force, in 2015 it was formally ratified. It represents the economic pillar of Korea-EU relations and helps to develop bilateral trade in goods, with trade exceeding 66 billion EUR in 2010, reaching 94 billion EUR in 2017, and in 2018, trade in goods exceeded € 120 billion. Five years after the entry into force of the agreement, 98.7% of the duties were eliminated. The agreement includes rules relating to trade, intellectual property and public procurement.

South Korea is the EU's eighth largest export partner and the EU is South Korea's third largest partner in the same field. Most of the import duties were abolished in July 2011, with the two countries committed to abolishing 98.7% of the duties within five years. On July 1, 2016 the import duties on all goods were abolished except for a limited number of agricultural products (Ministry of Foreign Affairs of the Republic of Kore, 2018). Trade between the EU and Korea increased by 45% between 2011 and 2017 and EU exports increased by 53%. In addition, the EU and South Korea declare their joint commitment to fight protectionism and to support the multilateral trading system, which is at the heart of the WTO, with the two countries fully committed to reforming the institution.

Trade in goods

Total exports of goods from the European Union (EU-28) to the Republic of Korea amounted to 50.1 billion EUR in 2017. Germany ranks first with 35.9%, followed by the UK (13.2%) and the Netherlands (12.2%). European exports (EU-28) to the Republic of Korea increased by 13.6% (+ 6.0 billion EUR) in 2017. German exports of goods to Korea increased by 3.7% (+ 634.3 million EUR) in 2017, while those of the UK and the Netherlands increased by 24.7% (+ 1.3 billion EUR) and 59.4% (+ 2.3 billion EUR) respectively (Kingdom of Belgium, 2009).

The main countries to which the EU is exporting to are: China (20%), the USA (14%), Russia (7%), Switzerland (6%), Turkey (4%), Japan (3.7%), Norway (3.5%) and Korea (2.8%). The EU is Korea's third largest export market (Ministry of Trade of the Republic of Korea, 2008) with a market share of 9.4%, after China (24.8%) and the US (12%). The main exported products are transport facilities (18.5%), electronic devices (18%), machinery (14%), ships (10%), pharmaceuticals (7%), steel (6%), these goods occupy 80 % of total exports from Korea to the EU.

Korea, on the other hand, is the seventh largest EU export destination, accounting for 2.6% of the total EU exports. The main EU export destinations are the USA (19.7%), China (10.4%), Switzerland (7.9%), Russia (4.6%), Turkey (3.2%), Korea (2.6%), etc.

Table 1: South Korea Trade in Goods with Main Trade Partners, million EUR

	Total Korea Trade with	Million EUR	Share %	Korea Imports from	Million EUR	Share %	Korea Exports to	Million EUR	Share %
	World	814, 788	100	World	366, 819	100	World	447,969	100
1	China	190, 996	23.4	China	78, 572	21.4	China	112, 424	25.1
2	USA	99, 506	12.2	EU28	46, 848	12.8	USA	60, 307	13.5
3	EU28	88, 785	10.9	Japan	42, 878	11.7	EU28	41, 937	9.4

Source: Eurostat

If we look at the regulations on imports from third countries outside the EU by 2018, 86 import regulatory measures are in place, including 73 anti-dumping tariffs in 2018, 12 countervailing duties and 1 provisional guarantee on steel. Of the total 86 cases, 72% or 62 cases relate to steel, metal and chemical goods (41 cases to steel and metal products, 21 cases to chemical products) and 75% or 65 cases to China.

Regarding EU regulation of Korea's imports into the EU, as of 2018, the EU imposes a total of 6 temporary restrictions on imports from Korea, 5 of which are anti-dumping regulations and one is a safeguard for steel. From 2013 to 2016, the EU's long-standing trade deficit with Korea becomes surplus. In 2017, Korea again receives a trade surplus due to a significant 20% increase in EU exports in the context of economic recovery in the European Union.

Table 2: Exports of goods from Korea to the EU, in USD

		2015	2016	2017	2016/2017 increase (%)
	Total export of goods	46.90 bn	45.971 bn.	58.340 bn	26.9
1	Transport facilities other than railway lines	7.876 bn	8.588 bn.	10,776 bn	25.5
2	Electronic devices	9.918 bn	8.727 bn.	10.428 bn	19.5
3	Machines	6.452 bn	6.631 bn.	7.975 bn	20.3
4	Ships	4.636 bn	3.472 bn.	5.788 bn	66.7
5	Pharmaceutical products	536 mil.	832 mil.	4.028 bn	384

		2015	2016	2017	2016/2017 increase (%)
6	Plastic	2.866 bn	3.280 bn.	3.605 bn	9.9
7	Steel	2.765 bn	3.057 bn.	3.833 bn	25.4
8	Optical, measuring lenses and more.	2.591 bn	2.044 bn.	1.791 bn	-12.4
9	Organic chemical products	1.418 bn	1.302 bn.	1.684 bn	29.3

Source: Ministry of Trade of the ROK

According to Figure 2 in 2017, bilateral trade between the EU and South Korea continued to be concentrated in several sectors, namely the exchange of industrial goods. With the Standard International Trade Classification (SITC) classified, the most important EU imports in 2017 are machinery and transport equipment (63%, especially road vehicles, electrical machinery, apparatus and appliances), chemicals (14%) and industrial goods (classified mainly by materials) (13%). Of the EU exports, the most important SITC sections are machinery and transport equipment (50%; in particular road vehicles, specialised machinery for certain industries and general industrial machinery and equipment), chemicals (15%) and miscellaneous articles (13%).

In 2017, with regard to South Korea exports to the EU, there is a significant increase in transport equipment (cars with a cylinder capacity of no more than 1000 cubic centimetres transport of people and goods).

As indicated, total EU imports from Korea have increased by 21% since 2010. This increase is particularly important in the areas of chemical products (260%), beverages and tobacco (197%), animal and vegetable oils, fats and waxes (151%) and food and live animals (135%). Imports are down compared to 2010 in miscellaneous items (-24%) and goods and transactions (-19%). Total EU exports to Korea increase by 70% between 2010 and 2017. Growth is particularly important for mineral fuels (1291%), food and live animals (138%) and various products (112%). The only drop in exports was observed in the field of crude materials (excluding fuels) by 12%.

The total imports of machinery and road vehicles into the EU (Section 7 of the Standard Classification for International Trade, or SITC) have increased by 4% since 2010 onwards. The most important imports into the EU are electrical machinery, appliances (22%) and road vehicles (30%). During the same period, EU exports increased significantly (65%), yet the EU maintained a negative trade balance in this respect. Part of the explanation lies in the fact that in many sectors the EU has a more open market than Korea before concluding the agreement. EU exports are mainly related to machinery specialised in certain sectors (18%); other industrial machinery and parts (15%), electrical machinery, apparatus and appliances (12%) and road vehicles (34%). EU imports of road vehicles (69%) are passenger cars (excluding buses) and 30% are vehicle parts and accessories. EU exports of the same section (77%) are passenger cars (excluding buses), 12% are vehicle parts and accessories, and 7% are special purpose motor vehicles and motor vehicles.

The automobile sector has been an important part of EU-Korea trade relations for many years. Korea is the fifth largest passenger car manufacturer in the world and the third largest source of imports to the EU in this respect after Turkey and Japan. The EU is a major global player and is second on the list of global car manufacturers with Germany, Spain, France, the United Kingdom and the Czech Republic as key players (ACEA, 2019). Korea is the sixth largest export market for passenger cars in the EU (in units). Although the EU market for passenger cars has been declining since 2010 overall, Korea's car imports into the EU are increasing every year. Discussions on access to the motor vehicle market are repeated in the relevant FTA Working Party and the Trade Committee. They are of great importance to the European automotive industry. Issues related to regulation, technical standards and environmental standards are particularly important. The European Commission also acknowledged that tackling other non-tariff barriers in the automotive sector remains a challenge.

At the time of the conclusion of the agreement, the EU feared that Korea would register large commercial profits in the textile sector at the expense of EU producers. Although the EU maintains a trade deficit in the textile sector, the deficit has narrowed significantly over time. In 2017, textile imports accounted for about 2.5% of total imports from Korea. Exports account for 2.4% of total exports of goods from the EU to the Republic of Korea.

Electronics and telecommunications account for 9.5% of total EU goods imports from Korea and 3% of total EU goods exports (Eurostat, 2019). Imports of electronic integrated circuits (47%) and telephones (20%) are particularly significant. EU exports are dominated by electronic integrated circuits (43%), electronic boards and consoles (15%) and telecommunications equipment (14%). Overall, EU imports from this industry have decreased by 22% since 2010, while exports have increased by 33%. However, in 2017 the EU maintained a small trade deficit.

Trade in services

Although trade in goods is crucial to EU-Korea trade relations, trade in services accounts for around 15 – 20% of the total bilateral trade over the last five years. The services sector is the fastest growing sector of the world economy as a result of the development of information and communication technologies. The services sector contributes more to economic growth and job creation in the EU than any other sector. It represents about 3/4 of the EU's gross domestic product. In addition, more than 3/4 of EU jobs are in the services sector. The EU is the world leader with a surplus of over 130 billion EUR in 2016. Imports into the EU are dominated by the transport sector and business services ('other business services'). In regards to the EU exports, transportation services (especially maritime transportation), business services and intellectual property fees are predominant. In the trade in services, there is a pattern of growth similar to that of the trade in goods (Boneva, 2014). Imports into the EU have increased by 38% and exports increased by 70%. The EU notes a significant surplus in trade in services with Korea. The FTA between the EU and South Korea has a positive impact on trade in services, as total bilateral trade in services has increased by about 46% over the last six years.

The impact of the FTA leads to increased trade in goods, services and investment between the EU and Korea, thereby increasing the demand for specialised cross-border and ancillary services.

The growth of exports of services in both directions shows that specialisation is being carried out in the services sector, leading to economic benefits. The innovations is an important element in the services for both countries.

Despite the overall positive trend, in 2016 there was a stalemate in trade in services between both parties. Exports of European Union services to South Korea decreased by 3.7%, from 13.06 billion EUR to 12.57 billion EUR while imports fell from 6.82 billion EUR to 6.6 billion EUR.

As a result, the EU's surplus in trade in services with South Korea dropped by 4%, from 6.23 billion EUR in 2015 to 5.98 billion EUR in 2016.

Table 3: EU-South Korea trade in services by sector 2013 – 2016, million EUR

	2013		**2014**		**2015**		**2016**	
	Imports	**Exports**	**Imports**	**Exports**	**Imports**	**Exports**	**Imports**	**Exports**
Total	5,703	10,787	6,286	11,888	6,829	13,060	6,600	12,587
Manufacturing services	60	357	108	272	64	306	77	213
Maintenance and services	113	104	145	97	178	153	190	171
Transport	2,427	3,043	2,282	3,022	2,320	3,025	2,244	2,628
Travel	241	855	270	1,071	277	1,270	301	1,255
Construction	54	118	93	203	68	302	63	418
Insurance and pensions services	102	416	70	103	81	150	106	296

	2013		2014		2015		2016	
	Imports	Exports	Imports	Exports	Imports	Exports	Imports	Exports
Financial services	243	440	250	432	247	552	234	504
Intellectual property	552	1,884	402	1,897	870	2,264	446	2,242
Telecommuni-cations, computer, etc.	391	720	357	787	214	980	241	995
Other business services	1,415	2,504	2,263	3,537	2,472	3,3374	2,592	2,891
Personal, cultural and recreational	9	35	12	42	11	291	10	441
Total	87	41	31	44	11	47	78	46
Services not allocated	8	269	1	281	15	362	7	385

Source: Eurostat

Market conditions are expected to continue to improve over the coming years thanks to liberalisation, deregulation and re-regulation processes as Korea and the EU move towards gradual liberalisation to stimulate competition in the services sector. EU exports to South Korea are highly concentrated in several sectors, in particular: business services (23%), maritime transport (21%) and royalty and license fees (18%). Korea's exports to the EU also focus on business services (39%) and maritime transport (34%).

The last element of the economic relations between the EU and Korea is foreign direct investment (FDI). The EU is the largest source of FDI in South Korea (32% of total FDI in South Korea), followed by Japan (26%) and the United States (19%). According to Eurostat, foreign direct investment stocks in South Korea reached EUR 50 billion in 2016, 12% up compared to the previous year. FDI in South Korea also increased in 2016, an increase of 3% compared to the previous year, reaching 20 billion EUR.

In 2016 among EU Member States, the Netherlands was the largest investor in South Korea, owning about 37% of the total EU foreign direct investment in South Korea, followed by Germany (over 16%) and the United Kingdom (15%). On the other hand, Germany is Korea's leading FDI destination in the EU (about 25% of the total stock), followed by Slovakia (15%) and the Czech Republic (12%).

Table 4: Foreign Direct Investment to Korea coming from the EU and ROK-EU, million EUR

Year	Million EUR				Year-on-year growth %			
	Stocks		Flow		Stocks		Flows	
	Inward	Outward	Inward	Outward	Inward	Outward	Inward	Outward
2013	15,517	32,097	1,853	873	-8	-9	-57	
2014	17,928	42,936	4,326	7,766	16	34	133	790
2015	18,666	44,853	1,811	- 4,287	4	4	-58	
2016	19,232	50,339	989	3,426	3	12	-45	

Source: Eurostat

The EU-Korea FTA has been the centre of trade and economic relations between the two countries since 2011 onwards. The agreement was signed in October 2010 in Brussels. It was provisionally applied from July 2011 onwards and officially entered into force in December 2015, after ratification by Korea and all EU Member States. This contrasts with the much longer process of ratification of the FTA between Korea and the United States. The FTA has introduced a system of gradual liberalisation and removal of import duties to allow domestic producers on both sides to adapt gradually. This gradual liberalisation scheme ends in June 2016 and there is no difference between fully, partially or non-liberalised products (EU-Korea F.T.A., 2011).

The EU-Korea FTA is the first of a new generation of EU free trade agreements launched in 2007 as part of the Global Europe initiative, which called for the EU to renew its commitment to Asia. It was the first EU agreement to be concluded amid a wave of deep and comprehensive Free trade agreements, which Brussels launched after the abolition of a self-imposed moratorium on such agreements in favour of multilateralism at the end of the 20th century. At the time of its conclusion, it was also the most ambitious trade agreement agreed by the EU. For Seoul, the EU-Korea FTA enters into then-presidential strategy Lee Myong-bak (and his predecessor, No Mu-hyun), to transform the country into a free-trade centre in Northeast Asia. They both view free trade agreements as a necessity to boost Korea's wealth in the face of competition from Japanese and Chinese firms on the one hand, and the rapidly ageing Korean workforce on the other.

Conclusion

The agreement is seen as beneficial to both parties, albeit relatively more to the EU. Changes in trade flows to the FTAs are difficult to attribute, as other macroeconomic factors are also inevitably in place. For example, slow GDP growth and the depreciation of the euro against the South Korean won over the past five years have broken some expected and projected results. Despite Korea's perception that the EU is raising more funds than the agreement, Korea's exporters have a higher rate of utilisation of preferences than European companies (there are also large differences between EU Member States). Two key reasons are at the heart of this observation – first, Korea's exporters, which are often large export chaebols (large family conglomerates), are experienced and resourceful when it comes to administrative customs procedures, while the EU industry is more fragmented. Second, the "direct transport clause" of the agreement does not allow some EU exporters to use their regional centers in Asia to benefit from FTA preferences.

Despite the overall positive assessment, specific concerns remain on both sides. The EU (especially the European Parliament) see there is room for progress in regards to Seoul's progress in trade and sustainable development, especially when it comes to labour rights such as freedom of association. The EU also wants to make progress in allowing exports of EU beef to the RC, which has been blocked since 2001 due to the "bovine spongiform encephalopathy" (BSE), or mad cow disease in the 1990s. Korea wants a decision to export ginseng chicken soup. Other recurring issues are usually market access, especially as regards sanitary and phytosanitary measures, technical barriers and intellectual property rights.

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