

Changing Economic Environments in Mercosur and Strategic Ways to Foster Business Cooperation between Korea and Mercosur

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I. Introduction

In recent years, the economic ties between Korea and Mercosur countries have declined due to various factors. However, the emergence of market-friendly governments in Brazil and Argentina that put emphasis on reform and accessibility could prove to be the catalyst to reignite stagnant economic relations between Korea and Mercosur. In addition, the announcement of trade agreement negotiations between Korea and Mercosur will likely prove to be a turning point in their cooperation relationship. In this regard, this study was conducted to help forward a breakthrough in mutual cooperation, with a particular focus on business cooperation.

II. Major Changes of Economic Environments of Mercosur and Prospects

1. Macroeconomic Climate

Member states of Mercosur, due to a severe decline in world trade caused by weak global demand and slow growth, are faced with

shared macroeconomic challenges, such as low growth, high prices, high exchange rates, imbalance in balance of payments, and a declining job market.

Although many macroeconomic indicators of Mercosur member states have shown a synchronized pattern, there has been a lack of efforts to coordinate policies in a way that enables joint responses to economic fluctuations. As a result, the structural asymmetry between members has deepened, thus impeding further integration.

2. Productive Integration

Mercosur has implemented productive integration as a way to overcome the asymmetry of production capabilities among countries and industries and to foster regional integration. Productive integration aims to develop regional comparative advantages, diversify production structures into higher value-added sectors, and build regional value chains (RVC) through vertical integration and horizontal institutionalization.

Mercosur, however, has only achieved limited results in productive integration. Despite some successful outcomes including intra-industry trade growth in basic chemical and chemical products (pharmaceuticals), general machinery (including agricultural machinery) and automobiles, and the improved performance of firms participating in productive integration programs within the automotive and oil/gas industries, our quantitative analysis has shown a low level of RVC and PII (productive integration index) throughout the industries. The main reason for such limitation is the lack of initiative on the part of local enterprises. Therefore, in order for productive integration efforts within Mercosur to produce substantive results in the future, strengthening cooperation among intra-regional enterprises and inter-regional enterprises will be the key.

3. Foreign Trade Policy

Mercosur needs to set a new direction for its foreign trade policy beyond “open regionalism” and “post-liberal regionalism.” The internal and external trade environment has been characterized by a protracted recession in global trade, the prevalence of protectionism and segmentation of international trade systems. In response, Mercosur has revitalized its efforts to further intra-regional integration and conclude negotiations with various trade partners, which demonstrates a new attitude on the part of Mercosur toward trade policy.

In particular, if trade agreement negotiations with the EU are concluded in 2018, Mercosur’s foreign trade norms will become more advanced and trade negotiations with other countries will be accelerated. In this respect, the Mercosur-EU trade agreement will contribute significantly to a potential Korea-

Mercosur trade agreement.

III. Cases of Business Cooperation and Implications

Interactive cooperation with local corporations is essential to reduce physical costs, overcome non-tariff barriers and improve sustainability of cooperation. The study categorizes various types of business cooperation by five concepts borrowed from the inter-firm Bridge Model: manufacturing/production, logistics/infrastructure, distribution/marketing, financial cooperation and R&D/technical cooperation. The following case studies have important implications that could potentially allow Korea to expand the scope of its business cooperation partners and focus on strategic sectors within Mercosur.

Firstly, firms lower production costs through manufacturing/production cooperation. A joint venture established among Korea’s Dongkuk Steel and POSCO and Brazil’s Vale is an exemplary case of maximizing mutual benefits, leveraging each party’s comparative advantages in raw materials procurement, production operation and final purchases. On the other hand, Paraguay is gaining more attention from Brazilian and Chinese manufacturers as a South American production base. While the Maquila system offers a wide range of tax relief, its cheaper wage and electricity rates, geographical accessibility to Brazil through rivers, and the advantages of being GSP+ beneficiary provide a favorable production environment.

Secondly, firms overcome difficulties resulting from long distances, high transportation costs and lack of infrastructure through logistic cooperation. Costa Oriental, for example,

is a logistics service provider in Uruguay which offers integrated logistics services as a regional logistic center for various multinational companies.

Third, firms distribute and promote new products and services in new markets through distribution/marketing cooperation. The case of the Japanese e-commerce company Rakuten in Brazil illustrates the importance of establishing effective online distribution channel through cooperation with local companies. Another example is provided by UDI, a global publisher which distributes mobile applications in Latin America, whose case also helps expand the view on distribution cooperation beyond a mere physical network.

Fourth, firms secure finances and expand their business through financial cooperation. It is important to find new financial cooperation partners, as has been the case of cooperation in the banking sector between China and Spain. In addition, financial cooperation with NXTP Labs, a Latin American start-up accelerator, can provide opportunities to build ties in advance with prospective companies in Latin America.

Finally, firms mutually upgrade their knowledge, capabilities and technology through technology and R&D cooperation. Hana Micron's entry into Brazil is meaningful in that it is one of the scarce examples of R&D and technology cooperation in Latin America. Hana Micron contributed to the development of the semi-conductor sector in Brazil, in return for which it received substantial benefits from the Brazilian government, including investment financing, manpower, and tax benefits.

IV. Promising Areas for Cooperation between Korea and Mercosur

Our quantitative analysis has helped identify promising areas of cooperation between Korea and Mercosur in export and investment.

In trade, promising export products are those in which Korea or Mercosur has a comparative advantage in exports in the world market but has generated only limited trade between the two regions.

Regarding investment, sectors where domestic demand exceeds domestic production and demand for foreign investment is high provide future opportunities. At the same time, Korean companies should be competitive in such sectors, which can be measured by a trade surplus in global trade. The analysis focuses on Brazil and Argentina, as they are more relevant destinations for Korean investment.

It is noteworthy that expanding investments in these sectors can also improve the trade balance. Loss of profit caused by transferring production facilities abroad can be made up through profits generated from overseas branches. Also, this can lead to an increase in exports of intermediate goods from Korea.

Moreover, investing in sectors where productive integration has progressed relatively well allows both regions to gain mutual benefits. Korean investment promotes further productive integration by encouraging joint participation of large corporations and small and medium-sized firms, and in return, Korean firms can take advantage of already existing productive networks. These sectors are where South America's value chain participation index is high and Korean companies are competitive.

Table 1. Promising Areas of Cooperation

	Promising areas
Export	(Korea) Chemicals, Yarn and thread, Iron and steel products, Power-generating machinery and equipment, Metalworking machinery, Industrial machinery and equipment, Ships
	(Mercosur) Bovine meat, Sugar, Feeding stuff for animals, Oil-seeds, Leather
Investment	Printing, Coke and refined petroleum products, Chemicals and chemical products, Rubber and plastic products, Fabricated metal products, Electronic components and communication equipment and apparatuses, Machinery and equipment, Motor vehicles trailers and semi-trailers
Productive Integration	(Manufacturing) Rubber and plastic products, Fabricated metal products, Ships, Medical appliances and instruments and appliances for measuring, Electrical Machinery and Apparatuses, Motor vehicles trailers and semi-trailers, Coke and refined petroleum products, Chemicals and chemical products, Computers and office machinery
	(Service) Electricity and gas, Financial and insurance activities, Construction, Information and communications

Source: author

V. Promotion of Cooperation between Korea and Mercosur

The study proposes several policy suggestions for the government and firms to improve cooperation between Korea and Mercosur. The proposals are summarized in Table 2. The implications of the study are that the government, based upon an accurate understanding of changes in the economic environment of Mercosur, should establish various types of sustainable platforms for cooperation and develop a comprehensive approach towards Mercosur as an integrated bloc. The private sector, on the other hand, should diversify its cooperation partners and expansion strategies and es-

tablish a solid channel for dialogue. This can also play an important role in accelerating trade agreement negotiations by forming a consensus among private sector actors through joint research or conferences. **KIEP**

Table 2. Proposals for Korea-Mercosur Future Cooperation

Actor	Proposal
Government	① Make the best use of trade agreements as a platform for business cooperation
	② Introduce a Local Currency Payment System between Korea and Mercosur to support SME trade
	③ Participate in Mercosur Productive Integration programs
	④ Set up a Korean Desk as a channel to arrange business cooperation partners
	⑤ Establish a Korea-Mercosur Technology Innovation Center
	⑥ Conduct joint research on strengthening Korea's role as a bridge to Asia
	⑦ Build a standing B2B platform
	⑧ Operate an Export Incubator for the Mercosur market
	⑨ Identify new products for trade
Firms	① Diversify strategies and methods of overseas expansion
	② Expand cooperation with Latin American technology-based firms (Tecnolatinas)
	③ Hold Korea-Mercosur Business Summit or Forum on a regular basis
	④ Establish the Chamber of Commerce and Industry between Korea and Mercosur as a bloc
	⑤ Establish foundation for exports of SMEs by expanding cooperation with local e-commerce and home shopping companies
	⑥ Support trade agreement negotiations

Source: author