


# Opinions

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## Evaluation of the Korea-Chile FTA and Its Implications



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The Korea-Chile FTA celebrated its 10-year anniversary in 2014. As Korea's very first FTA, it symbolizes Korea's one step closer toward globalization. Its economic impact may not be comparable to that of the Korea-China or Korea-US FTA, but that does not mean its significance can be disregarded; the Korea-Chile FTA still merits close follow-up and evaluation. In this paper, I provide some important highlights of the trade relations between Korea and Chile after the FTA took effect, and discuss the impacts of the Korea-Chile FTA on the Korean economy.

Since the Korea-Chile FTA came into force in April, 2004, trade between Korea and Chile has dramatically increased. Korea's export to Chile jumped to US\$2.5 billion in 2012 from US\$0.5

billion in 2003, with an average annual growth of 19 percent. Korea's import from Chile increased to US\$4.7 billion in 2013 from US\$1 billion, recording 18 percent growth on average each year. These rates are impressively high, given that Korea's total export and import grew at about 12 percent per year over the same period, and especially since average annual growth rates of export and import between Korea and Chile were only -2.5 percent and 1.1 percent, respectively, during the pre-FTA period of 1995 to 2003.

Apparently the items that Korea and Chile have been trading since the FTA conclusion were concentrated in a few product categories. Korea has chiefly exported industrial products to Chile. Korea's major exports were motor vehicles and chemical products. They accounted for 47 percent and 29 percent of Korea's total exports to Chile during the period from 2010 to 2012, respectively. On the other hand, Korea has mainly imported copper and copper-related products such as copper ore and concentrates which accounted for more than 70 percent of Korea's total import from Chile during the same period. Although agricultural-fishery products accounted for only 9 percent of Korea's total import from Chile, they have been increasing rapidly, recording an average annual growth rate of 22 percent since the FTA. Korea's primary agricultural imports from Chile included fresh grapes, kiwi fruit, pork, and various processed foods.

If we look at the traded items at finer levels, it is clear that the Korea-Chile FTA significantly contributed to diversifying trade items. Korea's export items (HS 10 digit) to Chile increased by 66.5 percent from 938 items in 2003 to 1,562 items in 2013 due to the exports of machinery, chemicals, electronics, etc. During the same period, imported items from Chile also expanded from 168 items to 386 items due mainly to the increase in imports of agricultural-fishery products. The Korea-Chile FTA also played an important role in expanding the number of exporting firms for Korea. Its number multiplied around threefold from 733 firms in 2003 to 2,096 firms in 2013 and more than 200 new firms have been entering the Chilean market every year.

After the FTA implementation, exports from Korean small and medium-sized enterprises (SMEs) also made remarkable progress. From 2007 to 2013, SMEs exports to Chile increased by 4.6 percent on average, while large companies' exports decreased by 6.3 percent. The reason for the decrease in exports by large companies is that the price competitiveness of Korean products weakened after the Japan-Chile and China-Chile FTAs went into effect. On the other hand, SMEs were more willing to harness the new opportunities created by the

FTA and were more aggressive in pioneering the Chilean market. As a result, the share of SMEs in total exports increased from 16.5 percent to 27.3 percent in the period of 2007 to 2013. Also importantly, the utilization rate of the FTA's preferential tariff was high in the case of the Korea-Chile FTA. In 2013, the utilization rate on preferential tariffs on exports was 78.4 percent and the rate of imports reached 98.3 percent. These rates exceeded the overall average utilization rate of Korea's preferential import and export tariffs, which were 67 percent and 69 percent, respectively.

It seems there has been a more substantial impact on Korea's imports from Chile than Korea's exports to Chile. Korea's trade deficit with Chile has steadily increased since the Korea-Chile FTA. As suggested above, raw materials for manufacturing products account for a considerable part of Korea's imports from Chile. However, around 50 percent of the total copper imports included in Korea's export products from 2005 to 2009 is Chilean copper. It seems that Korea's trade deficit with Chile is related to its trade surplus with the world which results from the two countries' complementary industrial structures. It therefore suggests that the Korea-Chile FTA has likely contributed substantially to Korea's overall export activity.

There might be, on the other hand, an adverse effect on domestic agricultural production. Chilean agricultural products have been rapidly penetrating the Korean market, especially fruit and pork, since the Korea-Chile FTA implementation. Most representatively, Korea's imports of Chilean fresh grapes and processed food, accounting for over 80 percent of total crop imports from Chile, have increased at an average of 27 percent per year from 2005 to 2012. Korea's pork imports from Chile reached US\$126 million in 2012 from US\$80 million in 2005. Nevertheless, the cultivation of greenhouse grapes, which was predicted to be the sector most damaged by the Korea-Chile FTA, has been steadily growing rather than declining and domestic pork production has also been rising, thanks to increased per capita consumption of fruit and pork in Korea. Hence, it is hard to say that the potential damages of the Korea-Chile FTA to the Korean agricultural sector have been realized.

Let me summarize the above-mentioned findings. The Korea-Chile FTA, Korea's first FTA, has contributed to quantitatively and qualitatively upgrading trade relations between Korea and Chile. First, the FTA not only led to trade expansion but also to the diversification of trading items. Second, the Korea-Chile FTA contributed to expanding exports of SMEs. Latin America is a market that Korean SMEs typically avoid entering, owing to psychological barriers caused by the linguistic and cultural differences and long distance. Under these circum-

stances, signing an FTA between the two countries has acted on closing the psychological distance. Third, the FTA between Korea and Chile showed a high rate of utilization. A high utilization rate indicates that firms in both countries are actively enjoying preferential tariffs. These rates surpassed the overall average utilization rate of Korea's preferential import and export tariffs.

However, in spite of these positive outcomes, there are several areas to improve in order to maximize the effect of the FTA. First, Korea's export base established after the FTA has weakened in the Chilean market because of the recent exhaustion of the first mover effect and intensifying competition with later FTA partner countries such as Japan and China. In order to maintain cooperative momentum fostered through the FTA, it is necessary to diversify the cooperative scope from trade oriented economic cooperation to comprehensive cooperation including industry, investment, service, education, and technology. Second, the Korea-Chile FTA greatly contributed to boosting trade between the two countries, but its effect on increasing mutual investment is slight so far. In addition to this, in 2004, when the Korea-Chile FTA went into effect, Chile was expected to be an important bridge for Korean companies to advance into the Latin American market. However, there has been almost no instance of a Korean firm's entry into the Latin American market so far. [KIEP](#)