

Strengthening the Korea-Baltic States Economic Relationship



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Among the high-level guests of the PyeongChang 2018 Olympic and Paralympic Winter Games were the heads of states of the three Baltic countries: Presidents Kersti Kaljulaid of Estonia, Raimonds Vējonis of Latvia and Dalia Grybauskaitė of Lithuania. Each of the three held a meeting with their South Korean counterpart, President Jae-in Moon, to discuss strengthening their country's relationship with Korea. In particular, they agreed with President Moon to launch a joint economic committee between Korea and the Baltic states this year to explore possibilities of meaningful economic cooperation.

The Baltic states are not familiar in Korea due possibly to their small size in terms of territory, population, economy and trade with Korea.¹ Located on the eastern coast of the Baltic Sea (and hence the nomenclature), the area of their territories ranges from 45,228 km² (Estonia) to 65,300 km² (Lithuania), or about 45–65% of the southern half of the Korean Peninsula. Their combined population is about 6 million, slightly more than 10% of Korea's, and the size of their economies sum up to about 85 billion euros, or about 7% of the Korean economy. In fact, they are among

¹ The figures in this paragraph are for 2016.

the smallest in the European Union in all these measures. Korea's trade volume with the region is also small, although it is relatively significant with Lithuania, the largest of the three, driven mainly by the Korean export of intermediate goods in chemicals. Perhaps the best-known Baltic import to Korea is the Korean cover of the 80's popular song *Dāvāja Māriņa meitenei mūžiņu* (also known as Million Roses) from Latvia.²

Due to their similarities in location and size, the Baltics' path in modern history have largely coincided. Since their independence from the Soviet Union in 1991, they sought to adapt to the market economy by liberalizing regulations, privatizing state enterprises and attracting foreign investments. Estonia and Latvia joined the WTO in 1999, and Lithuania followed suit two years later. They all joined the EU in 2004; and Estonia joined the euro area in 2011, followed by Latvia in 2014 and Lithuania in 2015. Accession to the EU allowed them, among others, access to the European Structural and Investment Funds for development projects, which amounts to 4.4–8.4 billion euros during 2014–2020 for instance. Estonia and Latvia have been members of the OECD since 2010 and 2016, respectively, and Lithuania is on the firm path to accession. Their regulatory regimes are now considered among the most business-friendly in the world by the World Bank.

Not all their common features are on the bright side. Their economies were by far the hardest hit in the EU during the Great Recession, with all three contracting by more than 14% in 2009. This was amplified by their interlinkages and common exposure to neighboring, larger countries, most notably Russia, Germany and the Nordic countries. Latvia, which has the highest reliance on the other two, had to ask the IMF and the EU for a bail-out. More than 1% of population leave Latvia and Lithuania each year, which results in the population decline of an equivalent magnitude, while the EU as a whole and on average has an increasing population.³ The situation is slightly less severe in Estonia, the most developed of the three, but still worse than the EU average. Their income distributions are among the least equal in the EU, as indicated by their Gini coefficients of 33–37⁴, with no clear sign of improvement.

Apart from these macroeconomic similarities, the industrial structures of the Baltic states show differences in specialization. Estonia produces shale oil and has a well-developed electronics industry. It boasts world-class IT infrastructures which have enabled digitalization of

² Coincidentally, Latvia is the only Baltic country whose embassy has physical presence in South Korea (since 2014) and that won a medal in the PyeongChang Olympic Winter Games.

³ Annual average of 2011–2015.

⁴ Figures are for 2016.

administration, business, election and schooling to name a few. Lithuania derives more than 10% of its value-added from transportation and storage services thanks to its strategic location.⁵ It also has the only LNG terminal among the three and a growing chemical industry, which are important sources of imports in intermediate goods. Latvia is more specialized in raw materials and natural-resources-intensive products, with food processing accounting for about a quarter of total manufacturing.⁶ More than 70% of Latvian exports to Korea in 2017 are concentrated on wood products.

Regarding the gains from strengthening the Korea-Baltic states economic relationship, the Baltics have the potential to attract Korean tourists. The number of Koreans traveling abroad increases by around 10% each year,⁷ and there are signs of Korean tourists shifting away from Western Europe when selecting European destinations. With relatively low price levels, beautiful sceneries and historical sights, such as the UNESCO World Heritage site of Riga, the Baltic states can attract those Koreans looking for an alternative to the more usual destinations in the West. In fact, the number of Koreans traveling to Latvia is estimated to have increased by 30% last year for instance. Also, with their well-developed IT infrastructures, world-class business-friendly regulations, higher level of education and relatively low labor costs – less than a half of the EU average – they have potential to host Korean IT companies and startups aiming to enter the European market.⁸ This is among the goals of the MoUs Estonia and Latvia signed with Gyeonggi Province during the PyeongChang 2018 Olympic Winter Games. In particular, Korean game producers, who saw their exports to Europe more than doubled recently,⁹ can use the region for localization and as a local distribution hub.

As for Korean firms, they can benefit from the EU-funded infrastructure projects in the region. Thanks to the Korea-EU FTA, they are exempt from the track record requirement for participating in those projects, and some of them have already won such contracts in Poland and Slovakia. Given the composition of Estonia's and Lithuania's exports, Korea also has the potential to increase its intermediate goods supply to the region. More generally, Korean exporters can use the region's strategic location and relatively low wage levels for localization and distribution to the European market.

⁵ According to 2014 data.

⁶ Based on 2015 figures.

⁷ Annual average of 2007–2016.

⁸ Based on 2016 figures.

⁹ According to 2015 data.

The PyeongChang 2018 Olympic Winter Games offered a rare occasion to improve the nearly nonexistent mutual understanding and economic relationship between Korea and the Baltics, thanks to the efforts made by the heads of the Baltic states to travel to Korea and support the "Peace Olympics." The mood is set, and the opportunity should not be wasted. Successfully launching the joint economic committee without delay will be the first step to making the best out of this momentum. **KIEP**