

# A Strategy for the Successful Conclusion of the South Korea-Chile Free Trade Agreement

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## FOREWORD

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This project was completed to fulfill a requirement for a Master's Degree in Commercial Diplomacy from the Monterey Institute of International Studies (MIIS).

For the purpose of this project, I assume the role of a trade official for the Republic of South Korea Ministry of Foreign Affairs and Trade (MOFAT, hereafter). My specific task is to develop a comprehensive strategy to successfully complete the South Korea-Chile Free Trade Agreement (FTA) negotiation. The negotiation has stalled at the final phase, mainly due to mounting opposition from the South Korean agricultural community.

MOFAT is responsible for developing and coordinating South Korea's international trade, commodity, and direct investment policy, and directing negotiations with other countries on such matters. Since 1998, MOFAT has led the South Korea-Chile FTA negotiations.

I chose this subject because a South Korea-Chile FTA, if concluded, will mark South Korea's first ever free trade agreement, and thus will carry significant implications for their trade policy. I hope that my project can help conclude a South Korea-Chile FTA by providing MOFAT with strategies to build domestic consensus on opening the agricultural market. The timeframe for this report is the short-term (years 2002–2003).

I thank my project advisor Professor Geza Feketekuty for his guidance. I also thank Professor William Arrocha and Bill Monning for their input and enthusiasm throughout the entire study at the MIIS.

## EXECUTIVE SUMMARY

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In 1998, the South Korean government, with the ultimate goal of building an “open trading country,” decided to pursue free trade agreements (FTAs) with major trade partners. The main objective, to overcome the structural weakness of the South Korean economy, sharpened after the 1997 financial crisis. The crisis prompted South Korea to adapt to the changing economic environment, i.e., the recent trend of growing regional integration in the world economy.

Since its decision to open the economy, the government has been negotiating its first FTA with Chile. After four rounds of negotiations, the process stalled due to a wide difference on tariff concession schedules, particularly regarding exception items of agricultural products. South Korea insists that sensitive fruits like grapes, apples, and pears retain tariffs, while Chile calls for South Korea to abolish tariffs on all Chilean products, including agricultural goods, within 10 years of signing an FTA.

The bilateral trade pact is expected to have a positive economic effect for South Korea. It is likely to boost exports by \$660 million and improve South Korea’s welfare by \$960 million, while creating new export opportunities in Latin American markets. Chile’s open trade policy and its experience in concluding FTAs with other countries would provide invaluable experience to South Korea, not only in its attempts to further liberalize its own economy, but also in its pursuit of FTAs with larger economies such as Japan and the US.

Despite potential economic benefits, the agricultural sector poses obstacles to the conclusion of the South Korea-Chile FTA. Though the agreement’s impact on South Korea’s agricultural sector is likely to be small due to seasonal growing differences between the two countries, agricultural groups, in conjunction with other NGOs, have waged a fierce campaign against the agreement. In addition, negative public opinion towards trade liberalization and presidential election politics are working against the successful conclusion of the FTA deal.

To maximize the effect of a South Korea-Chile FTA, the South Korean government should

attempt to conclude the FTA with Chile as soon as possible. In order to overcome the domestic opposition, MOFAT must develop a domestic strategy to mitigate farmers concerns and a negotiation strategy to resolve differences on the agricultural concession schedule with Chile.

To these ends, the following strategy is recommended:

- By forming alliances with proponent groups, MOFAT should proactively engage in a dynamic public campaign to educate the public on potential benefits and costs of the FTA to the national economy. MOFAT could turn the public discussion from whether to conclude the FTA to how to best compensate potential losers of the FTA.
  - To address potential harm to the agricultural sector, MOFAT should propose a tripartite commission, comprised of representatives from government agencies, business groups and agricultural organizations. The main task of the commission is to reach an agreement on specific compensation measures for farmers greatly impacted by the South Korea-Chile FTA.
  - To resolve differences on the agricultural concession schedule, rather than exclude sensitive products from the agreement (except rice), the government might agree to an extra-long tariff phase-out period of 15 years for fruits like apples and pears. As for grapes, seasonal duties should be considered. The agreement must include special safeguard measures that protect against import surges for most import-sensitive products.
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## INTRODUCTION

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In his annual report to the President on the 2002 diplomatic agenda, Minister for Foreign Affairs and Trade Choi Sung-hong made it clear that a top diplomatic priority for the year would be MOFAT's pursuit of an early conclusion to the free trade agreement with Chile. Launched in 1998, the South Korea-Chile FTA negotiation stalled in 2000 at the fourth round of talks. The main sticking point is the discrepancy on tariff concessions, particularly regarding agricultural products.

To successfully conclude the agreement, MOFAT must overcome major challenges on the domestic front. First, the agricultural community is posing fierce opposition to the South Korea-Chile FTA out of fear that the increase of cheap Chilean fruit imports will severely hurt the local fruit industry and therefore destroy the domestic agricultural sector. Second, a presidential election is approaching in December, and politicians do not wish to lose farmers' votes. It is thus politically difficult for the government to achieve Parliament ratification this year. Third, without adequate understanding of the benefits of free trade to the South Korean national economy, public opinion remains largely negative toward the government's new FTA policy.

To overcome domestic challenges and make the negotiation a success, MOFAT must build domestic consensus among stakeholders on opening the agricultural market and compensating farmers affected by the FTA. The biggest problem during the last two years of negotiations has been the lack of consensus among domestic interest groups, government agencies and politicians. This has from the outset greatly restrained flexibility and strength at the negotiating table. Given the political sensitivity surrounding the agricultural sector during this election year, MOFAT, in conjunction with other government agencies, should take extra effort to promote free trade among the general public prior to the height of the presidential campaign in November/December. If presidential candidates pledge to thwart the negotiation by taking sides with farmers, the chances for successful conclusion of the South Korea-Chile FTA are slim.

This report presents a strategy for domestic consensus on agriculture for the South Korea-Chile negotiation. Domestic consensus will pave the way for parliamentary ratification and make possible a negotiation strategy to mitigate domestic farmers' concerns and resolve differences on the agricultural concession schedule with Chile. This report provides background information on the South Korea-Chile FTA initiative and the current state of the FTA negotiations. It addresses the South Korea-Chile FTA in terms of economic benefits, commercial effects on the local fruit industry, and the domestic politics surrounding the agricultural sector.

## BACKGROUND

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### 1. 'New trade policy'

In 1998, the South Korean government, with the ultimate goal of building an “open trading nation,” reversed its previous opposition to regional trade blocks and decided to pursue free trade agreements (FTAs) with major trade partners. The main objectives were to overcome the structural weaknesses of an economy crippled from a financial crisis, and to maximize the economic benefits of market expansion and foreign investment. The reversal of policy reflected concern for being left out from the growing regional integration of the world economy.

The government’s decision took into consideration the following factors:

➤ Accelerating restructuring and opening of the South Korean economy

The 1997 economic crisis exposed a structural weakness in the South Korean economy. To stimulate growth, the government implemented a series of economic reforms, including unilateral trade liberalization measures that have contributed to a rapid recovery. The government recognized that new trade pacts could help plug the South Korean economy’s structural weakness by encouraging inflows of foreign capital and management skills, and by injecting new competition into the domestic market.

➤ The spread of Regional Trade Agreements (RTAs) in world trade

Since its accession to the General Agreement on Tariffs and Trade (GATT) in 1967, South Korea has maintained steadfast devotion to the multilateral trading system and has not entered into preferential trading arrangements. Meanwhile, the number of regional trade economic agreements notified to GATT/WTO rapidly expanded in the 1990s, as shown by the following Table 1.

**Table 1: Number of regional trade agreements notified to GATT/WTO**

	1948~ 1954	1955~ 1959	1960~ 1964	1965~ 1969	1970~ 1974	1975~ 1979	1980~ 1984	1985~ 1989	1990~ 1994	1995 ~ 2001.3
Number of notifications	2	3	12	9	21	19	6	5	47	101
Total notified	2	5	17	26	47	66	72	77	124	225

Source; WTO Secretariat (2001)

The spread of regionalism has been accompanied by drastic increases in intra-regional trade, inter-regional trade, and total world trade. According to IMF trade statistics, the share of world trade within the framework of regional agreements grew steadily from 22.5% in 1959 to 66.3% in 1997. The increase in intra-regional and inter-regional trade signals the importance of regional economies in the world.

The European Union now has 29 regional and bilateral free trade or special customs agreements, and is in the process of negotiating with 12 additional countries. NAFTA members are entering into FTAA negotiations, which aimed to link North and South American regions under one trade region. Japan has completed a free trade agreement with Singapore and is exploring options with ASEAN countries, Canada, Mexico, and Chile. And China, a WTO newcomer, is pursuing an FTA with the ASEAN countries. The United States recently signed an US-Jordan FTA agreement and US-Vietnam bilateral trade agreement, and is also negotiating FTAs with Chile and Singapore. The US is discussing a 'Pacific 5' formula involving Singapore, Chile, New Zealand and Australia, and is negotiating Free Trade Areas of Americas.

All told, there are 130 regional free trade and customs agreements in the world; South Korea belongs to none, leaving South Korean exporters at a disadvantage in world markets. The government has recognized the necessity of joining a regional block to secure stable export and investment markets and to defend South Korean exporters against the discriminatory effects of other regional groups. In addition, if the potential

FTA partner is already a member of another FTA, it would be easier for South Korea to gain access and diversify its exports to a larger regional market.

➤ Strengthening Political and Economic Ties

Economic cooperation could have important spillover effects on political and diplomatic cooperation, covering such issues as security, environment, labor and cultural exchanges. By deepening the economic partnership with major trading partners through FTAs, South Korea can strengthen cooperative efforts on other important political and foreign policy goals, including cooperation in multilateral fora such as the WTO, OECD and IMF.

In November 1998, the Inter-Ministerial Trade Policy Coordination Committee (ITPCC) formally announced that South Korea would first seek a FTA with Chile, then would explore the economic feasibility of FTAs with such other trading partners as the US, Japan, New Zealand and Thailand. In December 1998, the government formed a special task force on a South Korea-Chile FTA. The task force consisted of five working groups, covering market access, trade rules, services, intellectual property and legal procedures.

South Korea has since been conducting a joint feasibility study of FTAs with Japan, New Zealand and Thailand at the level of private institutes. South Korea is also engaging in ongoing informal talks on the formation of ASEAN+3 (i.e., South Korea, Japan and China), which could counterbalance other major regional economic blocs such as NAFTA and the EU.

## **2. South Korea-Chile Free Trade Agreement**

### **1) Chile as South Korea's first FTA partner**

South Korea chose Chile as its first FTA partner because of high complementarities in trade structure and the potential to learn from Chile's plentiful experience in negotiating regional trade agreements. Chile, in turn, chose South Korea for its influence with neighboring Asian countries, and for its growth potential given reforms in several sectors, including the financial sector. The South Korean government specifically chose Chile as its first FTA partner for the following reasons:

➤ The structure of South Korea-Chile bilateral trade is complementary

The South Korea-Chile FTA is likely to benefit both countries because the two economies are highly complementary in their trade structures. Chile exports primary goods like copper and wood products, which are highly complementary to South Korea's exports of manufactured goods like automobiles and electronic products. Also, since Chile's agricultural export structure is centered on fruits and vegetables, the political burden of South Korea's agricultural market opening, particularly on the sensitive sectors of rice and beef, is expected to be less severe.

➤ It is South Korea's interest to pursue an FTA with a small economy like Chile's

Before establishing FTAs with large trade partners such as the US and Japan, South Korea needed to pursue strategic FTAs with smaller partners to gain negotiating and operational experience. An FTA with a relatively small economy like Chile will require lower adjustment costs on the South Korean economy, yet force South Korea to update many of its outdated economic institutions and practices. Following this adjustment period, South Korea will be in a better position to enter into FTAs with Japan, the US, or other major economies. It is thus in South Korea's interest to start a FTA with a smaller country and in this respect, Chile showed strong interest in signing a FTA with South Korea.

➤ We can learn from Chile's negotiation experience in establishing multiple RTAs

Chile is one of the most active countries in terms of liberalizing trade and establishing FTAs. Chile has already signed several FTAs with neighboring Latin American countries and Canada. It is also currently discussing FTAs with the US and the European Union. Chile's open trade policy and its accumulated experience in concluding FTAs makes it a model for South Korea, not only in its attempts to further liberalize its own economy, but also in its pursuit of further FTAs with larger economies.

**Table 2: Chile's Trade Agreements**

Chile is negotiating Free Trade Agreements (FTAs) with:  
The United States, the European Union, the European Free Trade Association

Chile has negotiated FTAs with:  
Canada (1997), Mexico (1998), Central America (2001)

Chile has comprehensive market opening agreements with:  
Bolivia (1993), Venezuela (1993), Colombia (1994), Ecuador (1995), Peru (1998)

Chile joined Mercosur (the South American Common Market, which includes Argentina, Brazil, Paraguay and Uruguay) as an associate member in 1996. It is now engaged in FTAA negotiations.

➤ Chile can serve as a gateway to the South American Market

Through an FTA with Chile, South Korea can secure export market access to Chile, but moreover can use Chile as a base to extend exports to other Latin American countries. In the meantime, Chile can take advantage of South Korea's trade links to widen market access to other Asian countries. Experience in FTA negotiation across the Pacific is essential for both countries to open further FTA opportunities. In addition to FTA negotiations with South Korea, Chile is researching alternative FTAs with Japan, New Zealand and Singapore. Chile's goal is to form FTAs with all APEC members by 2010.

**2) Preliminary Negotiations**

South Korea and Chile reached an agreement to establish an FTA at the bilateral summit talks of the APEC leaders' meeting in November 1998. A South Korea-Chile FTA Joint Committee Meeting was held in Chile to discuss the specific negotiation procedures. In April 1999, the two governments initiated the first high-level meeting for FTA negotiations. The main goal of this meeting was to discuss in depth the current economic situation of the two countries and major issues related to an FTA on the basis of the previously exchanged questionnaire. The second meeting was held in June 1999 in Santiago, Chile.

The two countries, after extensive exchange of information within FTA coverage, designed the Framework Agreement. Based on the draft of the Framework Agreement proposed by the South Korean government, both sides agreed on three basic principles of a South Korea-Chile FTA: 1) a comprehensive FTA, 2) liberalization in all areas, and 3) transparency. The scope of coverage includes seven specific subjects: goods, services, investment, IPR, government procurement, competition policy, and other legal matters such as dispute settlement. After two successful high-level meetings, the heads of state declared an official launch of South Korea-Chile FTA negotiations at the APEC summit meeting in September 1999.

### **3) FTA Negotiations and Current Status**

Currently, the South Korea-Chile FTA is negotiated through 5 groups, each with representatives from 15 government agencies (e.g., MOFAT, the Ministry of Finance and Economy, the Ministry of Commerce, Industry and Energy, the Ministry of Agriculture and Fishery, etc.). For its part, the Chilean negotiation team is led by the Ministry of Foreign Affairs.

#### ➤ 1<sup>st</sup> round of negotiation (December 14–17, 1999)

The two countries reviewed the draft text of the agreement prepared by the Chilean government. Each government agreed to set up five working groups covering market access, technical barriers, service and investment, trade remedy rules, and other legal issues such as dispute settlement. The two sides set January 1, 2000 as a starting point for negotiation and agreed to conclude the FTA agreement by the end of 2000. The agreement was set to take force in July 2001. The current effective tariff rate would be applied as a base for tariff negotiation.

#### ➤ 2<sup>nd</sup> round of negotiation (February 29–March 3, 2000)

The countries exchanged a tariff concession schedule of products. South Korea provided a tariff concession schedule for manufactured goods and agreed to present a tariff concession schedule for agricultural products (including forestry and fisheries products) prior to the third round of negotiations.

➤ 3<sup>rd</sup> round of negotiation (May 16–17, 2000)

Each country expressed strong complaints about the other's concession schedule. Chile griped that South Korea's tariff elimination schedule on the primary Chilean agricultural products had been withdrawn after the WTO agricultural negotiations. For its part, South Korea complained that its vital manufactured products had been excluded from the Chilean concession schedule. Both sides agreed to exchange a list of products of main concern.

In June 2000, Chile presented a revised tariff concession schedule of products. The schedule suggested that upon implementation of the agreement, 40% of products would get immediate duty free access, the tariff for 27% of products will be phased out within 5 years, the tariff for 32% of products would be phased out within 10 years, and 1% of products would receive special treatment.

The agricultural tariff schedules South Korea presented were as follows: 15% of Chilean agricultural products would get immediate duty-free access, tariffs for 31% of products would be phased out within five years, tariffs for 12.7% of products would be phased out within 10 years, tariffs for 1.5% of products would be phased out over the 5-year-period after 5 years of suspension, tariffs for 4.5% of products would be phased out within 15 years, and 1.3% of products, including rice, would be excluded from the concession schedule. Furthermore, such sensitive fresh fruit products as apple, pears, and grapes would be excluded, or the tariff elimination schedule would be put off until after related WTO agricultural negotiations.

➤ 4<sup>th</sup> round of negotiation (December 12–15, 2000)

Major differences over the concession schedules continued throughout the fourth round of negotiation. While South Korea continued to insist that some sensitive agricultural products be exempt, Chile insisted on no exceptions and, if not, that some manufacturing products from the tariff concession be excluded. The negotiation ended unsuccessfully and the fifth round of talks was put off.

To break the deadlock, the two countries agreed to hold a high-level meeting in June 2001

to revise and adjust their respective tariff concession schedule. Both sides reconfirmed their political will to continue the FTA negotiation at the bilateral foreign ministers' meeting during the APEC Summit in October 2001.

➤ Current state of the negotiations

After a year of suspension, the two countries held a working-level meeting in February 2002 in which South Korea presented the latest proposal on a tariff concession schedules. This included a new recommendation on Chilean fruit imports. Chile is expected to offer a revised proposal after which it will be decided whether the fifth round of negotiations should be held to finalize the deal.

At present, while offering immediate duty free access for all Chilean manufactured goods except copper cathodes (of which tariffs will be phased out by 10 year period), South Korea insists that such sensitive fruits as grapes, apples and pears retain their tariffs. Chile remains unchanged in its position on no exceptions, calling for South Korea to abolish tariffs on all Chilean products, including agricultural goods, within 10 years of signing an FTA. If not, Chile insists that it will exclude such manufacturing sectors as textiles, foot wear, washing machines and refrigerators — vital South Korean exports.

It should be noted that 80 percent of agreements have already been reached in such areas as competition, trade rules and dispute settlement. The sticking point for the conclusion of South Korea-Chile FTA is South Korea's agricultural concession schedule. Narrowing positions on fresh fruits like apples, pears and grapes, at the core of contention, will be the key to a successful outcome.

### **South Korea-Chile Economic Relations**

Chile was the first Latin American country to approve the South Korean government in 1949. Since they established diplomatic ties in 1962, South Korea and Chile have expanded mutual cooperation in economic and political affairs. The two countries will be celebrating the 40<sup>th</sup> anniversary of diplomatic relations in April. Over the four decades, Chile's exports to South Korea shot up from \$3 million in 1971 to \$902 million, while Chile's imports from South Korea, increased from \$17,000 in 1971 to \$592 million in 2000.

## **1) Overview of the Chilean Economy**

Chile has a market-oriented economy with ample foreign trade. Imports and Exports account for over 50 percent of the country's gross domestic product. In 1999, exports increased to \$18.3 billion from \$15.6 billion. Imports increased to \$16.9 billion from \$14 billion the previous year. Unilateral trade liberalization, including the elimination of most non-tariff measures, has left Chile with a relatively open economy. There is wide consensus across the political spectrum in favor of economic liberalization.

Chile is endowed with rich mineral resources near the sea, which have turned it into the world's leading copper and iodine producer, and a growing source of gold and non-metallic minerals. It abandoned import substitution in favor of free-market policies in the mid-1970s, more than a decade before the rest of Latin America. This unleashed competition and productivity growth and permitted an expansion of the traditional export industries of mining and fishing. The free market fostered the development of new sectors, such as cellulose, fruit, salmon, wines and methanol production, and a variety of services, including tourism. Chile's strong and increasingly diversified export sector has been its main engine of economic growth over the past two decades.

Between 1991 and 1997, Chile recorded real GDP growth of about 8 percent per year. The economy slowed during the financial crisis and a severe drought in 1999 caused negative economic growth for the first time in over 15 years. By the end of 1999, exports and economic activity picked up the pace. Chile recorded 5.4% GDP growth in 2000.

Chile's key industries today are copper, other minerals, foodstuffs, fish processing, iron and steel, wood, transport equipment, cement and textiles. Its main export items are copper, fish, fruits, paper/pulp and chemicals. Copper accounts for 42 percent of exports, other minerals (gold, iron, nitrate, titanium, and others) approximately 20 percent, fresh fruit 10 percent, fish and fish products 7 percent, and pulp and paper 6 percent. Chile's main trading partners are the United States (which takes 22 percent of exports and provides 20 percent of imports), Japan (9 and 10 percent), Germany (10 and 8 percent), and Brazil (7 and 8 percent).

Chile's single import tariff rate was cut from 9% in 2000 to 8% in 2001 and is scheduled to fall further, to 7% in 2002 and 6% in 2003.

## 2) South Korea-Chile Bilateral Trade

In 2000, South Korea-Chile bilateral trade totaled \$1.5 billion. South Korean exports to Chile in 2000 totaled \$592 million, while imports totaled \$902 million. South Korea is Chile's 6th largest export market in the world, and Chile is South Korea's second largest trading partner in Latin America. Since the mid 1990s, the bilateral trade volume has remained between \$1.1–1.6 billion annually. South Korea has run a constant trade deficit with Chile of about \$0.3–0.5 billion. Chile is the only country in Latin America to which South Korea is indebted. Exports from Chile to South Korea grew at 12.7% from 1991 to 1999, while Chile's global exports grew at 7.3%.

**Table 3: South Korea's trade balance with Chile (Unit: US \$ millions)**

	'96	'97	'98	'99	2000
Export	640	655	567	455	592
Import	331	1162	707	815	902
Trade balance	-187	-507	-139	-360	-310

Source: South Korea Trade Association

The economic size of Chile is relatively small, and trade volume between the two countries is a small percentage of South Korea's total trade. South Korea's exports to Chile accounted for around 0.3–0.5% of South Korea's total exports of US \$175.8bn in 2000. Imports from Chile were less than 0.8% of South Korea's total imports of US \$159.2bn in 2000. South Korea paid an average tariff for exports to Chile of 8.9%, while Chile paid an average tariff of 3.6% in 2000.

South Korea's primary exports to Chile include transportation vehicles, laundry machines, polyethylene, and such electronic products as refrigerators, televisions, and microwave ovens. South Korea's primary imports from Chile include copper, copper ore and concentrates, iron ore and concentrates, methanol and other refined copper. (See Table 4: South Korea-Chile Bilateral Trade 2000)

**Table 4: 2000 South Korea –Chile Bilateral Trade (Unit; millions, %)**

Exports to Chile			Imports from Chile		
Sector	Amount	%	Sector	Amount	%
<b>Total Exports</b>	<b>592</b>	<b>100</b>	<b>Total Imports</b>	<b>902</b>	<b>100</b>
Automobiles	164	27.8	Copper cathodes	462	51.2
Vehicle with cargo capacity	49	8.6	Copper ores and concentrates	195	21.6
Transmission equipment	29	4.9	Chemical wood pulp	72	8.0
Textiles	28	4.8	Methanol	38	4.2
Gasoline for other uses	28	4.7	Iron and ores	36	3.9
Ethylene politereftalate	27	4.6	Zinc and ores	16	1.8
Laundry machine	26	4.3	Wood pulp	14	1.5
Auto parts	17	2.9	Fishery frozen	12	1.3
Other transportation vehicles	17	2.8	Fresh grapes	10	1.2
Television	15	2.6	Animal feeds	10	1.1
Rubber tires	14	2.4	Molybden/concentrates	9	1.0
Refrigerator	11	1.8	Material wood	6	0.7
Steel. Prod	10	1.6	Particleboard	3	0.3

Source: MOFAT, 2001

### 3) South Korea-Chile Agricultural Trade

#### ➤ Chile's Agricultural Sector

Chile's land area is 756,946 square km, 7% of which is arable. Agriculture and forestry accounts for about 7% of GDP (1999). Most Chilean agriculture production is modern and efficient, achieving high yields. Among sectors that have expanded rapidly are fruit, poultry, pork and dairy processing, pasta manufacturing and wine and snack food production. Chile's agricultural sector (including forestry and fisheries products) now accounts for over 35% of total exports.

Chile is the largest fruit exporter in the world. Major crops include apples, table grapes, pears, apricots, plums, peaches, oranges and avocados, etc. (See Table 5: Leading Chilean Fresh Fruit and Vegetable Exports to the World, 1995–1999). The Chilean fruit industry utilizes the most advanced technologies, production techniques, genetics, marketing and business

strategies to produce and sell high quality fruit on the world market.

About 50% of Chile's fruit production is exported, with the US accounting for about 40% of its fruit exports, followed by Europe, Latin America and the Far/Middle East. In 1999, the export of agricultural products totaled about US \$1.5 billion worth of dollars, with fresh fruits like grapes, apples and kiwis totaling about US \$1.1 billion. Grapes, in particular, accounted for about 40% of the total Chilean agricultural exports.

**Table 5: Leading Chilean Fresh Fruit Exports to the World, 1995–1999 (US\$ millions)**

Fruits	1995	1996	1997	1998	1999
Grapes	519.7	598.5	635.6	265.3	605.6
Apples	226.5	267.8	213	265.3	259.4
Avocados	38.3	23.7	32	75.8	90.5
Pears	80.9	100.2	85.6	79.7	82.9
Plums	62.4	76.2	72.7	61.2	76.3
Kiwi fruits	77	86.6	79.3	98.3	71.9
Others	157.1	191.5	173.4	172.5	209.6
Total	1,161.90	1,344.50	1,291.60	1,364.70	1,395.60

Source: Prochile based on Central Bank of Chile data

➤ South Korea's Agricultural Sector

With the population shifting to urban areas, and the continued growth of the manufacturing and services sectors, the agricultural sector declined from 45 percent of South Korea's GDP in 1964 to just 5.4 percent in 1999. South Korea imports about 70 percent of its agriculture, and that percentage is expected to increase over time. In 1998, South Korea's 1.4 million farming households produced \$26.6 billion in output with rice accounting for nearly one-third of this production. Table 6 presents the major output of South Korean agriculture.

**Table 6: South Korean Agricultural production, by sector 1999**

Sector	Value(million dollars)
Rice	8,450
Farming Livestock	6,607
Vegetables	5,735
Fruit	2,506
Dairy, livestock products	1,850
Other	1,396
Total	26,613

Source: South Korean Agricultural information and Statistics Bureau

Farming in South Korea is dominated by small landholders and independent cooperatives. Only 20% of South Korea is farmable, and shortly after World War II, the government implemented strict limits on the amount of land that any one farm household might own. Small landholdings and significant trade protection are important features of South Korean agriculture.

Fruit is the most dynamic product in South Korea's agricultural sector. Fruit production has increased rapidly, from 833,000MT in 1980 to 1,766,000MT in 1990 and 2,452,000MT in 1997 (Table 7). The main fruit growers in South Korea are small individual farmers, 70 percent of whom own less than 2 hectares of land. The area planted with fruit has been increasing. The area, 99,000 ha in 1980, increased to 176,000 ha in 1997. Horticultural crops have replaced grain crops in recent years because of the higher profitability of fruits and the downturn in other agricultural sectors. The government has encouraged grain farmers to switch to horticulture as an alternative crop to rice production. Fruit production still depends heavily on weather conditions and farming technologies.

Although the rate of fruit consumption per person has increased by 1.9% annually, production has increased by only 0.5%, resulting in increased demand for imported fruit. Self-sufficiency levels for fruit will drop to 88.2% by 2004 from 93.1% in 1995. Demand for imported fruit such as oranges and grapes will grow. The fruit industry in South Korea is dominated largely by apples, grapes and pears and to lesser extent, mandarin oranges (see Table 7). South Korea's main fruit imports are bananas, pineapples, kiwi, grapes, grapefruit, lemons and

oranges. Bananas used to account for over half of total fruit imports in the early 1990s, but oranges and grapes now make up a significant sector of the market.

**Table 7: Fruit Production and Cultivated Area Production (1000MT), Area (1000ha)**

	1980		1990		1996		1997	
	Prod.	Area	Prod.	Area	Prod.	Area	Prod.	Area
Total	833	99	1,766	133	2,207	173	2,452	176
Apple	410	46	629	49	651	44	652	40
Pear	60	9	159	9	219	18	260	22
Grape	56	8	131	15	357	27	393	28
Peach	89	19	115	12	128	10	147	11
Mandarin	161	12	493	19	514	25	649	26
Persimmon	NA	NA	NA	NA	211	27	240	20
Other fruits	57	14	239	29	127	21	111	29

Source: Ministry of Agriculture and Fishery (MAF), 1998, South Korea

Under the terms of the Uruguay Round Agreement on Agriculture (URAA) signed in 1995, South Korea liberalized imports of all agricultural products except beef and rice. Still, most agricultural products remain highly protected by both tariff and non-tariff barriers. Tariff rates on most imported fruit and vegetables are between 30 and 50 percent. South Korea's main agricultural import partners are the United States (31.5%), China (13.2%) and Australia (8%).

➤ Agri-food trade with Chile

South Korea is a net importer of agri-food products from Chile. In 1999, agricultural imports from Chile reached US \$14 million against agri-food exports of only US \$0.9 million. Agricultural imports from Chile totaled 26 million dollars in 1997, 6 million dollars in 1998 and 14 million dollars in 1999, accounting for just a slight percentage of South Korea's total agricultural imports (See Table 8).

South Korea's main agricultural imports from Chile are fresh grapes, kiwi and tomato paste. Most other fruits, including Chilean apples and pears, are forbidden at present due to quarantine regulations. Chilean grapes, which in 1997 accounted for 98% of South Korea's total grape imports, currently account for more than 90 percent.

**Table 8: Chilean Fresh Fruit Exports to South Korea (US\$ millions)**

Fruits	Chilean global exports(1997)	Applied tariff	South Korea's total imports		Imports from Chile(1998.9)
			1997	1998.9	
Grapes(fresh)	628	47%	18.9	2.1	2.0
Apples(fresh)	211	48%	0	0	0(forbidden)
Pears(fresh)	102	48%	0.08	0	0(forbidden)
Peach	29	50%	0	0	0(forbidden)
Plums	72	50%	0	0	0(forbidden)
Kiwi fruits	78	48%	14.5	4.3	0.4

Source : Prochile based on Central Bank of Chile data, KOTIS, South Korea Custom Service

Climatic and geological conditions, market oriented agricultural policies, and the plantation structure of processing, marketing and logistics make Chilean fruit exports competitive. By comparison, the South Korean fruit industry is characterized by limited arable land, a less temperate climate for growing fruits, an underdeveloped marketing structure, small family subsistence farming and the government support. (Refer to Appendix 2 for a comparison of South Korea-Chile agriculture sector and bilateral trade, 1999)

### 3. WTO Agricultural Negotiation

WTO members agreed to initiate negotiations for agricultural trade reform a year before the end of the implementation period, i.e., by the end of 1999. These talks began in early 2000 under the original mandate of Article 20 of the Agriculture Agreement. At the November 2001 Doha Ministerial Conference, the agriculture negotiations became part of a single undertaking in which virtually all linked negotiations are set to end by January 1, 2005.

The first phase of agricultural negotiations consisted of countries submitting proposals for their starting positions. The second phase of negotiations ended with discussions on specific topics and technical details. The next tasks are formulas and other “modalities” for countries’ commitments by March 2003, and for countries to submit comprehensive draft commitments by the Fifth Ministerial Conference in Mexico in 2003. Significant tariff reductions, domestic support and export subsidies can be expected to be the main focus of agricultural negotiations.

In the ongoing WTO agricultural negotiations, South Korea is trying to secure developing-country status. South Korean agriculture still needs some degree of protection, and developing-country status would facilitate gradual liberalization and minimize shocks to local farmers from the market opening. On the other hand, as a member of Cairns group of agricultural exporting countries, Chile supports a substantial opening in agricultural markets and the elimination of export subsidies.

## ANALYSIS

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### 1. Analysis of the Economic Effects of a South Korea-Chile FTA

#### Potential benefits

A South Korea-Chile FTA is expected to benefit both countries. While Chile exports raw materials, South Korea exports manufactured goods. According to a study by the South Korea Institute for International Economic Policy (KIEP), an FTA with Chile would boost South Korean exports by \$660 million and imports by \$220 million, thereby improving South Korea's trade balance by about \$440 million. The FTA will also improve South Korea's welfare by \$960 million dollars (See Table 9). South Korean producers of automobiles (occupying 18% in Chilean import market), refrigerators (31%), microwave ovens (69%), washing machines (65%), tires and automobile batteries, textiles, elevators and PVC would be the greatest beneficiaries of a free trade agreement.

Tariff elimination with Chile will have secondary benefits for South Korea. The FTA's that Chile has already signed with other countries act to block South Korean exports. For example, preferential tariffs imposed by Chile on Canadian and Mexican exports through FTA agreements block South Korea's export of automobiles and tires. A South Korea-Chile FTA will provide South Korean products price competitiveness, enabling them to compete with other countries in Chilean market.

Mexico, with an industrial structure similar to South Korea's, benefited significantly from its own FTA with Chile. Mexican exports to Chile jumped from \$180 million in 1992 to \$930 million in 1996. South Korea is expected to enjoy a similar export expansion with a Chilean FTA. Furthermore, the FTA has potential for securing an effective gateway to the Latin American market. The Latin American population is a huge potential market for South Korean automobiles and other South Korean manufactured products.

#### Potential costs / Sensitive sector

Of the manufacturing sectors, the copper processing industry in South Korea will be most affected by a South Korea-Chile FTA. This is because Chilean copper is leading the world in exploitable reserves, production, and export volume. The mining sector is the most important

and competitive sector in the Chilean economy, accounting for more than half of global exports.

The most affected industry from a South Korea-Chile FTA, however, is likely to be South Korea's agricultural sector. According to the Revealed Competitive Advantage (RCA) indices, relative competitiveness for grapes, plum, kiwi, pears and apples were higher than any other Chilean agricultural products. Therefore, it is likely that the export of such Chilean fruits as grapes, apples and pears to South Korea would increase as the South Korea-Chile free trade agreement entered into force.

Agricultural imports from Chile totaled \$26 million in 1997, \$6 million in 1998 and \$15 million in 1999, accounting for a tiny fraction of South Korea's total agricultural imports. Moreover, due to their respective geographical locations, the fruit harvesting seasons differ and thus most Chilean fruit imports do not compete directly with local fruits. Though the increase of Chilean fruit imports is likely to inflict some damage on competing domestic fruit producers, the impact on South Korea's entire agricultural sector would be small. The study by South Korea Agriculture Economic Institute (KREI) predicts that with the complete tariff elimination on the agricultural sector, domestic fruit and vegetable production would decrease by about 0.007 percent while imports would increase by about 96%.

### Conclusion

Some argue against the South Korea-Chile FTA, not because of potential damage to South Korean fruit farmers, but rather because the economic size, purchasing power and trade volume of Chile is relatively small. The spending power of Chile is only 20 percent that of South Korea. Regionalism, however, is an important trend today and a growing number of countries are affiliating themselves with regional trade arrangements in one form or another. FTAs involving South Korean trading partners but excluding South Korea can seriously damage South Korean exporters. KIEP estimates that such non-participation will cost South Korea about US \$35 billion worth of lost exports.

As a country whose economy heavily depends on foreign trade—total foreign trade represented about 73 percent of South Korea's GDP in 2000—South Korea has few BATNA (Best Alternative To a Negotiated Agreement) other than to engage in regional trade

agreements. If South Korea does not participate in FTAs, it will lose a golden opportunity to expand economic ties and promote further economic growth and development. A number of recent studies conclude that as countries reduce barriers to trade (both internal and border restrictions), per capita income increases significantly.

A South Korea-Chile FTA will likely bring sizable gains to South Korea in the long run. South Korea should learn from Chile’s experience in establishing FTAs, and South Korea should pursue its own FTAs with major trading partners like Japan and the United States. The positive side of an FTA is not limited to growing trade volume. As seen in the case of the EU, the agreement is a catalyst for competition among member nations to accelerate industrial realignment and expedite economic reformation.

The following table is a summary of KIEP studies on the economic effects of a South Korea-Chile FTA. In assessing economic effects, three basic scenarios are presented. The first scenario is based on complete tariff elimination by both countries across all sectors. The second scenario is based on complete tariff elimination in general sectors and partial tariff reduction for agricultural products and livestock. The last scenario assumes zero tariffs in all sectors except for agriculture and livestock.

**Table 9: Expected Economic Effects of a South Korea-Chile FTA (Unit: US\$ millions)**

	Overall tariff Liberalization	50% Tariff Reduction in Agriculture	With Agriculture Excluded
Welfare	960	960	950
GDP(%)	0.01	0.01	0.01
Exports	660	660	660
Imports	260	250	240
Trade Balance	400	410	420

Note: 1) In value terms  
 Source; Cheong In-kyo (2000). South Korea-Chile FTA: Background, Economic Effects and Policy Implication KIEP Policy Analysis 00-27

**2. Commercial Analysis of the FTA Impact on the South Korean Fruit Industry**

A South Korea-Chile FTA would likely bring a surge of Chilean fruit imports, affecting the domestic fruit industry. As already stated, Chilean fruit exports, both natural and processed, are highly competitive and maintain a dominant position in the world market. South Korean

farmers and agricultural organizations fear that imports of grapes, pears and apples from Chile will dramatically increase with tariff elimination, resulting in decreased sales and domestic prices and reduced income for farmers. South Korean farmers argue that a South Korea-Chile FTA would completely destroy the domestic total fruit industry.

The domestic grape industry is the most sensitive sector in the South Korea-Chile FTA negotiation. Since 1996, when the domestic grape market was liberalized for the first time, Chilean grapes have accounted for over 90 percent of market share of total imported grapes. Even after the introduction of Chilean grape imports to the domestic market, however, domestic grape production continued to rise. In 1999, domestic grape production amounted to 0.47 million tons. Chilean imported grapes represented only 1.3 percent of the total domestic grape production, as shown by Table 10.

**Table 10: Domestic grape production and imports**

	93	94	95	96	97	98	99
Domestic production(A) (ton)	163,780	211,930	316,443	357,274	393,195	397,784	470,124
Area harvested(ha)	16,991	19,773	26,030	27,196	28,290	29,871	30,537
Grape imports (ton)	-	-	-	2403	8896	1140	6111
Import from Chile(B)(ton)	-	-	-	2403	8896	1140	6062
B/A	-	-	-	0.67%	2.26%	0.29%	1.29%

Note: 1) The number of grape farming households is 53800, which represents 19.3% of the entire fruit farming households in South Korea.

2) Greenhouse production of grapes accounts for 772 ha, 2.6% of the total grape production.

Source: KREI, <agriculture outlook>

That domestic grape production has expanded despite increased imports is partly due to a steady increase in domestic fruit consumption. Per capita consumption of fresh fruit has increased from 41kg in 1990 to 58kg in 1997. That imported grapes have had insignificant impacts on domestic grape production, however, is mainly due to different marketing seasons for imported and local grapes. As revealed by Table 11, Chilean fruit imports are largely received during the March-June period, South Korea's non-marketing season. Local grapes start to enter the market by July, with an exception of the greenhouse-produced grapes, which

are being released by May. Thus, for the most part, the Chilean imported grapes are unlikely to compete with local grapes.

**Table 11: Comparison of marketing season between Chilean grapes and local grapes**

January	February	March	April	May	June	July	August	September	October
Chilean grape production									
		Chilean grape marketed in South Korea							
				Local greenhouse grape produce marketed					
						Local grape produce marketed			

Chilean imported grapes are much cheaper than local greenhouse grapes, as evidenced by Table 12. Currently, the import cost of Chilean fruits is 2300 won per kilogram with a current tariff rate of 47 percent. With the complete elimination of duties under FTA, the import price might fall to 1600 won. The marketing cost of imported grapes, however, including transport, storage and other costs added, could double the price. On the other hand, the KIEP study predicts that with complete tariff elimination, Chilean grape imports are likely to increase by 66 percent from 1997 levels

**Table 12: Price comparison between local and Chilean imported grape (unit; won/kg)**

	Chilean grape price		Local grape price		Applied tariff (1999)
	Import price	Retail Price	Prod. Cost	Retail price	
Greenhouse produce	2300	+2300	3395	6960	47%
Natural produce			1790	2198	

Source; Ministry of Agriculture and Fishery (MAF)

With FTA implementation, the increase of lower-priced Chilean grape imports will likely decrease demand for domestic greenhouse grapes, inflicting damage on domestic greenhouse grape farmers. The government should thus consider a special measure in the FTA negotiation to address the potential harm on local greenhouse grape producers. Nonetheless, greenhouse grape production represents only about 2.6 percent of total domestic grape production. Consequently, the overall effects on the domestic grape industry are expected to be less than

economic benefits for South Korea from the South Korea-Chile FTA.

Greenhouse grape producers are not the only ones concerned—domestic pear farmers also worry about the loss of income from increased imports of Chilean products. They fear that income will decrease about US \$2 million. Yet, it is known that Chilean pears are not the same as domestic pears. Since they are currently banned from the domestic market, it is hard to predict precisely how much impact imported pears and apples would have on the local industry. It is almost certain, however, that pear and apple imports from Chile would increase with an FTA agreement, and domestic prices would decrease. Still, given that there is a seasonal difference and that South Korea is one of many export markets for Chilean fruits, it is highly dubious that Chilean fruit imports would destroy the South Korean fruit industry.

Though the local fruit farmers' concern is considered overblown, the domestic fruit industry will likely be the most affected by the FTA. Therefore, the government must take a cautious approach and negotiate special terms that could minimize damage. A gradual market opening over a long period for grapes, pears and apples should be considered an alternative to the complete exclusion of those fruits from the tariff elimination.

### **3. Political Analysis**

Opening the agricultural market in South Korea has always been very sensitive, both politically and economically. Though rice, the most politically sensitive item, will likely be excluded from the proposed South Korea-Chile FTA, the agricultural sector still presents the biggest hurdle for the successful conclusion of the FTA.

The current impasse in the FTA negotiation can largely be attributed to domestic politics of the agricultural sectors in South Korea. South Korea's farm sector is heavily subsidized and though uncompetitive, wields substantial clout in national politics. The farm sector has disproportionate representation in the National Assembly, even though agriculture, forestry, and fishing account for only 5 percent of GDP and 11 percent of the South Korean population. More than 40 percent of the representatives have an agricultural region as their constituency. Due to the rapid urbanization and industrialization of the past 30 years, a good share of urban

population still has family members in agricultural areas and thus support farm protection and subsidies.

Over time, these ties—and the political power they lend the farm sector—are likely to weaken with the continued decline in agricultural population. Only 6 percent of young workers (age 20 to 24) are farmers, and almost 70 percent of the agricultural work force is over 50 years old. In the near term, however, agriculture poses the largest obstacle to the South Korea-Chile FTA.

The agricultural sector in South Korea has been protected by government intervention for over three decades. The government has over the years tried to strengthen its own agricultural production and avoid imports. With the launch of the WTO in 1995, however, imports of almost all agricultural products, save beef and rice, were liberalized through tariffs. The agricultural sector was ill-prepared for the market access required under the URAA, and the UR agriculture negotiations left farmers with widespread bitterness toward the government for its failure to protect them. The WTO has begun agriculture negotiations that will further open the agricultural sector in South Korea. With these developments, the announcement of the South Korea-Chile FTA has provoked vociferous opposition from farmers.

The farming community, which felt threatened by the possible increase of Chilean fruit imports, has called for the cessation of the FTA negotiation or the exclusion of the agriculture sector from the agreement. Farm groups have been staging a fierce campaign against the agreement, claiming that the FTA may threaten the livelihood of 5 million farmers. While the fiercest opposition is from the ‘Farmers Association of Grapes’, the National Farmers Association is leading concerted efforts among 21 farm groups against FTA talks. They argue that the government has forsaken the agriculture sector for the manufacturing sector, and that large conglomerates will benefit at the expense of farmers. They also fear that a South Korea-Chile FTA might lead to future FTAs with larger economies like Japan and the United States, ultimately leading to economic subordination. Farmers’ groups are forming political alliances with such NGOs as citizen groups, labor unions and even consumer groups in the campaign against FTA negotiation. Those groups have been traditional allies in protesting the government’s past policy.

Politicians, keenly conscious of farmers' votes in the upcoming presidential election, have been lukewarm on pushing ahead with the agreement. The ruling party, Millennium Democratic Party (MDP), called for the government to either slow down the FTA process or to exclude agriculture from the agreement. Rep. Jang Jeong-eon of MDP announced that he would push for parliamentary rejection of South Korea-Chilean FTA by generating supra-partisan support. Noting Chilean apples, grapes and kiwi fruit are among the world's finest, he said that a free trade accord with such an agrarian country will devastate South Korea's agricultural basis. He also added that opening the domestic agricultural market to Chile would invite other countries, including the US and other WTO members, to ask for equal access to the South Korean market.

Despite such remarks, in light of the fact that the FTA negotiation were initiated under the leadership of President Kim Dae-Jung, the official head of MDP, it is unlikely that the ruling party and its presidential candidate will completely denounce the FTA process unless the opposition party candidate criticizes the deal. The official remarks have not been made by the opposition party (Grand National Party, GNP) on the South Korea-Chile FTA issue. If the GNP decides to attack the current FTA negotiation, however, the potential MDP candidate would have no choice but to oppose the South Korea-Chile FTA deal in efforts to win farmers votes during the election period. This would result in complete cessation of the negotiation amid the swirl of domestic politics.

In the meantime, the lack of consensus among government agencies has further complicated the FTA process. While MOFAT remains firm in its plan to conclude FTA talks as soon as possible, the Ministry of Agriculture and Forestry (MAF) has been largely negative toward the FTA, often presenting uncompromising proposals on the agricultural market opening. The Minister of Agriculture and Forestry Kim Dong-tae recently recommended that the government suspend its FTA negotiations with Chile until after 2005 when the WTO finalizes the new Doha round of global trade talks. His remarks came just as the two countries resumed working-level talks in February after a year of suspension. It's hard to fathom the intention of his remarks, but the apparent disunity among government agencies only creates confusion and hinders the negotiation process. Already, some media blame the lack of unity among government agencies for the failure of FTA negotiations.

It is important that policymakers work in a consistent and responsible manner to gain public confidence and support for its FTA policy. MOFAT should coordinate with MAF to gain support from farm groups in completing the FTA with Chile. MOFAT, in cooperation with MOCIE (Ministry of Commerce, Industry and Energy) and MOFE (Ministry of Finance and Economy) in support of the FTA, should make efforts to create an overall pro-FTA environment within the government agencies, giving MAF pressure to facilitate the agreement.

Opening the South Korean agricultural market is a painful process for South Korea, especially given domestic agriculture's poor competitiveness and underdeveloped structure. With WTO agricultural negotiations underway, however, it is inevitable that South Korea will soon face further opening of the agricultural market in the near future. Considering the domestic agricultural difficulties, the South Korea government should attempt to ensure gradual liberalization and minimize shocks from opening the market. More fundamentally, however, South Korea should direct its efforts at enhancing competitiveness of the agricultural sector in the long run rather than rely on protectionist measures, which will increasingly be challenged by foreign countries.

It is not possible to exclude the agricultural sector, as requested by domestic farmers and some politicians, from negotiating free trade agreements. This is particularly true of the FTA negotiation with Chile, since the Chilean agricultural sector stands to benefit from the agreement. In fact, Chilean farmers' groups are strong proponents of the FTA with South Korea, while Chilean manufacturing groups oppose the deal. Excluding the agricultural sector would give Chile little incentive to pursue the South Korea-Chile FTA.

Chile is willing to allow unhindered access of manufactured goods if South Korea opens its agriculture sector. Therefore, the successful conclusion of a South Korea-Chile FTA depends largely on gaining domestic consensus on agriculture. To narrow the difference with Chile, the government should exert more flexibility in its agricultural concession schedule. Rather than insisting on exempting contentious fruit products from the schedule, the government should consider gradual market opening. In the meantime, the government should devise real compensation measures for seriously affected local farmers.

#### **4. Public opinion**

Public opinion of the current FTA process, influenced by agricultural groups' strong protests, remains negative. Without correct understanding of the FTA and its potential benefits, the general public thinks of it as a unilateral market opening process, with trade liberalization leading solely to import surges that hurt the domestic industry. Some even consider the FTA, with its large economies, a form of subordination to a dominant economic power. Ironically, consumer groups that oppose the South Korea-Chile FTA would actually benefit from cheap imports.

While the agricultural community leading the campaign against the FTA is shaping public opinion, proponent groups that stand to gain from the FTA are less vocal in their support. South Korea's manufacturing sector favors a South Korea-Chile FTA, as most exports to Chile consist of such manufactured goods as automobiles and electronic goods. Manufacturers, however, are solely relying on the government to generate support for FTA talks. According to the South Korea Economic Research Institute's recent survey of 154 domestic corporations, 88.3 percent, or 136 firms, favor more active FTA policy by the government. Business and industrial groups that will be the main beneficiaries of an FTA should take a more active role in promoting the benefits of the FTA to the overall economy.

The government should also be blamed for the current lack of understanding among the general public. The government did not make sufficient efforts to educate people on the benefits of the new policy and did not solicit the private sectors' opinion in its trade policy decision-making process. Unfavorable attitudes towards the government's FTA policy and the South Korea-Chile negotiations resulted.

The lack of public knowledge and negative attitudes toward trade liberalization need to be addressed for the government to conclude the South Korea-Chile FTA and pursue FTAs with other economies in the future.

## **5. International Legal Aspects: Conditions for the formation of an FTA under GATT/WTO**

Since South Korea and Chile are WTO members, a prospective South Korea-Chile FTA is bound to meet FTA requirements set forth by the GATT/WTO. The GATT adheres to the basic principle of nondiscriminatory treatment between its contracting parties (Article 1, GATT) and has worked to eliminate trade barriers to all member nations. It does, however, in Article 24, approve of Free Trade Agreements (FTAs) and other regional agreements as intermediate solutions. Though such agreements, strictly speaking, violate the nondiscriminatory principle, it is likely they will in the long run lead to global liberalization.

Article 24 of the GATT/WTO and Article 5 of GATS define certain exceptions to the principle of MFN and set forth the following five basic FTA requirements:

First, even if an FTA is formulated, trade barriers with other contracting parties should not be raised (Article 24, Clauses 4 and 5[b]). If an intermediate treaty is concluded, it should include plans and schedules to establish a FTA within a reasonable period (Article 24, Clauses 5[c]). According to the interpretation of Article 24 agreed during the Uruguay round, a “reasonable period” is ten years. Countries participating in the FTA should immediately notify GATT/WTO members (Article 24, Clauses 7). Under the FTA, customs tariffs and other restrictive trade rules and regulations should be abolished for substantially all sectors (Article 24, Clauses 8[b]).

Yet, as the FTA between the US and Israel excluded the agricultural sector, the phrase “substantially all trade” has been interpreted to allow some latitude in the structure of trade agreements. Numerous free trade pacts have been negotiated without comprehensive coverage of agricultural trade. The Canada-US FTA exempts important farm products from its liberalization commitments, and these exemptions were carried over into NAFTA. NAFTA eliminates all farm trade barriers between the US and Mexico, albeit over a lengthy transition period, but allows the industrial countries to avoid free trade in agriculture. The European Union limits the scope of its farm trade reforms in all its preferential trade pacts, including its most recent FTA with Mexico. In each case, the partner countries justify their actions by

arguing that agriculture is a small share of bilateral trade and that the pact covers “substantially all” trade.

In the case of the South Korea-Chile FTA, exempting such a politically sensitive sector as agriculture from the FTA liberalization schedule would be possible under the Article 24, even though such an exception is highly unlikely. The FTA including services trade should satisfy requirements similar to those stated above pertaining to the commodity trade (GATS Article 5, Clauses 1, 4 and 5–7)

South Korea and Chile have traditionally favored a multilateral approach to trade and investment liberalization. Both countries committed themselves to the rule-based requirements of GATT/WTO for forming a FTA in order not to undermine the basic principle of nondiscrimination and bring harm to third countries. This position is reflected in the three basic principles of the South Korea-Chile Framework Agreement: a comprehensive FTA, liberalization in all areas, and transparency in implementation. The international response to South Korea-Chile FTA is likely to be muted due to the non-threatening size of the agreements.

## RECOMMENDATION

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The South Korean government should conclude the FTA negotiation as planned. A South Korea-Chile FTA will not only bring economic benefits for South Korea, but will also help South Korea pursue further FTAs with larger economies in the long run. If negotiations fail, it may tarnish South Korea's national image and credibility in the international trade community, making it difficult for the government to pursue FTAs with other countries. Given the suspicion in international society that South Korea's push for economic reform began after the economic crisis had declined, the successful conclusion of the South Korea-Chile FTA will end doubts of South Korea's commitment to economic reform and building an open trading nation.

Considering the political sensitivity of the agricultural sector and its poor competitiveness against Chilean agricultural imports, MOFAT should come up with a two-pronged strategy. The domestic strategy should build consensus on the sensitive agricultural issues, and the negotiation strategy should resolve differences with Chile over the agricultural concession schedule. It is critical that the government create a pro-FTA environment among the general public to prevent the politicization of the South Korea-Chile FTA during the presidential campaign period this November–December.

To achieve the goal, it is recommended that MOFAT implement the following measures:

- MOFAT should form alliances with proponent groups to shift the public discussion from 'whether to conclude the FTA' to 'how to compensate potential losers'.
- Domestic consensus among stakeholders on agricultural market opening should be established, and measures on restructuring the agricultural sector and compensating farmers from damages should be formed.
- With domestic consensus, MOFAT should exert more flexibility in its concession schedule on less sensitive agricultural products and compromise with Chile to conclude the South Korea-Chile FTA.

## DOMESTIC STRATEGY

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### **The overall objective of the domestic strategy is the following:**

- Educate the South Korean people about potential benefits and costs of the FTA
- Shift the negative public opinion about the South Korea-Chile FTA
- Build domestic consensus among stakeholders
- Shift nationwide debate from whether to conclude the FTA to how to compensate farmers
- Gain support from the general public on the early conclusion of the South Korea-Chile FTA and create consensus among presidential candidates to ensure parliamentary ratification of the agreement after elections.

### **The key messages to be conveyed through the domestic strategy are the following:**

- South Korea is one of few countries without regional trade agreements
- As a result, South Korea's exports face increasing discrimination in world markets, harming the South Korean economy
- Economic openness and liberalization is key to renewed economic success after the 1997 economic crisis
- South Korea-Chile FTA would bring significant economic gains
- The potential harm on the South Korean agricultural sector is small
- Compensation for farmers and an economic plan for agricultural reform will be developed (openness will eventually enhance the competitiveness of the agricultural sector)

### **1. Public Campaign Strategy**

#### **Objective**

- Shape general consensus among the South Korean public on the necessity of an FTA for the national economic strategy
- Educate the South Korean public on the potential benefits and costs of a South Korea-Chile FTA

- Stress the government efforts to address the agricultural sector
- Make consumer and labor groups more aware of benefits to them in terms of lower prices and the creation of jobs
- General consensus among the South Korean public in support of the South Korea-Chile FTA will prevent presidential candidates from using the negotiation as an election issue to pander for farm votes in December.

### **Recommendation**

MOFAT should propose a task force on South Korea-Chile FTA during the next session of Inter-Ministerial trade policy coordination committee (ITPCC), stressing the importance of a dynamic public campaign to achieve the early conclusion of South Korea-Chile FTA. Also, MOFAT might suggest promoting the South Korea-Chile FTA as a South Korea-Chile Regional Trade Agreement (RTA) to reduce public anxiety over free trade. The government should mobilize business groups, which will mainly benefit from the deal, to help promote the deal.

The task force will be comprised of the following ministries: the Ministry of Foreign Affairs and Trade (MOFAT), the Ministry of Finance and Economy (MOFE), the Ministry of Commerce, Industry and Energy (MOCIE), the Ministry of Agriculture and Forestry (MAF), and the Government Information Agency (GIA).

### **Action Plan**

- 1) If the proposal is approved, the task force will pursue the following media strategy:
  - Publish an education booklet on the benefits of the South Korea-Chile FTA (GIA)
  - Disseminate information through various government agency websites on such benefits of the FTA as job creation and economic growth
  - Run public TV ads and full-page newspaper ads (GIA, business groups)
  - Run the op-Ed in major news papers (MOFAT, MOCIE, MAF, MOFE)
  - Engage government officials in TV debates on the issue (MOFAT, MOCIE, MAF, MOFE)

2) The government should mobilize business groups of the South Korea-Chile FTA, such as the South Korea Trade Association and the Federation of South Korean Industries, to start their own media campaign. The business groups could run TV ads and full-page ads in major newspapers on free trade's benefits to the South Korean economy. The government should also urge state-sponsored research institutes like KIEP to submit articles to major newspapers and engage in public discussion on the benefits of a FTA to the South Korean economy.

3) The government should hold public hearings and seminars on the South Korea-Chile FTA. It should disseminate information brochures to the public regarding the benefits of FTAs and invite all stakeholders, NGOs, agricultural groups, etc., to the meetings for an exchange of opinions.

## **2. Domestic Consensus Building Strategy on Agricultural Liberalization**

### **Objective**

- Bring agricultural groups into dialogue
- Determine compensation for local farmers affected by South Korea-Chile FTA
- Develop a long-term agricultural reform policy to enhance the competitiveness of South Korea's agricultural sector and brace for WTO agricultural negotiations
- Build domestic consensus on agricultural market opening and gain support from the agricultural groups toward the South Korea-Chile FTA

### **Recommendation**

At the next session of ITPCC, MOFAT should propose the creation of a tri-party commission of representatives from government, business and agricultural groups to build consensus on the agricultural issue in South Korea-Chile FTA.

- The task of the commission is to reach an agreement among three parties on the following points, among others:
  - The agricultural sector will not oppose the deal and will engage in the process in a

constructive way

- The government will negotiate a gradual reduction of tariffs on agricultural products and will compensate affected farmers from the FTA.
- The business community will cooperate with the government to compensate the affected sector from the FTA.
- The business community to benefit from the FTA may agree to raise the so-called “FTA fund” to compensate the agricultural sector, especially the fruit industry.
- The commission will agree to specific compensation measures to enhance the competitiveness of the agricultural sector and accelerate agricultural reform.

### **Action Plan**

- Propose the idea to other ministries involved in the FTA negotiations: MAF, MOFE, and MOCIE
- Each ministry will consult with its constituent groups, that is, MAF with agricultural groups, and MOE and MOCIE with business groups
- If agreed upon by government agencies, agriculture, and business groups, MOFAT will present the proposal to the inter-Ministerial committee on trade policy coordination

### **3. Legislative Strategy (Election Strategy)**

#### **Objective**

- To raise awareness among potential presidential candidates of the importance of the FTA with Chile for South Korea’s national economic strategy
- To shift possible debate among candidates from whether to conclude the FTA to how to compensate South Korean farmers and how to reform the agricultural sector
- To pave the way for parliamentary ratification of a South Korea-Chile FTA regardless of the election outcome

#### **Recommendation**

If strategies 1) and 2) as stated above succeed, there will be less incentive for presidential

candidates to attack the current FTA negotiation. Still, the government must ensure that presidential candidates do not make the trade pact an issue to win farmers' votes in the upcoming December election. It is advised that the government adjust the pace of negotiation and postpone finalizing the deal until after the election.

### **Action Plan**

- Convince President Kim Dae-jung that if South Korea fails to finalize the deal, it will tarnish South Korea's national image and credibility in the international community
    - Suggest to the President that he dissuade ruling party candidates from publicly denouncing the FTA deal, and instead direct candidates to stress the government pledge to compensate farmers and develop an agricultural reform plan to enhance farmers' welfare.
  - Mobilize business groups to lobby both opposition and ruling party members to support the South Korea-Chile FTA, stressing the benefits of export markets in Chile and Latin America.
  - Request a meeting between government officials and the staffs of presidential candidates to educate them on the necessity of a South Korea-Chile FTA deal for South Korea's national economy.
    - Underscore that it is in the best interests of both candidates to address the agricultural sector constructively rather than promise farmers to thwart the FTA negotiation.
-

## **NEGOTIATION STRATEGY**

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### **Objective**

- Mitigate domestic farmers' concerns
- Narrow differences with Chile over the exclusion of agricultural products from the free trade agreement
- Finalize the agreement

### **Recommended Proposal on apples, pears, grapes**

To assuage farmers, the government might agree to a less beneficial concession plan for the manufacturing sector to achieve more concessions on agricultural, especially for the fruit industry.

Regarding the agricultural concession schedule,

- South Korea will not insist on excluding apples, pears and grapes
- Instead, the following can be suggested:
  - South Korea will consider seasonal tariffs on Chilean imported grapes
  - South Korea will agree to consider an extra-long tariff phase-out period of 15 years for apples and pears
  - South Korea will request that the agreement include special safeguard measures to protect against import surges for import-sensitive agricultural products.

### **Basic Arguments**

In negotiating with Chile on the recommended concession schedule, the government should base its positions on the following arguments:

- South Korea is not ready to accept Chile's demand that tariffs be abolished for all products, especially for agricultural items.
- Items particularly sensitive to imports were excluded or given extra-long tariff elimination periods in Chile's FTAs with countries like Canada and Mexico.
  - For example, in the Canada-Chile Agreement, Chile tariffs on milling wheat imported from Canada will be eliminated only after 17 years.

- The Chile-Mexico FTA excluded 46 commodities imported to Chile from Mexico (such as barley, wheat, flower, and seed oil), and 59 commodities (such as fisheries, diary products, and tobacco) imported to Mexico from Chile.
- It is politically impossible for the South Korean government to get ratification from parliament without special consideration for South Korea's agricultural sector. If our proposal is not met, South Korea has no choice but to stop the negotiation.
- Cancellation of negotiations for an FTA will bring about negative effects for both South Korea and Chile in terms of image and credibility within the international community.

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## Appendix 1: A Timetable of South Korea-Chile FTA Negotiations

1994	Chilean President Eduardo Frei visits South Korea.
1996	President Kim Young-sam visits Santiago.
Nov 1998	South Korea and Chile reach an agreement to establish an FTA at the bilateral summit talks of the APEC Leaders' Meeting.
April 1999	South Korean and Chilean trade officials meet in Seoul to prepare for a free trade agreement (FTA) between the two countries. Chile requests that the South Korean government allow the import of Chilean lemons. South Korea agrees to revise some of its quarantine regulations to help Santiago export more grapes and kiwis to South Korea.
Dec 1999	South Korea and Chile begin first round of negotiation on free trade pact based on the draft presented by Chile.
Jan 2000	Chile moves to curb imports of South Korean washers and refrigerators by filing anti-dumping suits against them.
Feb 2000	2nd round of negotiations is held in Seoul.
May 2000	3rd round of negotiation is held in Santiago.
Jun 2000	Chile launches its first-ever antidumping investigation into South Korean-made imports of expanded polystyrene.
Oct 2000	Chile decides to investigate dumping charges raised against South Korean refrigerators and washing machines.
Nov 2000	A ruling party lawmaker in South Korea says that he would push for parliamentary rejection of the FTA between South Korea and Chile for agricultural concerns.
Dec 2000	4th round of negotiations is held in Seoul.
Mar 2001	South Korean government asks Chile to put off negotiations, especially on matters related to farm products such as pears and apples, until the World Trade Organization (WTO) concludes its agriculture agreement.
Feb, 2002	South Korean government presents a latest proposal on tariff concession schedule. Chile is expected to offer its counterproposal in June/July of 2002.

## Appendix 2: Comparison of South Korea-Chile agriculture and bilateral trade 1999

Classification		South Korea	Chile
Population	Total Population (thousands, A)	46,858	15,287
	Agri-Population( thousands, B)	4,210	2,372
	Ration of B/A (%)	9.0	15.8
GDP	GDP (billion \$)	4,067	675
	Per capita GDP(\$)	8,680	4,492
	Agriculture Sector (including fishery and forestry) (%)	5.0	7.0
Land	Total Land (thousand Ha, C)	9,943	75,663
	Arable Land (thousand Ha, D)	1,899	2,294
	Ratio of D/C (%)	19.1	3.0
Production	Grain Production (thousands tons)	5,593	2,147
	Wheat	6	1,197
	Corn	79	624
	Potato	678	995
	Rice	5,263	41.0
	Barley	235	81.4
	Fruit and Vegetables (tons)	2,385	4,118
	Grape	470	1,575
	Apple	490	1,165
	Pear	259	350
	Peach	157	310
	Tomato	291	1,243
	Onion	936	263
Exports	Total Exports (US \$ billion, E )	1,437	161
	Agri-products (including meat, fishery, forestry, F)	16.8	29.7
	Ratio of F/E (%)	1.2	18.5
Imports	Total Imports(billion \$, G)	1,198	151
	Agri-Products (including meat, fishery, forestry, H)	73.9	11.7
	Ratio of H/G (%)	6.2	7.7

Source : Ministry of Agriculture and Fishery, South Korea

**Appendix 3: Current Positions of Major Government Agencies, Interest Groups and NGOs on the FTA**

Positions	Interest groups
Strongly support	Research Institutes Ministry of Foreign Affairs and Trade
Positive	Chaebols The Federation of South Korean Industries Ministry of Finance and Economy Ministry of Industry and Energy The Blue House(The President)
Neutral	Conservative press Political parties/ruling and opposition party
Negative	Ministry of Agriculture and Fishery Citizen groups Progressive press Labor unions
Strongly oppose	National Farmers' Association

**Appendix 4: Major Stakeholder Analysis Chart for a South Korea-Chile FTA**

People	Interest	Options	Batna	Obj.Criteria
<u>South Korea</u>				
Ministry of Foreign Affairs and Trade	<ul style="list-style-type: none"> <li>- Successfully conclude the first FTA</li> <li>- Engage in economic and trade diplomacy to enhance economic competitiveness</li> <li>- Maintain and strengthen friendly relations with Chile</li> <li>- Ease concern about MOFAT's negotiating credibility</li> </ul>	<ul style="list-style-type: none"> <li>- Wrap up the negotiation regardless of farmers' opposition by presenting more compromising concession schedule</li> <li>- Generate unity among the government agencies</li> <li>- Generate public support for the FTA process</li> <li>- Provide compensation measures for the losers from the FTA</li> <li>- Stop the negotiation and to pursue other FTAs</li> <li>- Focus on WTO new round talks</li> </ul>	Stop the negotiation and to pursue other FTAs	<ul style="list-style-type: none"> <li>- Chile-Mexico, Chile-Canada FTA agreement and other regional agreements</li> <li>- Economic analysis report on South Korea-Chile FTA by KIEP, KREI</li> </ul>

<p>Business groups Chaebols, The federation of South Korean Industries, manufacturing companies</p>	<ul style="list-style-type: none"> <li>- The successful conclusion of the FTA</li> <li>- Gain economic benefits from the FTA and increase exports to Chile and other Latin markets</li> </ul>	<ul style="list-style-type: none"> <li>- Support the FTA negotiations</li> <li>- Proactively pursue PR activities for the FTA to garner public support</li> <li>- Request the government to engage in further FTAs with larger economies such as the US</li> <li>- Provide compensation measures for the losers from the FTA</li> <li>- Lobby the politicians to support the FTA process</li> <li>- Enhance competitiveness in world markets</li> </ul>	<p>Urge the government to engage in other FTAs</p>	<ul style="list-style-type: none"> <li>- Chile-Mexico, Chile-Canada FTA agreement and other regional agreements that Chile has concluded</li> <li>- Economic analysis report on South Korea-Chile FTA by KIEP</li> </ul>
<p>Ministry of Finance and Economy, Ministry of Industry and Energy</p>	<ul style="list-style-type: none"> <li>- Successfully conclude the FTA</li> <li>- Increase national economic growth</li> <li>- Boost exports</li> <li>- Protect South Korean business in world markets</li> <li>- Accelerate the economic reform restructuring process</li> </ul>	<ul style="list-style-type: none"> <li>- Continue to support the FTA process</li> <li>- Accelerate the voluntary economic reform process</li> <li>- Provide compensation measures for the losers from the FTA</li> <li>- Stop the negotiation and pursue other FTAs</li> </ul>	<p>Stop the negotiation and pursue other FTAs</p>	<ul style="list-style-type: none"> <li>- Chile-Mexico, Chile-Canada FTA agreement and other regional agreements that Chile has concluded</li> <li>- Economic analysis report on South Korea-Chile FTA by KIEP</li> </ul>
<p>The Blue House(the President)</p>	<ul style="list-style-type: none"> <li>- Continue economic reform</li> <li>- Maintain economic satiability and growth</li> <li>- Concern with its economic legacy</li> </ul>	<ul style="list-style-type: none"> <li>- Continue to support the FTA negotiation</li> <li>- Actively engage in the government PR campaign to generate support of the public toward the FTA process</li> <li>- Remain neutral to the FTA process</li> <li>- Stop the negotiation</li> </ul>	<p>Remain neutral to the FTA process</p>	<ul style="list-style-type: none"> <li>- Chile-Mexico, Chile-Canada FTA agreement and other regional agreements that Chile has concluded</li> <li>- Economic analysis report on South Korea-Chile FTA by</li> </ul>

	<ul style="list-style-type: none"> <li>- Support the ruling party presidential candidate in the upcoming presidential election</li> </ul>			KIEP
The Ruling Party (Presidential candidates)	<ul style="list-style-type: none"> <li>- Win presidential election</li> <li>- Avoid alienating the farmer vote</li> <li>- Express concern for national economy</li> </ul>	<ul style="list-style-type: none"> <li>- Keep FTA from being an election issue</li> <li>- Support the FTA from the national economic strategy</li> <li>- Differentiate from the incumbent president policy and to denounce the FTA negotiation</li> </ul>	Remain neutral to the FTA process	Public opinion poll
The Opposition Party (Presidential Candidates)	<ul style="list-style-type: none"> <li>- Win presidential election</li> <li>- Avoid alienating the farmers' vote</li> <li>- Show concern for national economy</li> </ul>	<ul style="list-style-type: none"> <li>- Criticize the ruling party for the current FTA deal and to promise to stop the negotiation</li> <li>- Keep FTA from becoming an election issue</li> <li>- Support the FTA from the national economic strategy</li> </ul>	Denounce the FTA and promise farmers to stop the negotiation	Public opinion poll
Ministry of Agriculture and Fishery	<ul style="list-style-type: none"> <li>- Protect the domestic agricultural sector</li> <li>- Represent domestic farmers' interests</li> <li>- Express concern about the government policy from the national</li> </ul>	<ul style="list-style-type: none"> <li>- Present the compromising schedule on the agricultural sector and to support the early conclusion of the FTA with Chile</li> <li>- Strongly oppose the FTA and urge other government agencies to stop the negotiation until after the WTO talks</li> <li>- Secure compensation measures from the business groups for the losers from the FTA</li> <li>- Provide economic development plan for the agricultural sector</li> </ul>	Secure compensation measures for the farmers affected by the South Korea-Chile FTA	<ul style="list-style-type: none"> <li>- Chile-Mexico, Chile-Canada FTA agreement and other regional agreements on agricultural sector</li> <li>- Economic analysis report on South Korea-Chile FTA by KIEP and KREI</li> <li>- WTO agricultural negotiations</li> </ul>

	<p>economic strategy</p> <ul style="list-style-type: none"> <li>- Express concern about the unity among the government agencies</li> </ul>			
Consumer /Citizen group	<ul style="list-style-type: none"> <li>- Support the farmers' cause</li> <li>- Access cheap imports</li> </ul>	<ul style="list-style-type: none"> <li>- Continue to oppose the FTA</li> <li>- Support the FTA</li> <li>- Prefer the status quo</li> </ul>	Prefer the status quo	<ul style="list-style-type: none"> <li>- Economic analysis report on South Korea-Chile FTA by KIEP and KREI</li> </ul>
National Farmer's Association	<ul style="list-style-type: none"> <li>- Protect domestic farm industry</li> <li>- Retain income</li> <li>- Protect domestic fruit industry</li> <li>- Oppose agricultural market opening</li> <li>- Enhance domestic agricultural sector's competitiveness</li> </ul>	<ul style="list-style-type: none"> <li>- Block the ongoing South Korea-Chile FTA</li> <li>- Continue demonstrations</li> <li>- Secure compensation for affected farm industry from the FTA agreement</li> <li>- Exert lobbying efforts on politicians</li> </ul>	Block the all FTA talks	<ul style="list-style-type: none"> <li>- Chile-Mexico, Chile-Canada FTA agreement and other regional agreements on agricultural sector</li> <li>- Economic analysis report on South Korea-Chile FTA by KIEP and KREI</li> <li>- WTO agricultural negotiations</li> </ul>

People	Interest	Options	Batna	Obj.Criteria
<u>Chile</u>				
Ministry of Foreign Affairs	<ul style="list-style-type: none"> <li>- Successfully conclude the FTA with South Korea</li> <li>- Conclude FTAs with APEC countries by 2010</li> <li>- Maintain and strengthen economic and political relations with South Korea</li> <li>- Ease concern about Chilean credibility in international trade community</li> <li>- Enhance economic competitiveness and to expand Chilean exports market</li> </ul>	<ul style="list-style-type: none"> <li>- Agree on less beneficial agricultural concession schedule and finalize the deal</li> <li>- Stop the negotiation and to conclude the FTA with the US and the EU</li> <li>- Pursue alternative FTAs with other Asian countries</li> </ul>	Pursue alternative FTAs with other Asian countries	<ul style="list-style-type: none"> <li>- Chile-Mexico, Chile-Canada FTA agreement and other regional agreements</li> <li>- Economic analysis report on South Korea-Chile FTA by research institutes</li> </ul>
Chile manufacturing company groups	<ul style="list-style-type: none"> <li>- Protect domestic industry from competitive South Korean manufacturing goods</li> <li>- Retain domestic markets to South Korean companies</li> <li>- Secure economic compensation for possible income loss from the FTA deal</li> <li>- Enhance competitiveness and expand exports in foreign market</li> </ul>	<ul style="list-style-type: none"> <li>- Oppose the FTA negotiations</li> <li>- Urge the government to secure more concession on domestically sensitive manufacturing sector such as textile and electronic goods.</li> <li>- Secure compensation measures for the losers from the FTA deal</li> <li>- Request the government to focus on FTAA negotiations and other FTAs with the US and the EU</li> <li>- Enhance its competitiveness against the South Korean companies</li> </ul>	Enhance competitiveness against the South Korean companies	<ul style="list-style-type: none"> <li>- Chile-Mexico, Chile-Canada FTA agreement and other regional agreements that Chile has concluded</li> <li>- Economic analysis reports about the benefits of South Korea-Chile FTA</li> </ul>

Chile Agricultural Groups	<ul style="list-style-type: none"> <li>- Increase agricultural exports to South Korea</li> <li>- Secure best beneficial concession schedule on the Chilean agricultural products</li> </ul>	<ul style="list-style-type: none"> <li>- Continue to support the FTA process</li> <li>- Agree on less beneficial agricultural concession plan</li> <li>- Stop the negotiation and pursue other FTAs</li> </ul>	Support other FTA initiatives	<ul style="list-style-type: none"> <li>- Chile-Mexico, Chile-Canada FTA agreement and other regional agreements that Chile has concluded</li> </ul>
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## **Exhibit 1: Briefing Memo to the Prime Minister**

### **Memo**

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To: The Prime Minister, The Inter-Ministerial Trade Policy Coordination Committee (ITPCC)  
From: Minister for Trade, Ministry of Foreign Affairs and Trade  
Date: April 30, 2002  
Re: South Korea-Chile FTA

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### **Issue**

The South Korea-Chile FTA negotiation, launched in 1998, has stalled at the final phase due to persistent opposition from the agricultural sector. It is vital that the government successfully conclude the free trade agreement with Chile. Not only will it bring economic benefits, but it carries the strategic significance of opening further FTAs with larger economies in the long run. Three major domestic obstacles remain to early conclusion of the trade pact: 1) fierce opposition from the farmers group, 2) the possibility of Presidential candidates politicizing the FTA in the upcoming presidential election, and 3) negative public opinion. There is an urgent need for the government to launch a concerted effort to overcome these domestic challenges and lead the FTA to completion.

### **Background**

In 1998, the government, with the ultimate goal of building an “open trading country,” resolved to pursue free trade agreements (FTAs) with major trade partners. The main objective was to overcome the structural weakness of the South Korean economy exposed by the 1997 financial crisis, and to adapt to the changing economic environment, i.e. the recent trend of growing regional integration in the world economy. In November 1998, ITPCC formally announced that South Korea would seek an FTA with Chile and explore the possibility of FTAs with other partners like the US and Japan.

Since the decision, the government has been negotiating its first FTA with Chile. The process was stymied after four rounds of negotiations due to a wide difference on the tariff concession schedule between the two countries, especially regarding agricultural products. South Korea insists that such sensitive fruits as grapes, apples, and pears be excluded from tariff elimination, while Chile calls for South Korea to abolish tariffs on all Chilean products, including agricultural goods, within 10 years of signing an FTA.

The South Korean fruit industry is very sensitive to FTA talks. Though the impact of the trade pact on South Korea’s entire agricultural sector is likely to be small due to seasonal differences between the two countries, local fruit farmers will likely be most affected, as Chilean apples, grapes and kiwi fruits are among the worlds finest. It is not possible to completely exclude the agricultural sector in South Korea-Chile FTA as requested by domestic farmers. Consequently, given the sensitivity of South Korean fruit farms, the government has tried to negotiate a gradual market opening for such products. To address South Korean farmers’ concerns, however, the government must devise more realistic compensation measures for seriously affected local farmers.

The lack of understanding among the general public toward the FTA process is another problem. After the financial crisis, there was growing acceptance among the public on the necessity for liberalization and economic reform. Influenced by the farmers' protests, however, public opinion has turned negative toward the South Korea-Chile FTA. To prevent the FTA from becoming a political issue for presidential candidates to win farmers votes, the government should proactively promote to the public the necessity of the FTA and its benefits to the South Korean economy.

The bilateral trade pact is expected to have a positive economic effect for South Korea. It is likely to boost South Korean exports by \$660 million and improve South Korea's welfare by \$960 million, while increasing South Korean export opportunities in Latin American markets. Chile's open trade policy and experience in concluding FTAs with other countries would provide invaluable experience to South Korea, not only in its attempts to liberalize its own economy, but also in its pursuit of FTAs with larger economies like Japan and the US. In light of the growing international suspicion that South Korea's impetus for economic reform began after the economic crisis declined, concluding the South Korea-Chile FTA will confirm South Korea's commitment to economic reform and an open trading nation.

### **Recommendation**

To build domestic consensus for the South Korea-Chile FTA, it is recommended that the government 1) set up a PR task force on the South Korea-Chile FTA to pursue a dynamic public campaign and to shift public discussion from whether to conclude the deal to how to compensate potential losers, and 2) create a tripartite commission of government, business and agricultural groups to build consensus on agriculture for the South Korea-Chile FTA, and to draw specific compensation measures for the affected farmers from the deal.

/The End/

**Regionalism and South Korea-Chile FTA**

The world economy has become more integrated with the multilateral system of the WTO, and regionalism has added yet another layer of integration. The number of regional trade agreements has rapidly increased in the 1990s. The European Union now has 29 regional and bilateral free trade or special customs agreements, and is currently negotiating with 12 more countries. NAFTA members (the US, Canada and Mexico) are entering into FTA negotiations that aim to link the North and South American regions under one trade entity. Even Japan has concluded a free trade agreement with Singapore in 2001.

While South Korea's major trading partners are joining regional trade agreements to maximize economic gains—there are 130 regional free trade and customs agreements in the world—South Korea has joined none, and thereby is the only WTO member, save China and Taiwan (new entrants to the WTO), without a regional trade agreement. This is a worrisome development for the South Korean economy because regional trade agreements involving South Korea's trading partners leave South Korean exporters at a competitive disadvantage in foreign markets.

The successful conclusion of the South Korea-Chile FTA is very important. It would mark South Korea's first ever free trade agreement and would bring sizable benefits to the South Korean economy. The bilateral trade pact would boost South Korean exports by \$660 million and improve South Korea's welfare by \$960 million. It also would increase future export opportunities in the Latin American markets. South Korea could learn from Chile's experience with open trade policy and further liberalize its own economy, pursuing FTAs with larger economies like Japan and the US.

Contrary to domestic farmers' arguments, the potential harm to South Korea's agricultural sector is small. The government is attempting to negotiate gradual agricultural market opening for sensitive domestic agricultural products to minimize shocks to local farmers, while also compensating farmers who would be hurt by the South Korea-Chile FTA. Opening South Korea's agricultural market to free trade is painful, given the agricultural sector's poor competitiveness and undeveloped structure. With WTO agricultural negotiations underway, however, it is inevitable that South Korea will soon face further opening of the agricultural market in the near future. It is not desirable that South Korea avoid the market opening and resort to protection measures. Rather, it is time that South Korea accelerates agricultural restructuring to enhance the competitiveness of the sector in the long run.

From the standpoint of national economic strategy, South Korea has few alternatives than to engage in regional trade agreements. Total foreign trade represents about 73 percent of South Korea's GDP in 2000. If South Korea does not participate in FTAs, it loses a golden opportunity to expand economic ties with trading partners and promote further economic growth and development.

Contributed by Sunyoung Kim  
Deputy Director for multilateral trade cooperation division, MOFAT

### **Exhibit 3: Sample letter to the Ministry of Agriculture and Fishery**

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To: Ministry of Agriculture and Fishery

From: Ministry of Foreign Affairs and Trade

Date: April 30, 2002

Re: Recommended proposal on sensitive fruit products in the South Korea-Chile FTA

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1. The Chilean foreign ministry has informed MOFAT that Chile wants to resume official talks on the FTA negotiation to resolve differences over the tariff concession schedule between the two countries. In the letter, the Chilean side states that it is willing to allow unhindered access to manufactured goods if we open further our agricultural sector.
2. Given the positive response from the Chilean side, our government needs to be more flexible on the agricultural concession schedule to narrow differences with Chile and complete the FTA as soon as possible.
3. In this regard, MOFAT proposes that the government consider an extra-long period for tariff phase-out of sensitive fruit products rather than excluding apples, pears and grapes from the agricultural concession schedule. The following is the recommended proposal for the contentious fruits products:
  - Apply seasonal tariffs on Chilean imported grapes
  - Apply an extra-long tariff phase-out period of 15 years for pears and apples.
  - Include special safeguard measures against possible import surges for import-sensitive agricultural products
4. Please notify MOFAT by May 8 of MAF's position on the newly recommended proposal.

/The End/

**Exhibit 4: Press release on the formation of a tripartite commission on the agricultural issues in South Korea-Chile FTA**

**Ministry of Foreign Affairs and Trade**

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**The government, business and agricultural groups meet to discuss compensation measures for farmers affected by the South Korea-Chile FTA**

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1. In an effort to build domestic consensus over the agricultural market opening in the South Korea-Chile FTA talks, the government has decided to create a tripartite commission among the government, business and agricultural groups. The announcement came after the Inter-ministerial Trade Policy Coordination Committee held a meeting to discuss a strategy to successfully conclude the South Korea-Chile FTA. The FTA talks had recently stagnated due to strong opposition from the agricultural community.
2. The commission will be charged with reaching an agreement among government, business and agricultural groups on specific compensation measures for domestic farmers who are made vulnerable by the trade agreement. In addition, the government will consult with agricultural groups to prepare a tariff schedule on agricultural products to be presented to Chile at the next round of FTA negotiation. Furthermore, the commission will discuss measures to enhance the competitiveness of the South Korean agricultural sector in response to increasing agricultural market opening. It will present a long-term economic development plan for the agricultural sector. Further details of the structure and logistics of the commission will be decided when the three parties hold their first meeting on May 30, 2001 at the government headquarters.
3. If an agreement is reached among the three parties, it is hoped that MOFAT will present a more flexible concession proposal to Chile and thus succeed in finalizing the deal at the next round of negotiations. Since the fourth round of talks, the South Korea-Chile negotiation has frozen due to a wide difference on the tariff concession schedule between the two countries, especially regarding agricultural products. South Korea insisted that such sensitive fruits as grapes, apples, and pears be excluded from tariff elimination, while Chile called for South Korea to abolish tariffs on all Chilean products, including agricultural goods, within 10 years of signing an FTA.
4. If concluded, the South Korea-Chile FTA will mark South Korea's first ever free trade agreement—a benchmark in South Korean history.

/The End/