European Union – Korea Free Trade Agreement Sustainability Impact Assessment: Phase Two

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  - Financial Services
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Overview of Phase Two

- Analysis of Sectors
  - Analysis of specific segments, partial equilibrium analysis
  - Economy wide modelling of specific sectoral impacts
  - Incorporation of “behind the border”, FDI and technology effects
  - Sustainability impact assessment

- Analysis of horizontal issues
  - Identification of sectoral aspects
  - Sustainability assessment

- Overall impacts
Automotive Sector

- Growing role of FDI in the base case, e.g., Renault Samsung and Hyundai/Kia investments in Central Europe.
- Global context for automobile production and trade is important:
  - Spreading technology development costs over volume.
  - Emergence of China, India, SE Asia, Russia in production.
- **Economic Impact:** Model based estimates show large increases in trade volume but our estimates are much lower than Copenhagen economics study.
- Market segment analysis with competitive responses by EU producers, technology changes, third country effects, and FDI shows less impact on trade volumes but offers potential economic gains.
- Implications of preferences under KORUS and potentially with Korean FTA with Japan.
Automobile Sector

- Dealing with behind the border issues especially technical regulations and standards are important to the sector
- Social Impact: relative shift to skilled labour from unskilled labour in EU although overall impact is modest
- Difficult to separate the incremental impact of the EU Korea FTA on employment in the sector from other factors
- Overall social impacts and adjustment are limited with tariff phasing and dealing with technical regulations
- Environmental Impacts: The EU and Korean industry face similar challenges in reducing CO2 emissions and achieving higher levels of fuel efficiency.
Agri-food Sector: Economic Impacts

- Earlier FTAs such as Korea-Chile have had significant effects in certain sectors such as wine.
- An EU-Korea FTA is not expected to have as much of an effect on the agriculture and fishery industries of Korea as the KORUS FTA.
- The EU is expected to concentrate on expanding exports of processed foodstuffs such as alcoholic beverages and processed dairy products such as butter and cheese.
- Any increase in the export of Korean food products to the EU is expected to be small, and concentrated in non-sensitive areas such as ramyon (instant noodle) and kimchi.
**Agri-food Sector: Social and Environmental Impacts**

- The expansion of specific exports from the EU such as dairy products, pork, wine or spirits could have regional impacts on employment in the exporting regions in the EU.
- Some restructuring of the Korean food processing sector may be necessary, but such adjustment would be already occurring with KORUS.
- The adverse social impact in Korea would be on older workers in segments of the agri-food sector.
- **Environmental Impacts:** Given the relatively small scale of the potential export expansion and the associated production response, it is doubtful that there would be significant environmental impacts. EU exports to Korea currently account for about 1.5% of the EU total, and about 0.1% of total industry turnover.
Financial Services

- In our view the main effect of liberalisation of financial services will be increased FDI.
- Economic Impact: The Copenhagen study foresees contraction in Korean financial services sector and expansion of EU exports.
- In our analysis output will increase in both EU and Korea in financial services.
Financial Services

- **Social Impact:** If FDI is taken into account then the effects of Korean financial services liberalisation are likely to be an increase in efficiency and in output and economic activity. This will lead to increased demand for skilled labour in the financial services sector in Korea.

- **Environmental Impact:** effect of financial liberalisation on environment is ambiguous since the liberalisation has environment impacts through many channels.

- **Direct environmental impact** is extremely difficult to assess as financial services are typically low-energy consumption and low-CO2 emitters industries. Thus, expansion of the share of financial services in the economy can be said to have a positive environmental impact.

- **When financial liberalisation leads to higher economic growth and employment, it may have negative impacts on environment**
Environmental Goods and Services

- Korea has made significant progress in environmental protection and pollution control especially in the last decade since joining the OECD.
- As a densely populated urbanised society Korea has further needs for environmental protection.
- Korea depends heavily on imported energy and renewable energy could play a more active role.
- Environmental Goods are included in machinery sectors where Korea had a trade surplus and shows strong output gains under the Copenhagen study.
- Environmental goods are products where the tariffs and lower and the EC has a positive trade surplus in a number of products and in environmental services.
- Economic impacts: Strong pattern of overlapping intra-industry trade, which suggests mutual benefits from trade expansion.
- Environmental impacts: Liberalisation of environmental goods and services offers benefits in exchange and development of clean technologies.
Rules of Origin

- It is appropriate to have high content requirements for Pan European rules with Cumulation for countries contiguous with EU or for regional blocs.
- High content requirements are a challenge for Korea due to the structure of the economy and distance from the EU.
- High content requirements are more warranted in sectors with high and dispersed third country tariffs.
Technical Regulations and Standards

- Technical regulations and standards are important in specific sectors
  - Automobiles
  - Cosmetics
  - Electronics

- Technical regulations and standards should make greater use of international norms

- Development of Mutual Recognition of Conformity Assessment
**Intellectual Property Rights**

- Legal framework in Korea needs to be strengthened in a few areas such as Regulatory Data Protection and patent linkage.
- Better enforcement of IPRs including for counterfeit goods is a priority.
Investment

- Increased Foreign Direct Investment will contribute to economic benefits from the FTA
- Increased FDI is likely to be the most significant mode for trade in services
- Increased FDI can also contribute to aggregate investment and improved economic growth
Conclusions: Economic Impacts

- The overall economic effects of the EU-Korea FTA are likely to be modest because both partners already have very open economies and highly integrated into the world economy.

- Second, the emergence of Korea as a developed economy and the degree of overlap that has developed in the industry structure for goods and for services between the EU and Korea suggests that there are increased opportunities for intra-industry specialisation, scale effects, pro-competitive effects and induced investment and innovation effects.
Social Impacts

- There are unlikely to be large inter-industry shifts in output and employment that could lead to disruption of labour markets at either a national or regional level.

- In the medium to longer term both the EU and Korea face common challenges to increase productivity and labour force participation and employment rates in order to sustain economic growth with a stable and aging population.
Environmental Impacts

- The convergence in economic development levels is leading to greater commonality in concerns about protection of the environment between the EU and Korea.
- The potential economic benefits of increased productivity and enhanced technology could translate into the development of, and the increased use and diffusion of clean technologies.
Next Steps

- Consultations with Industry Groups and Civil Society
- Revised Phase Two Report
- Phase Three Report