CHINA-SOUTH KOREA FREE TRADE AGREEMENT

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Executive Summary

1. China and South Korea signed a free trade agreement (FTA) on 1 June 2015 in Seoul. The FTA is scheduled to be implemented in late 2015 or early 2016 after obtaining approval from their respective legislatures.

2. The implementation of the FTA is expected to generate economic gains, especially for South Korea. South Korea's gross domestic product (GDP) will grow by an additional 0.96 percentage point while China's GDP growth will be 0.34 percentage point higher, according to the respective official estimates.

3. Bilateral trade is more important for South Korea as it is more dependent on China for its exports. The country ran a consistent and rising trade surplus with China from US$1.7 billion in 1995 to US$55 billion in 2014.

4. The FTA covers a large majority of the product items. In 20 years, 92% of South Korea's export items and 93% of China's will enjoy zero tariffs in bilateral trade. Several items are excluded, including automobile, petrochemical products and rice. The slow pace of full implementation and the limited width of tariff cut suggest that bilateral trade in goods is not key to this bilateral FTA.

5. A follow up negotiation on investment and services will take place in two years, implying that the two sides aim to promote greater opening in these areas. South Korea's investment in China is much higher than China's investment in South Korea, but the latter has risen more rapidly in recent years.

6. The FTA allows the South Koreans to shift its exports from intermediary goods to consumer goods and services. It will also facilitate Chinese investors to acquire Korean technology and take advantage of Korea's FTAs with the European Union and the United States to sell their products to these two markets.

7. The two sides have also committed to cooperate in other areas to enhance bilateral trade and industrial integration. In particular, the inclusion of products

manufactured in the Kaesong Industrial Complex (located in North Korea) in the FTA is expected to benefit the growth and stability in the Korean peninsula.

8. The bilateral FTA may allow China to pressure Taiwan to accelerate the cross-strait service trade deal and Japan for the trilateral FTA. It could also help China promote the development of Regional Comprehensive Economic Partnership and Free Trade Area of the Asia-Pacific.

9. The FTA is also useful for advancing the two countries' regional plans. China expects the FTA to pave the way for more trade pacts with countries in the "Belt and Road" initiative whereas South Korea is hoping to realise its Eurasia initiative through China.

10. The emphasis on investment and services in this FTA shows China's capacity and willingness to conclude a "higher standard" agreement, a step nearer to the US-led Trans-Pacific Partnership.