

Korea–Australia Free Trade Agreement

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The Korea–Australia Free Trade Agreement (KAFTA) was signed on 8 April 2014. Both countries are working toward ratifying the agreement and completing domestic treaty procedures to allow the agreement to come into force.

Australia is the fourth largest supplier of agricultural products to the Republic of Korea, accounting for around 10 per cent of the Republic of Korea's total agricultural imports. In 2013 Australian exports to the Republic of Korea were valued at around \$1.9 billion. The United States is the largest supplier of agricultural products to the Republic of Korea, accounting for around 23 per cent of the import market. Other competitors include China (12 per cent), Brazil (11 per cent) and Argentina (4 per cent). The major agricultural commodities imported by the Republic of Korea are maize, wheat, beef, livestock feed, sugar and pig meat.

This note provides an overview of the key agricultural outcomes of KAFTA, with a scenario analysis of potential change in Australian beef and cheese exports to the Republic of Korea.

Key outcomes of KAFTA

Once KAFTA is implemented, customs duties on most agricultural commodities imported from Australia will be progressively reduced to zero over periods of up to 20 years (see table). Tariffs on some products will be eliminated immediately, including wine and wheat (excluding seed). KAFTA covers most agricultural products. However, some commodities have been excluded, including rice, ginseng, honey, skim and whole milk powders, streaky pork and selected horticultural products including walnuts, blueberries, onions, shallots, garlic, apples, pears and watermelon. KAFTA will also provide duty-free quotas for several agricultural products, including sugar, barley, butter and cheese.

Australian cheese imports to the Republic of Korea will be given a tariff-free quota starting at 4630 tonnes. This is equivalent to around 80 per cent of the Republic of Korea's cheese imports from Australia in 2013. The quota will increase by 3 per cent a year until year 13 of the implementation period, at which point cheddar cheese imported from Australia will be tariff free and no longer require access to the quota. As a result, the quota will fall from 6409 tonnes in year 13 to 4443 tonnes, whereupon it will resume growing by 3 per cent a year to 5001 tonnes in year 18. In that year, imported fresh cheese (such as mozzarella and cream cheese) and processed cheese that is not grated or powdered will have tariff-free access. By year 20, all imports of Australian cheese will be duty-free.

Exporters and producers of beef, cheese, butter, malting barley and unroasted malt are expected to benefit most from the agreement, as these commodities are currently subject to relatively high import tariffs. In contrast, potential gains to Australian exporters and producers of commodities such as wheat, cotton, wool and sugar are expected to be modest, since they already benefit from low tariffs or tariff-free access to the Republic of Korea.

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Key outcomes for agriculture under the Korea–Australia Free Trade Agreement

Commodity	Outcome
Beef	Removal of 40 per cent tariff on beef and 18 per cent tariff on bovine offal over 15 years. Import tariffs for edible offal, including from bovine animals, will be phased out from the current applied rate of 18 per cent, as will the 72 per cent tariff on processed beef products.
Sugar	Removal of 3 per cent tariff on raw sugar on implementation of the agreement. Removal of 35 per cent tariff on refined sugar evenly over 18 years.
Cheddar cheese	Removal of 36 per cent tariff evenly over 13 years.
Grated and powdered cheese and speciality cheeses	Removal of 36 per cent tariff evenly over 20 years.
Mozzarella, cream cheese, processed cheese and all other cheese	Removal of 36 per cent tariff evenly over 18 years.
Butter	Removal of 89 per cent tariff over 15 years. Over this period, Australia will receive access to a tariff-free quota. The quota is 113 tonnes in the first year of the agreement and increases to 146 tonnes by the end of the tariff phase-out period in 2029.
Sheep and goat meat	Removal of 22.5 per cent tariff on sheep and goat meat over 10 years.
Pork	Removal of 22.5 per cent tariff in 5–15 years.
Wine	Removal of 15 per cent tariff on wine on implementation of the agreement.
Horticulture	Removal of 24 per cent tariff on cherries, 8 per cent tariff on almonds and 21 per cent tariff on dried grapes on commencement of the agreement. Tariffs ranging from 27 per cent to 54 per cent on products such as macadamia nuts, fruit juices, mangoes, asparagus and lentils will be removed over 3–10 years. Tariffs will be eliminated during Australia's exporting seasons on potatoes for chipping (Australia's largest horticultural export with current tariff of 304 per cent), oranges (50 per cent), fresh table grapes (24 per cent) and mandarins (144 per cent).
Wheat	Removal of 1.8 per cent tariff on wheat on commencement of the agreement.
Malt and malting barley	The Republic of Korea will provide a growing duty-free quota for malt and malting barley and remove out-of-quota tariffs of 269 per cent on malt and 513 per cent on malting barley over 15 years. During that period, Australia will have access to a single tariff-free quota across both goods. The quota is 10 000 tonnes in the first year of the agreement and will increase to almost 13 000 tonnes by the end of the tariff phase-out period in 2029.
Oilseeds	Removal of 8 per cent and 10 per cent tariffs on canola oil products and 3 per cent tariff on cottonseed over 15 years.
Seafood	Key products, such as southern bluefin tuna (current tariff of 10 per cent) and rocklobsters (20 per cent), will enter the Republic of Korea duty-free after three years.

Source: Australian Department of Foreign Affairs and Trade 2014, 'Korea–Australia Free Trade Agreement. Quick guide: key agricultural products outcomes', available at dfat.gov.au/fta/kafta/guides/quick-guide-key-agricultural-products-outcomes.html

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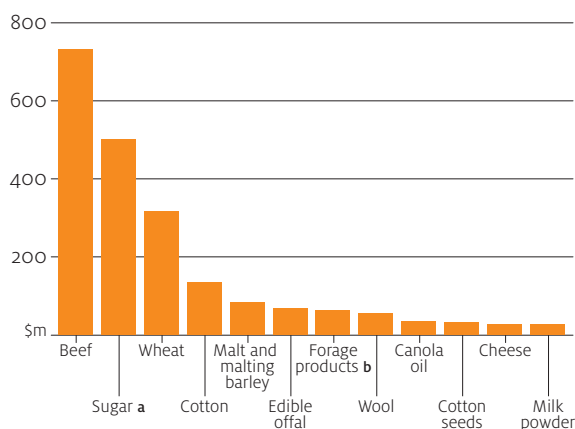
Safeguard measures

Some commodities, including beef, malting barley and unroasted malt, are subject to agricultural safeguard measures. The Republic of Korea can apply these measures if it determines that imports of Australian product are increasing at a rate that may cause serious injury to the Korean domestic industry. A safeguard measure can be activated when imports in a given year exceed a determined trigger volume. Under KAFTA, the trigger volume is scheduled to grow at 2 per cent a year. If the trigger volume is reached, import tariffs as high as the most favoured nation (MFN) tariff may be applied to any volume of imports in excess of the trigger. Under Article 6.7 of the KAFTA agreement, these duties may only be maintained until the end of the calendar year in which they are applied. This period allows for prevention or remedy of any economic injury to the Korean industry. The safeguard can be reapplied in the following year if the trigger is again exceeded. Under KAFTA, the safeguards for beef, unroasted malt and malting barley are removed in year 16 of the agreement.

Australian exports of key commodities to the Republic of Korea

Australia's total agricultural exports to the Republic of Korea were valued at around \$1.9 billion in 2013. The major exported commodities were beef (\$733 million), wheat (\$317 million) and cotton (\$134 million). Sugar exports were also significant, valued at \$502 million in 2012, the last year for which data are available.

Major Australian agricultural exports to Republic of Korea, 2013



Note: ^a The value of Australian sugar exports to the Republic of Korea is from 2012, the last year for which data are available. ^b Forage products include lupins, hay and chaff, lucerne and vetch.

Source: ABARES; Australian Bureau of Statistics, *International trade, Australia*, cat. no. 5465.0, Canberra

Beef

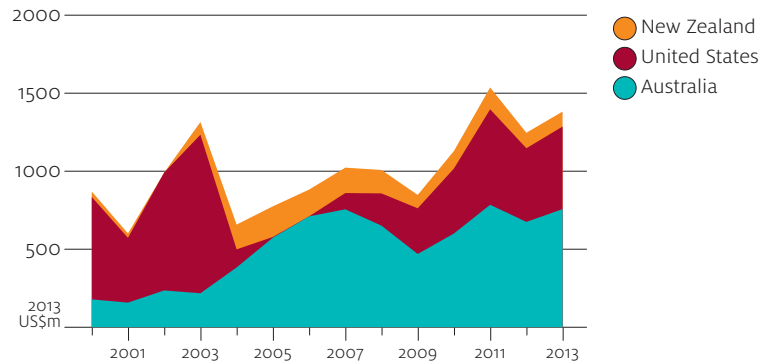
In 2013 the Republic of Korea was Australia's third largest export market for beef by value. Australia has been the main supplier of beef to the Republic of Korea since 2004, following a ban on US beef after an outbreak of bovine spongiform encephalopathy in the United States. However, since the ban was lifted in 2007,

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the United States has partially regained its market share. In 2013 beef imports by the Republic of Korea totalled around US\$1.4 billion, of which Australia accounted for 55 per cent and the United States 38 per cent. Australia's main competitors in that market are the United States and New Zealand, from which the Republic of Korea imported around US\$529 million and US\$96 million, respectively, in 2013.

Republic of Korea beef imports by source



Source: United Nations Comtrade Database, 2014

The Republic of Korea and the United States signed the Korea–United States Free Trade Agreement (KORUS) in late 2011. Under this agreement, the MFN tariff of 40 per cent will be phased out evenly between 2012 and 2026. The applied rate in 2014 is 31.99 per cent. This gives US beef preferential access to the Republic of Korea compared with Australia, which remains subject to the MFN rate until 2015.

Cheese

Cheese imports by the Republic of Korea have tripled over the past decade, to US\$403 million in 2013. This reflects strong growth in consumer demand and constrained domestic production. Cheese consumption has increased mostly for mozzarella and cheddar cheeses as a result of the growing popularity of fast food chains. These cheese types are mostly sourced from the United States.

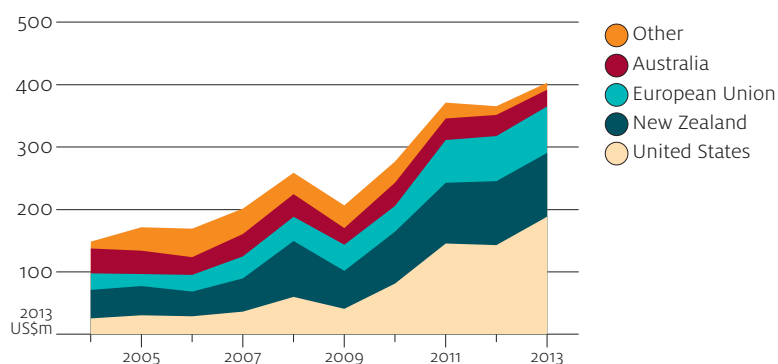
Despite the significant rise in total cheese imports by the Republic of Korea, the total value of cheese imported from Australia has declined over the past decade, from US\$40 million in 2004 to around US\$32 million in 2012 and further to US\$27 million in 2013. This has led to a decline in the market share of Australian cheese in the Republic of Korea from nearly 30 per cent in 2004 to less than 10 per cent in 2013.

Australia exports a variety of cheeses to the Republic of Korea. Its more significant exports include cheddar and cream cheese. Australia's major competitors in this market are the United States, New Zealand and the European Union, from which the Republic of Korea imported around US\$188 million, US\$102 million and US\$74.4 million, respectively, in 2013. The United States is the largest exporter across all cheese types, while the European Union exports principally high value, speciality cheeses and New Zealand exports mostly mozzarella and cheddar.

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Republic of Korea cheese imports by source



Source: United Nations Comtrade Database, 2014

Both the United States and the European Union already benefit from preferential market access through their respective FTAs with the Republic of Korea. Since 2012 Korean imports of US cheese have been more competitive than those from Australia. Under KORUS, the over-quota tariff of 36 per cent applied to imports of US cheese will be steadily phased out between 2012 and 2026. The agreement also specifies that the tariff-free quota will be increased from 7000 tonnes in 2012 to 10 280 tonnes in 2025. By 2026 imports of all US cheeses will be duty-free. Similarly, under the EU–South Korea Free Trade Agreement, the 36 per cent tariff is being phased out between 2011 and 2026. The tariff-free quota for the European Union will grow from 4560 tonnes in 2011 to 6696 tonnes in 2025, with full liberalisation in 2026.

Malting barley and unroasted malt

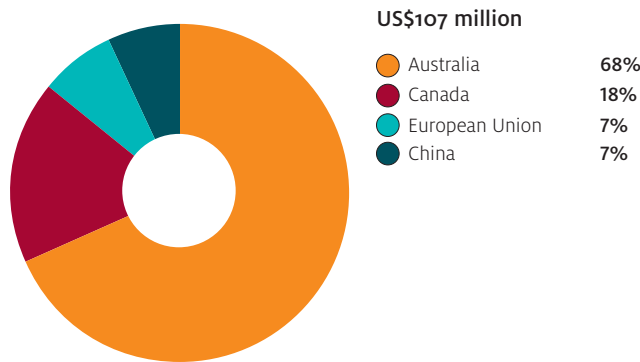
The Republic of Korea is Australia's largest export destination for unroasted malt, accounting for around 20 per cent of Australian export shipments in 2012. For malting barley, the Republic of Korea accounted for around 3 per cent of total Australian shipments.

Australia is the major supplier of malting barley and unroasted malt to the Republic of Korea, accounting for virtually all the Republic of Korea's malting barley imports and almost 70 per cent of unroasted malt imports in 2013. Australia's major competitor for unroasted malt in that market is Canada, which accounted for 18 per cent of imports in 2013, followed by the European Union (7 per cent) and China (7 per cent).

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Republic of Korea imports of unroasted malt by source, 2013



Source: United States Agricultural Trade Office, Seoul

Simulation analysis

Reductions in tariffs currently applied to imports of Australian agricultural products, and expansion of tariff-free quotas, will improve Australia's competitiveness in the Republic of Korea. These changes are expected to increase Australian agricultural exports to the Republic of Korea.

The Republic of Korea is an important market for Australian beef and cheese. Using ABARES world trade models for beef and cheese, a simulation analysis was undertaken to estimate potential changes to imports of these two commodities by the Republic of Korea following implementation of KAFTA in 2015.

In the analysis, separate baseline or 'business as usual' scenarios were developed for beef and cheese. In each baseline, it is assumed that KAFTA is not implemented. These results are then compared with those from a scenario in which KAFTA is implemented in 2015 with tariff reductions for beef and cheese. The baseline scenarios reflect a global trade environment that does not undergo significant change, such as production shocks or extreme weather events, over the simulated period.

The simulations for beef and cheese incorporate the EU–South Korea Free Trade Agreement (implemented in 2011) and KORUS (2012). Their inclusion in each simulation provides a more realistic assessment of future trade outcomes because the European Union and the United States are significant exporters to the Republic of Korea. The simulations also incorporate available information on the recently signed Japan–Australia Economic Partnership Agreement (JAEPA), which will improve market access for Australian beef and cheese to Japan. JAEPA's inclusion in the models allows for consideration of any influence it might have on Australian beef and cheese exports to the Republic of Korea.

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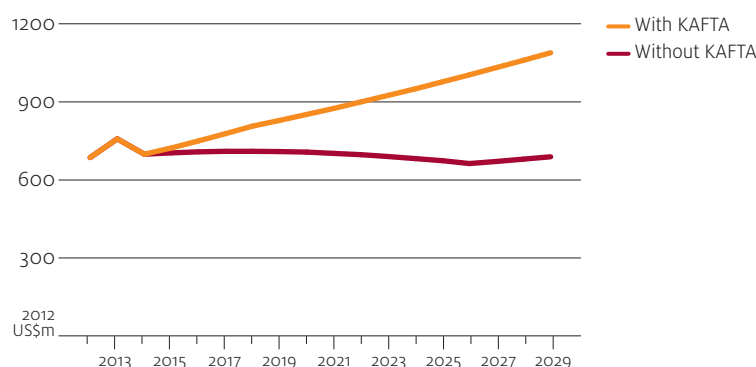
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Beef

In the baseline scenario (without KAFTA), imports of Australian beef by the Republic of Korea are projected to trend downward until 2026 because of the competitive advantage afforded to US beef by KORUS. That is, the consumer price of US beef imports declines in the Korean market relative to imports from the rest of the world because of the agreed tariff cuts on US beef. Only when KORUS is fully implemented in 2026 do imports of Australian beef to the Republic of Korea start to trend upward, reflecting modest growth in consumer demand in the Korean market.

Under KAFTA, the landed value of Australian beef imports to the Republic of Korea is projected to increase by 59 per cent between 2012 and 2029 (the year tariffs on Australian beef are fully removed). Under KAFTA, the landed value of beef imports from Australia in 2029 is projected to be around US\$1.1 billion (in 2012 US dollars) compared with US\$0.7 billion without KAFTA. This projected increase in Australian beef imports in 2029 under KAFTA is mainly driven by higher import volumes (58 per cent compared to the scenario without KAFTA). Under KAFTA, the consumer price of Australian beef in the Korean market by 2029 is projected to be 23 per cent lower than the price in 2012 (including tariffs) because of the agreed tariff reductions on Australian beef.

Projected value of Australian beef imports, Republic of Korea



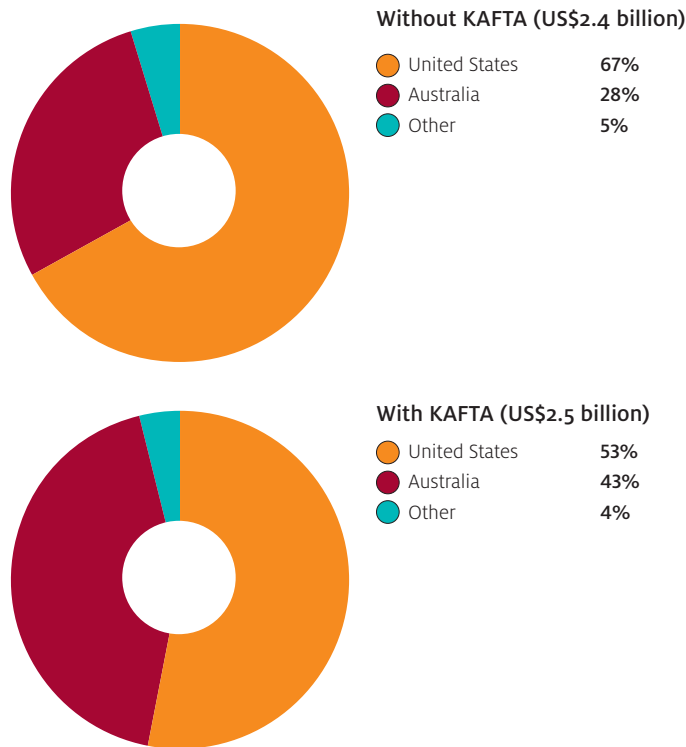
Note: Values are landed values, which include cost, insurance and freight (cif).
Source: ABARES model output

Despite the projected increase in imports of Australian beef, Australia's share of beef imports in the Korean market is projected to decline under both KAFTA and the baseline scenario compared with 2012. However, under KAFTA, Australia's share of beef imports in the Korean market is projected to be 15 percentage points higher in 2029 than without KAFTA. This relative improvement reflects the improved price competitiveness of Australian beef imports under KAFTA relative to many other major competitors in the Korean market. However, Australia will remain less competitive against US beef in that market during the implementation period of KAFTA because tariffs on US beef will be phased out earlier than on Australian beef under KORUS.

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Share of beef imports in 2029, Republic of Korea



Source: ABARES model output

Cheese

The Republic of Korea applies a tariff of 36 per cent on all imports of Australian cheese. Under KAFTA, Australia will be able to access a single tariff-free quota for all types of cheese; this quota will increase over the implementation period. The import tariff will still apply to Australian cheese imports exceeding the quota, but the applied tariff rate will reduce over the implementation period. Cheeses are defined in the agreement as:

Category 1 cheddar cheese—the 36 per cent tariff will be phased out evenly over 13 years, ending in 2027

Category 2 grated and powdered cheese and speciality cheeses (such as camembert and gouda)—the tariff will be phased out evenly over 20 years, ending in 2034

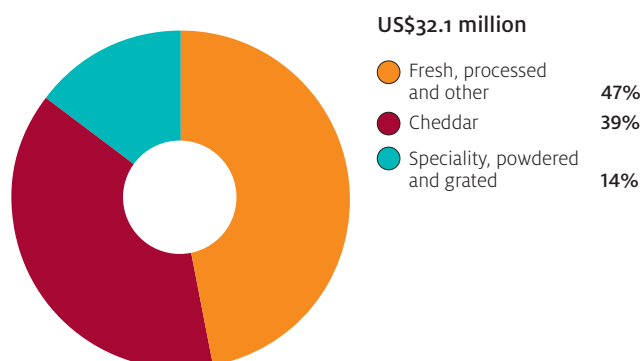
Category 3 fresh cheese (such as mozzarella and cream cheese), processed cheese and all other cheeses—the tariff will be eliminated evenly over 18 years, ending in 2032

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In 2012 (the base year of the simulation models), 47 per cent of Australian cheese imports to the Republic of Korea were in category 3 (fresh, processed and other cheeses). Cheddar cheese (category 1) made up 39 per cent, while powdered, grated and speciality cheeses (category 2) comprised 14 per cent.

Australian cheese imports to Republic of Korea, 2012



Source: United Nations Comtrade Database, 2014

Elimination of existing tariffs by the Republic of Korea is expected to create opportunities for Australian cheese exports. Without KAFTA, the landed value of Australian cheese imported by the Republic of Korea is projected to decline by 9 per cent between 2012 and 2034. This reflects improved competitiveness of the United States and European Union relative to Australia for cheese categories 2 and 3, given tariff reductions under their respective free trade agreements. Over the same period, the landed value of imported Australian cheddar cheese (category 1) is projected to increase by 23 per cent, mainly reflecting demand growth for cheddar cheese in the Korean market more than offsetting the effect of stronger competition from the United States and the European Union.

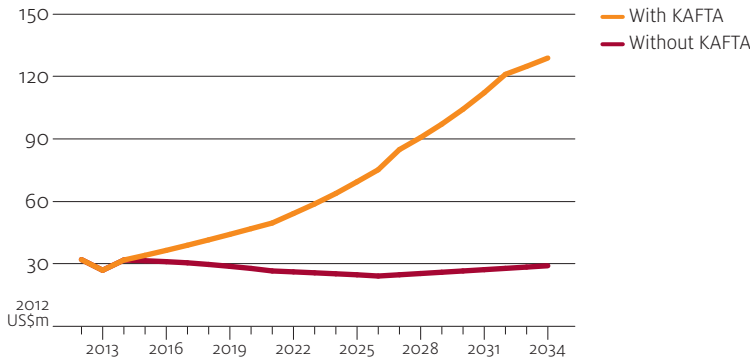
Under KAFTA, the total landed value of Australian cheese imports to the Republic of Korea is projected to increase fourfold between 2012 and 2034 to US\$129 million (in 2012 US dollars). This gain is mainly because of the projected increase in import volumes from Australia over the implementation period, although the average consumer price of Australian cheese in the Korean market is projected to be 15 per cent lower in 2034, compared with 2012, in response to the agreed tariff cuts. Without KAFTA, the total landed value of imported Australian cheese is projected to be US\$29 million in 2034.

Growth in imports of cheddar cheese is expected to drive growth in total Korean cheese imports from Australia in the early years of the implementation period under KAFTA. Import growth for the other two cheese categories is projected to accelerate toward the end of the implementation period. These results reflect expected strong demand for cheddar cheese in the Republic of Korea combined with tariff reductions under KAFTA (in which cheddar cheese achieves tariff-free status earlier than the other two cheese categories).

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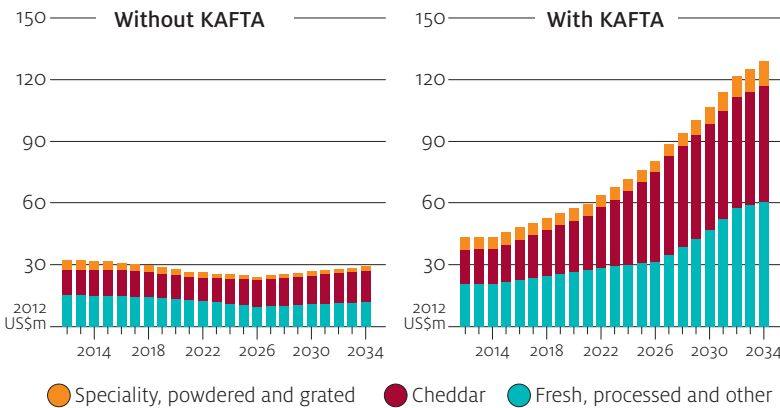
Projected total value of Australian cheese imports, Republic of Korea



Note: Values are landed values, which include cost, insurance and freight (cif).
Source: ABARES model output

Under KAFTA, Korean imports of Australian cheddar cheese are projected to be US\$56 million in 2034 compared with US\$15 million without KAFTA, a 268 per cent increase. Again, the projected increase for cheddar cheese under KAFTA is the result of a significantly higher volume of trade.

Projected value of Australian cheese imports, Republic of Korea



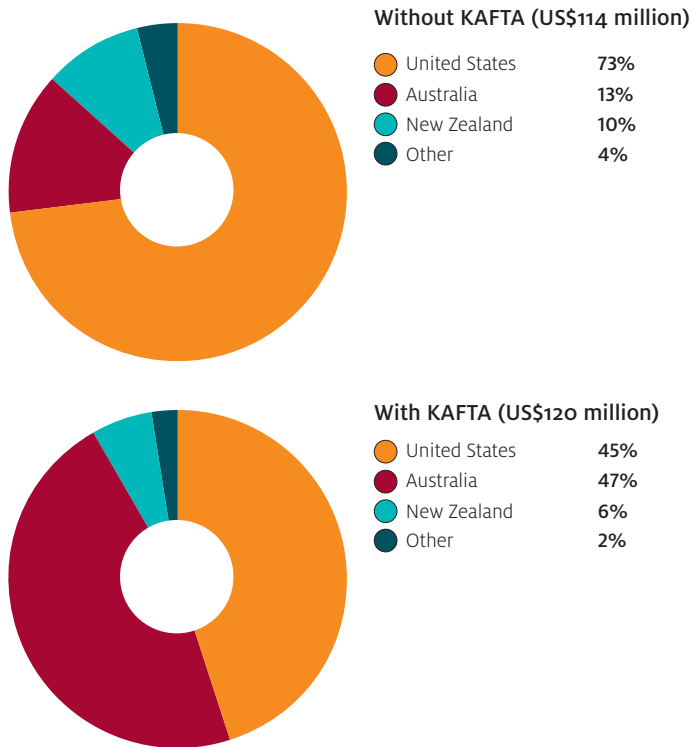
Note: Values are landed values, which include cost, insurance and freight (cif).
Source: ABARES model output

The share of Australian imports in the Korean cheddar cheese import market is projected to be significantly higher in 2034 under KAFTA than in the baseline scenario. Without KAFTA, Australian cheddar cheese is projected to comprise 13 per cent of the Korean cheddar cheese import market, compared with 47 per cent under KAFTA.

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Share of cheddar cheese imports in 2034, Republic of Korea



Source: ABARES model output

For category 2 cheeses, Korean imports from Australia in 2034 are projected to be 478 per cent higher under KAFTA than in the baseline scenario, at US\$12 million. Under KAFTA, the Australian import share for category 2 cheeses is projected to be 5 per cent in 2034 compared with 1 per cent in the baseline. Under KAFTA, Korean imports of category 3 cheeses (fresh, processed and other cheese) from Australia are projected to be US\$61 million in 2034, compared with US\$12 million without KAFTA. This is a fivefold improvement relative to the baseline. As a result, Australia's import share in the Korean market for category 3 cheeses increases from 3 per cent in the baseline to 14 per cent under KAFTA.