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The Rt Hon Kemi Badenoch MP
Secretary of State for International Trade and President of the Board of Trade
Department for International Trade
Old Admiralty Building
Admiralty Place
London
SW1A 2DY

02 February 2023

Dear Secretary of State,

SMI Response – Call for input on trade negotiations with South Korea

I write as Chief Executive of the Society of Maritime Industries (SMI) to inform the Department for International Trade's approach for starting negotiations on a free trade agreement with the Republic of Korea.

The Society of Maritime Industries (SMI) is the trade association for the UK's maritime engineering, science and technology community – looking to enable maritime organisations and businesses of all sizes to thrive. This we do in various ways – including annual conferences, overseas events and trade missions. We support our members to raise their profile and enjoy meaningful collaborations. As a trusted advisor to the UK Government, we look to create new momentum and progress for the industry as a whole, and create new levels of maritime innovation, within our own member community and beyond.

Our members believe that the Republic of Korea is a very important trading partner for the UK, making a permanent free trade agreement (FTA) an invaluable opportunity for our two countries to work together more closely. Besides responding to questions within the call for input, there are a few observations that the Government ought to take into account before entering negotiations with the Republic of Korea for a permanent FTA.

The UK Government should work with the Republic of Korea to:

- 1) consider trade benefits for UK defence within the broader framework of the FTA;
- 2) reach a mutual recognition agreement that covers testing on maritime equipment;
- 3) establish a level playing field that includes duty free entry to our respective markets;
- 4) create a more integrated maritime transport system between our two countries.

Trade benefits for UK defence

With rising defence capital equipment budgets in the UK, the ongoing war in Ukraine driving new defence procurement and the general needs of our armed forces to replace, upgrade or deploy new

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defence systems, it is not inconceivable that South Korean companies will develop a growing interest in seizing the trade benefits within this area.

By way of an example, the Ministry of Defence (MoD) has an emerging programme to replace its fleet of AS90 Self Propelled Howitzers and the South Korean company Hanwha is well placed to compete for this project. Since the end of the Cold War, the UK industry has shrunk to a critical point where the skills and equipment to design and build large calibre self-propelled guns such as the AS90 is rapidly becoming impossible. Should the UK Government decide to award a contract to South Korean companies such as Hanwha through open competition, any permanent FTA with the Republic of Korea must ensure that the UK will get more than just equipment in return.

Since 1982, the Republic of Korea has imposed a strict offsets policy on foreign contractors when procuring equipment from overseas. An offset obligation is imposed on a contract valued at more than USD 10 million. For programmes with competing suppliers, approximately 50% of the estimated main contract amount will be allocated to the offset scheme, while 10% is normally allocated in sole source programmes. In November 2022, the Republic of Korea's Defence Acquisition Programme Administration (DAPA) introduced lists of products and services that it seeks to prioritise under the country's defence offset policy, aimed at covering technology cooperation and component manufacturing. Crucially, technology cooperation is geared towards facilitating foreign contractor transfers of defence technology and knowledge to the South Korean industry.

In contrast to the Republic of Korea, the UK does not have an offset policy and leaves it up to foreign contractors to propose a programme of UK content under competition and against prescribed scoring criteria outlined in the tender. The proposed programme that overseas companies such as Hanwha offer in response to a tender will be scored against other companies' bids and – consequently – the benefits delivered to UK plc is largely in the hands of industry entities who will generally be reluctant to support the types of offsets that South Korea seeks for itself.

In light of the above, SMI believes that the UK Government needs to consider weaving trade benefits for our defence sector in the framework of the FTA with the Republic of Korea, preferably leading to the adoption of a similar offsets programme.

Mutual recognition

Under the temporary FTA with the Republic of Korea that the UK Government agreed in our transition outside of the EU, there is a Mutual Recognition Agreement (MRA). However, the Republic of Korea still insists on testing equipment at approved testing centres to the equivalent Korean standard. This constitutes a barrier for UK companies, despite the existence of an MRA, by virtue of the expensive costs that they have to bear in order to do business.

SMI asks the UK Government to make sure that full mutual recognition and acceptance of standards between our two countries is a key element of any permanent FTA with the Republic of Korea. This would not only remove a significant cost for UK businesses, especially small and medium-sized enterprise (SME), but it will enable them to expand their offering to smaller ships where prices are ultra-competitive.

Level playing field

Any permanent FTA between the UK and the Republic of Korea needs to achieve a truly level playing field between the two countries. Both countries have significant capacity for the development of

equipment for naval and commercial vessels, but duty costs remain a factor to be considered in every bid, especially when competing with respective local suppliers.

SMI asks the UK Government to pursue duty free entry in its FTA negotiations with the Republic of Korea, as it would give UK businesses an 8% price benefit in their tenders for equipment imported into that country.

A more integrated maritime transport system

On one hand, the UK continues to be a very strong actor in the planning and design of ports, most of which has recently been focusing on improving efficiency and modernising systems through automation and other techniques, whilst also minimising the carbon footprint of these terminals.

On the other hand, the Republic of Korea represents a very interesting market as one of world's top shipbuilding nations – especially for large ships – and by virtue of its geographical position in relation to the People's Republic of China.

Certain types of ships such as oil tankers can be designed freely, with ports successively having to adapt in order to accommodate them depending on their dimensions, while in other cases they have to be designed in order to fit into the port's dimensions. An example can be found in terms of draught for liquid natural gas (LNG) carriers and beam for large container vessels. This means that the overall maritime supply chain is not as efficient as it could be in terms of energy, timing and costs.

SMI would like to see the UK and the Republic of Korea working together within the framework of a permanent FTA to establish what aspects of ships and ports could be adapted, in order to create a more integrated maritime transport system. Such a partnership would reap immense dividends for both our countries in terms of exports, particularly if the Republic of Korea could be convinced to sign up to the Clydebank Declaration of Green Shipping Corridors.

In conclusion, our members believe that a future enhanced FTA with the Republic of Korea represents an opportunity to deliver benefits for the UK's maritime engineering, scientific and technology community, as well as the wider domestic maritime sector, provided that SMI's observations are taken onboard by the UK Government.

If you require any further information, please do not hesitate to get in contact with SMI's Policy and Research Manager, Giorgio Buttironi, at Giorgio.Buttironi@maritimeindustries.org.

Yours faithfully,

A handwritten signature in black ink, appearing to read 'T. Chant'.

Tom Chant MBE
Chief Executive, Society of Maritime Industries (SMI)