

Korea-U.S. Free Trade Agreement: Cementing Economic and Political Relations

Angela H. An



**4201 Wilson Blvd. #110-334
Arlington, VA 22203**

Introduction:

Korea is currently Asia's third largest economy and has experienced robust growth in the last decade despite the Asian fiscal crisis in 1997¹. Korea's export trade has consistently grown. Exports grew 20% to over \$30.9 billion in July 2007 from the previous month - the 18th consecutive month the country has shown double digit growth².

Trade is particularly strong with the United States, who is currently one of Korea's largest trading partners, importing 17% of Korea's worldwide exports. U.S. export trade to Korea is also strong and amounted to \$32.5 billion in 2006, an increase of 16.9% from the previous year, despite restrictive tariff and non-tariff barriers³.

To facilitate the increasing amount of trade between the two countries, the United States and Korea have designed a bilateral free trade agreement to open markets and boost economic growth and development. On June 30, 2007, U.S. Trade Representative Susan C. Schwab and Korea's Trade Minister Kim Hyun Chong signed the Korea - U.S. Free Trade Agreement - widely referred to as the KORUS FTA - marking the largest free trade agreement for the United States since the signing of the North American Free Trade Agreement in 1992.⁴

As the FTA waits for the approval from both countries' legislatures, the debate continues about the benefits and drawbacks of opening the doors of free trade between the U.S. and Korea as well as the goals both sides hope to accomplish. The following assessment will discuss the general provisions of the KORUS FTA and the relationships that can be drawn between U.S.-Korea foreign policy, the KORUS FTA and its predicted outcomes upon implementation.

¹ The Korean government recently published an updated 2007 economic growth forecast of 4.6% from the previous forecast of 4.5%.

² Go to the official website of the Korean Embassy in the USA for more economic information- <http://www.dynamic-korea.com/>

³ Website of the US Trade Representative- http://www.ustr.gov/assets/Document_Library/Fact_Sheets/2007/asset_upload_file811_11034.pdf

⁴ For more information on US Free Trade Agreements can be found at the official website of the Office of the US Trade Representative: <http://www.ustr.gov/>

KORUS FTA Provisions:

The KORUS FTA is comprised of comprehensive provisions that will eliminate nearly 95% of all tariffs and non-tariff barriers to trade in goods within three years of the FTA's implementation. Most remaining tariffs will be eliminated within 10 years.

Agriculture and Cattle:

Once implemented, the FTA will give duty-free status to more than half of current U.S. farm exports. Most other exports will fall under a two- or five-year tariff phase-out plan or a tariff rate quota. Many U.S. export products will benefit, including, but not exclusive to wheat, feed corn, soybeans, breads and pastries, cherries, lemons, raisins, chocolate, pet food, and an assortment of dairy products⁵.

Provisions have also been made to increase opportunity for U.S. beef and other meat products. Tariffs for U.S. beef exports will phase out over 15 years, tariffs on poultry products within 10-12 years and tariffs on pork products within 7-10 years.

Automobiles and Textiles:

Under the provisions of the agreement, tariffs on most U.S. and Korean passenger vehicles and trucks will be immediately lifted and Korea will cease to impose any new engine displacement taxes. The present engine displacement taxation system will be updated so that larger U.S. car manufacturers will not be liable to pay higher export taxes. Korea has taken an additional step for streamlining Special Consumption and Vehicle Taxes to a standard 5% and the U.S. is following with a phase out of its tariffs on larger Korean vehicle imports over three years.

In the textile industry, companies who utilize Korean or U.S. yarn will gain preferential trade treatment and approximately 61% of tariffs will be lifted on textile imports. Provisions have been negotiated for imposing 24-month restrictions, which may

⁵ Go to the official website of the United States Trade Representative (<http://www.ustr.gov>) for a complete list of goods that fall under the free trade agreement as well as a full transcript of the FTA.

be extended an additional two years on imports that cause major profit loss in an effort to protect the markets⁶.

Pharmaceuticals:

Under the FTA, there will be improved access for the U.S. and Korea to innovative generic pharmaceutical products, biologics and medical devices to provide quality healthcare. Predictability and transparency in pricing, reimbursement and regulation of drugs and medical devices are also ensured to promote fair market practice and discourage unethical business behavior.

Telecommunications, Broadcast and Service Industries:

The FTA aims to promote competition and efficiency in the broadcast, telecom and service markets. Within three years of the FTA's implementation, Korea will allow foreign companies and subsidiaries the opportunity for 100% investment in broadcast companies and 100% investment in telecom companies within two years. Moreover, Korea will improve access to service markets, including financial services, legal services and express delivery, and will uphold laws that protect the financial interests of foreign investors from unfair practices.

Protection of Businesses:

In order to safeguard the interests of foreign investors, the latter part of the FTA focuses on the protection and enforcement of intellectual property, regulatory transparency, and environmental and labor practice laws. Stronger laws and oversight aim to protect company trademarks, patents and other forms of intellectual property. Governments will only be authorized to use legitimate computer software and are responsible for combating and punishing copyright and counterfeit violators.

Transparency of testing and certification policy will be increased with each government mandated to publish any impending regulation changes, allowing an opportunity for comment once a change has been made, and requiring its publication in

⁶ Cooper and Manyin (2007, 6)

an official capacity.⁷ Transparency has also been insured in the implementation and operation of the FTA, allowing for access of related documents and opportunity for comment by third parties.

Protection of Workers and the Environment:

Protection of workers and the environment are included in the FTA. This includes effective abolition of child labor and assurance of a fair minimum wage, work hours, safety and health standards within the workplace, and worker's access to the law and courts in the case of grievances in accordance with the ILO Declaration on Fundamental Principles and Rights at Work and its Follow-Up (1998,1999). Environmental policy will be maintained according to domestic laws as well as agreed upon multilateral agreements and both countries will be responsible for increasing public participation on implementation⁸.

The Effects of the FTA:

Much discussion has taken place regarding the advantages and disadvantages of the KORUS FTA. Many analysts are supportive of the FTA, stating advantages that extend beyond economics, although various groups have voiced their concerns about the predicted benefits and others question the motivations of both governments.

Economic Results:

Presently, Korea benefits from a one-way low tariff rate averaging 3.7% while the U.S. has shouldered a tariff rate averaging 11.2%⁹. Previously, this was a method to help support Korea's growing economy, and the country is currently enjoying the healthy results. The effects of removing most tariffs will benefit both countries, which anticipate increased export trade estimated at \$7.1 billion for Korea and \$12.2 billion for the United

⁷ A more detailed description of the US-Korea Free Trade Agreement and its provisions can be found on the official Office of the US Trade Representative website:

http://www.ustr.gov/Trade_Agreements/Bilateral/Republic_of_Korea_FTA/Section_Index.html

⁸ The agreed upon multilateral agreements may be found on Annex 20-A under Chapter 20 of the final version of the Korea-US Free Trade Agreement, which may be found on the official Office of the US Trade Representative website.

⁹ Go to the US Trade Representative website for explanation of economic advantages

States¹⁰. This is particularly significant for the U.S., not only for the increased export revenue, but for the readjustment of the trade imbalance between the two countries. It signifies the growing strength of Korean markets, the increased influence of U.S. trade and the economic advantages of U.S. investment in the region.

Beyond increasing export revenue, the FTA will foster an increase in direct foreign investment (DFI) for Korea. Despite restrictive laws that limit foreign investors to minority stakes in Korean companies and subsidiaries, U.S. DFI totaled approximately \$18.8 billion in 2005¹¹. The FTA will create stronger laws to support and protect business interests resulting in increased foreign investment, an increase in jobs and a continued boost to the Korean economy.

Groups, such as Korean farmers, are not supportive of the FTA in fear that open markets will cause a significant drop in prices and push them out of the market. U.S. car manufacturers have likewise voiced their fears that the FTA does not effectively address non-tariff laws that block access to the Korean market. U.S. ranchers have voiced their concerns about the lack of stronger support for the U.S. beef export market, as they have faced restrictions on beef exports to Korea. Provisions have been created for these groups in the FTA to help offset losses and open markets.

Transparency and Efficiency:

Beyond creating trade equality, opening markets will bring Korean market policy and regulation to the global level as they aim to secure better access to foreign markets, increase their global competitiveness and obtain the benefits of trade liberalization. One predicted outcome of open Korean markets to foreign investment is an increased focus on greater efficiency and productivity to compete. This can lead to faster growth for both countries in the long term.¹²

This will be equally fueled by an incoming pool of educated workers with new sets of knowledge and expertise, facilitating technology transfer to Korean companies, resulting in increased productivity.

¹⁰ Lim, (2006, 2)

¹¹ Website of the US Trade Representative-

http://www.ustr.gov/assets/Document_Library/Fact_Sheets/2007/asset_upload_file811_11034.pdf

¹² Choi and Schott (2004,187)

Strengthening Strategic Alliances:

Beyond the commercial significance in terms of trade and increased efficiency, the FTA is seen as an avenue to reinforce and forward the regional and bilateral political and strategic interests of both countries.¹³ According to a study by the Institute for International Economics, if the U.S. maintains close security ties with a country, they are 51% more likely to have trade relations compared to a similar country without close security ties¹⁴.

It has been noted that the FTA would be more advantageous for the U.S. and there have been questions about Roh Moo-Hyun's government's motivation for moving forward despite drawbacks for specific industries and the possibility of more economically advantageous alternatives¹⁵. In response, both governments have drawn attention to the implications beyond economics. Beyond its rising economic influence, Korea is also strategically located within Northeast Asia and the promotion of trade relations helps cement and build upon the current political and strategic relationships that exist between the U.S. and Korea. The signing of the KORUS FTA signifies the importance the United States places on its presence in the region as well as the importance both sides put on fostering the strategic relationship they have maintained for over 50 years.

Conclusion:

The global economy is becoming increasingly intertwined with political and security policy. Trade is not merely a matter of currency and goods, it involves navigation between multiple interests, political and security issues as well as the economic outcomes. Each side attempts to balance their interests between anticipation of economic opportunity and innovation and the ultimate affects of having an open marketplace.

As Asia becomes increasingly influential and the United States' policy agenda includes more of the region, the KORUS FTA is a timely step for both the U.S. and

¹³ Kyoto and Stern (2007, 3)

¹⁴ Choi and Schott (2001, 49)

¹⁵ Lim (2006, 1)

Korea. As the most commercially significant free trade agreement the United States has concluded in over 10 years, the world will be watching closely as the FTA moves through the United States and Korean legislatures. Debate will continue on both sides of the free trade agreement's merits but the move to directly engage Asian nations in bilateral trade relations is a positive sign that the United States is taking notice of the importance that the region now plays and will continue to play in the future.

Bibliography

Altman, Daniel. April 8, 2007. Switching Tracts with a South Korean Pact. *The New York Times*, pBU5(L).

Choi Inbom and Jeffrey J. Schott. 2001. Free Trade between Korea and the United States? *Policy Analyses in International Economics* no. 62. Washington, D.C.: Institute for International Economics.

Choi Inbom and Jeffrey J. Schott. 2004. Korea-US Free Trade Revisited. In *Free Trade Agreements: US Strategies and Priorities*, ed. Jeffrey J. Schott. Washington, D.C.: Institute for International Economics. p. 173-196.

Cooper, William H. and Mark E. Manyin. 2007. *The Proposed South Korea-U.S. Free Trade Agreement (KORUS FTA)*. Washington, D.C.: Congressional Research Service.

Lee, Hee-beom. May 15, 2006. *Korea, U.S. FTA no longer and option*. Korea Herald. Korea. http://www.bilaterals.org/article.php3?id_article=4719.

Turner, Barry (ed.). 2006. *The Statesman's Yearbook 2007-The Politics, Culture and Economics of the World*. New York. p. 747-755.

Lim, Wonhyuk. June 13, 2006. KORUS FTA: A Pragmatic and Strategic View. *Policy Forum Online* 06-46A. San Francisco, CA: Nautilus Institute.

Kyoto, Kozo and Robert Stern. 2007. *Economic Effects of a Korea-US Free Trade Agreement*. Washington, D.C: Korean Economic Institute.

Ministry of Finance and Economy- Republic of Korea. July 12, 2007. *Government Revised GDP Growth for 2007 to 4.6 Percent*.
http://english.mofe.go.kr/news/pressrelease_view.php?sect=news_press&sn=5409.

-----, July 9, 2007. U.S. Agriculture Tell Congress to Approve FTA with Korea. *Asia Pulse*. Washington, D.C.

-----, August 1, 2007. Korean Exports Jump 20 Percent Year-on-Year in July. Embassy of the Republic of Korea in the USA. Washington, D.C.
http://www.dynamickorea.com/news/view_news.php?main=KTD&sub=ECO&uid=200700179326&keyword=

-----, 2007. *Strong Support for the Korea-US (KORUS) Free Trade Agreement*. Office of the United States Trade Representative. Washington, D.C. <http://www.ustr.gov>.

-----, 2007. *KORUS FTA: Opportunities for Agriculture*. Office of the United States Trade Representative. Washington, D.C. <http://www.ustr.gov>.

----- . 2007. *Free Trade with Korea- Brief Summary of the Agreement*. Office of the United States Trade Representative. Washington, D.C. <http://www.ustr.gov>.

----- . 2007. *Detailed Summary of the KORUS FTA*. Office of the United States Trade Representative. Washington, D.C. <http://www.ustr.gov>.

----- . 2006. *FTA: United States and Republic of Korea Economic and Strategic Benefits*. Office of the United States Trade Representative. Washington, D.C.
http://www.ustr.gov/assets/Document_Library/Fact_Sheets/2006/asset_upload_file582_8880.pdf