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Balancing Interests in the KORUS FTA
By Troy Stangarone

On April 1, 2007, after a marathon negotiating session that ended minutes before the expiration of President Bush's trade promotion authority, the United States and Korea reached a Free Trade Agreement that reflects the needs and concerns of both nations.

The FTA will create a free trade area ranking behind only NAFTA and the EU. Korea's economy is similar in size to all of ASEAN, worth around $1 trillion. Korea shipped $284 billon in merchandise in 2005, the equivalent of the world's smallest 118 economies, and lagging only the EU, Japan, China, the United States, and Hong Kong.

When the two sides began negotiating, the major areas of interest and sensitivity for each were readily apparent. Korea wanted to open the U.S. textile market to its products, to get relief from U.S. trade remedies, and to have goods from the Kaesong Industrial Complex in North Korea considered "South Korean" in the deal. South Korea insisted from the beginning that it would not open its rice market. For its part, the United States saw the FTA as an opportunity to resolve longstanding issues related to barriers in the Korean market regarding transparency, the Korean auto market, and pharmaceuticals. Korea's domestic market also held significant prospects for U.S. agricultural producers. For domestic political reasons, movement on trade remedies and the Kaesong issue were nonstarters for Washington.

The deal struck just before midnight April 1 seeks to balance these issues. Within three years of the KORUS FTA coming into force, nearly 95 percent of goods and industrial products will be tariff free, and could expand trade between the two countries by $20 billion.

For the United States, the big winner seems to be the U.S. auto industry. The U.S. negotiating team won a series of concessions and a unique set of safety provisions to help finally pry open the Korean market. Korea will immediately eliminate its tariff on U.S. autos, while over a three-year period reduce and compress its engine displacement tax into two tiers, one for engines above 1000cc and the other for those below. Further, the agreement commits the Korean government to not impose any new engine displacement tax. The FTA will also create a special Autos Working Group to address nontariff barriers and help provide an early warning system for regulatory issues that may develop. Additionally, the agreement will create an expedited dispute settlement system for violations of auto provisions in the FTA, which would allow the U.S. to immediately re-impose its tariff if Korea was found in violation. Lastly, the Korean press is reporting that U.S. negotiators won each U.S. producer the right to utilize California emissions standards until they sell 10,000 cars a year in Korea.

Nonetheless, the reaction from the auto industry and its supporters in Congress has been to either oppose the deal or call for changes that would bring it more in line with a proposal put forward by Congress a few short weeks before the negotiations were set to conclude. This contrasts with much of the overall U.S. industry reaction to the agreement, which has been largely positive.

While members of the U.S. auto industry such as Chrysler have said that they "will not support this agreement as we currently understand it," they have not publicly articulated their reservations. However, the immediate removal of the U.S. auto tariff, the 20-year phase out of the U.S. light truck tariff, and the industry's previous bad experiences in Korea are likely factors in this decision. An additional factor may be that their limited infrastructure in Korea means that they are unlikely to see significant immediate gains in Korea. True growth for the U.S. auto industry in the Korean market is likely to be a long-term process.

The U.S. negotiating team was successful in securing additional access for U.S. agricultural products. More than half of the $1.6 billion in U.S. agricultural exports to Korea will immediately become duty free. While tariffs will be phased out and tariff rate quotas increased for other U.S. agricultural products, the U.S. also gained access in two of Korea's most sensitive agricultural products. For oranges, the negotiators creatively segmented the tariff structure into "in" and "out" of season segments. The tariff will remain while oranges are in season in Korea, but the out of season tariff will be phased out over a seven-year period. Beef imports are still disputed, but the U.S. negotiating team was able to secure a 15-year phase-out of the tariff.

While technically not part of the FTA, Korea has not opened its market to U.S. boneless or bone-in beef. Prior to the FTA negotiations, there was an agreement on shipping boneless beef under 30 months of age to Korea, but all three shipments were rejected due to the presence of small amounts of bone chips. The American Farm Bureau and various cattle and ranch associations are withholding support for the deal until U.S. beef returns to the Korean market.

Finally, the U.S. did secure an investor-state provision to protect U.S. investors and win greater access for U.S. services in Korea, while staying true to its TPA mandate to not undertake any changes to U.S. trade remedy law. On pharmaceuticals, the U.S. also secured commitments from Korea for greater transparency in pricing and reimbursement.

Though Korea was not able to win changes to U.S. trade remedy law, it did have a series of successes in the negotiations. Korea secured the immediate elimination of tariffs on 61 percent of textiles and garments by import value. Though the FTA does contain a "yarn forward" rule, Korean sources are reporting that it contains exceptions for key Korean products such as men's shirts and women's jackets. Korea also had rice excluded from the FTA.

Korea also secured a provision for outward processing zones on the Korean Peninsula. A committee will be established one year after the agreement comes into force that will set criteria in areas such as labor, the environment, and denuclearization to determine if amending the FTA to include such areas is appropriate.

After the FTA is signed June 30, the Korean National Assembly and U.S. Congress must approve the deal. In Korea, there will be significant pressure to approve it before the December 2007 presidential election. President Roh and his supporters will be strong advocates of early passage to ensure that the FTA helps cement President Roh's legacy and not that of his successor. In light of the reaction of both China and Japan to the KORUS FTA, the deal could burnish his legacy by sparking additional trade liberalization in the region. Prospects for National Assembly approval of the deal seem to be improving. Through much of the negotiations, support for the agreement fluctuated around the 50 percent mark, with significant protests by groups opposing the FTA. Yet, after the FTA was announced, support was near 60 percent, and polls of the National Assembly found about 40 percent of members in favor, 40 percent undecided, with the remaining 20 percent opposed.

In the United States, the picture is less clear. Congress will likely wait until after Korea approves the deal to take it up, but the prospect of elections in 2008 means there will be pressure to move the agreement through Congress and keep it from being entangled in a larger debate about free trade in the presidential election. Members that have expressed an opinion on the agreement have largely been negative: while the autos issue will be important, beef could be the greatest problem, especially in the Senate. Unlike autos, U.S. beef is not being sold in Korea. Prior to the BSE ban, Korea was the third largest export market for U.S. beef, and some estimates show U.S. beef exports reaching $1 billion once the tariff is removed. If this situation is not rectified after the meeting of the World Organization for Animal Health in mid-May, the FTA's strongest and original proponent, Sen. Max Baucus (dem, Montana), will likely become its strongest opponent. Given the political influence of agriculture in the Senate, this will be a significant problem.

The KORUS FTA is a good deal that will add a significant new pillar to a key U.S. alliance. It provides nearly immediate benefits for U.S. and Korean consumers across a range of products, and utilizes creative new methods to address longstanding irritants in the U.S.-Korea economic relationship. While it's not ideal for either side, this larger picture that should be kept in mind as the debate moves forward.

Troy Stangarone (ts@keia.org) is the Director of Congressional Affairs and Trade for the Korea Economic Institute. His views are his own.