The Korea-US Trade Deal

Seoul ventures from behind its tariff walls to a new future

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The landmark bilateral trade agreement signed between the United States and South Korea Monday symbolizes the final end of the protected, export-led economic model that molded South Korea into one of Asia's biggest tiger economies and signifies that the country can no longer sit behind tariff walls and sell its goods to the world.

The agreement begins a new economic chapter for both countries, opening combined economies worth US$14 trillion to undeterred trade. It is the biggest trade deal signed by the United States in the 15 years since the birth of the North American Free Trade Agreement, and gives the country a toehold in northern Asia as well as a bulwark against Chinese hegemony.

The accord culminates 10 months of difficult negotiations, often hampered by fierce opposition from Korean farmers who fear losing their market to massive American imports. Trade talks in Seoul have been threatened constantly by leftwing workers and farmers holding violent protests and demonstrations. But, although one angry taxi driver set himself ablaze, screaming antigovernment slogans, the signing of the pact is remarkable for the relative calm in Seoul. In earlier years, even negotiations over such an agreement would have sent students into the streets to battle phalanxes of riot gear-clad police. It may be that Korea is ready now to open its doors ever wider.

Nonetheless, the ratification process by the US Congress and South Korea's National Assembly could be stormy despite the fact that the initialing of the agreement squeaked under the wire for so-called fast-track authority that allowed US President George Bush the luxury of a simple up-or-down vote by US lawmakers. Lawmakers in both Washington and Seoul have complained that the agreement is too favorable to one side or the other.

Among other things, the agreement calls for removing or lowering tariffs and non-tariff trade barriers on 93 percent of the goods traded between the two nations. Korea, the US's third-biggest market for beef, has agreed to once again import the commodity, suspended since the outbreak of mad-cow disease three years ago, and phase out the 40 percent tariff maintained on it over the last 15 years. Beef has been a subject of acrimonious exchanges following South Korea's return of shipments of beef containing bone fragments. In exchange, the US agreed to exclude rice from the FTA, a major concession.

But overall, Korea ends up reaping considerable benefits under the deal, persuading the US to consider importing goods made in the North Korean territory of Kaesong as eligible for potential exports, although the issue must still be haggled over. This represents a significant concession given the international uproar over North Korea's nuclear weapons program. This item is covered under the so-called Outward Processing category, an agenda to be worked on further.

In other areas, the US has relaxed controls on cars and textile imports. Korean subcompacts with 3,000cc engine displacement will be exempted from tax, while Seoul will revamp its tax system to phase out discriminatory treatment against US cars with big engines. US pharmaceutical companies, with a huge business potential in Korea, have won a deal ensuring a greater degree of transparency in fixing prices for new drugs.

In tandem with this move, Korea's much protected service sector ? such as legal and financial services ? will also be relaxed. All of this, according to estimates by think tanks in the two countries, will have the effect of adding 2 percentage points to South Korea's GDP, helping to create half a million new jobs, and bring an additional US$20 billion to bilateral trade, which last year was worth a whopping US$78 billion.

Korea is clearly looking beyond these immediate benefits, regarding the free trade agreement as a chance for a new economic leap forward. "In order to become a developed nation we must face the challenge, and this FTA is that challenge," said President Roh in his special address to the nation, indicating the weight he was giving it.

In Washington, President George W. Bush was hopeful of an expanded trade opportunity with the world's 11th biggest economy, which generates nearly US$1 trillion worth of GDP a year. In his letter to the Congress, he said the agreement "will generate export opportunities for US farmers, ranchers, manufacturers and service suppliers" to a fast growing market.

It is clearly a win-win deal for both sides, but the implications for Korea are far greater. It's no less than an attempt to reverse Korea's eroding competitiveness in the global marketplace, squeezed between a low-cost China and an increasingly upscale, high-tech Japan. Nothing in recent years has alarmed Korea's boardrooms more than the rise of China and India. Samsung business group chairman Lee Kun Hee pointed to this danger when he recently warned that unless it reshaped its competitiveness, Korea would be confronting a serious danger. President Roh shares that perception, ordering the negotiations at the risk of losing his support base among the leftwing labor and radical farm lobby.

Following on, Roh is expected to spur talks for a similar deal with Japan and the European Union. The US-Korean FTA is the fourth that Korea has signed in recent years, adding to Chile, Asean and Singapore.

Roh's main challenge rests at home. In the face of possible rejection of the deal as a "national sellout," he needs to push ahead with ratification through a fractured parliament controlled by the opposition. Luckily for him, the principal opposition Grand National Party – so far dead-set against him on the issue of reconciliation with North Korea ? is in favor of the FTA. It is his own supporters in the center-left Uri party that stand in the way of smooth passage.

Roh's next problem is restructuring the inefficient farming sector, plagued by dwindling population and high production costs. Farmers constitute fewer than 8 percent of Korea's mature industrialized population, contributing just 4 percent to GDP. Yet, like their counterparts in Japan, Korean farmers have forged a strong political lobby demanding special attention. Over the years, the government has kept them quiet with subsidies worth over a trillion won (US$1 billion) each year. That system of bribing the farmers has kept Korea's rice five times higher than international prices, beef five to six times higher than world prices and many manufactured goods twice the price of goods abroad.

But rice protection is a losing game. To avoid opening up its rice market, Seoul had agreed to a deal under the Uruguay Round for importing a certain intake of its rice consumption (now 4.4 percent or about 4 million tonnes) each year.

The rice problem bedevils the government in other ways: while Koreans with their changing dietary patterns consume less and less rice, the country's rice production continues to rise through better farming methods and expanded farmlands created through landfills and reclamation projects, resulting in ever-growing cost for storage.

The fiscal burden from the farming sector has so worsened that President Roh, going against his center-left constituency, now declares: “Even farmers need to respect market forces.” Even though he has managed to evade a market opening on rice this time, the problem will continue.

For all that, there’s little doubt that the Korea-US FTA constitutes a shining legacy for the Roh presidency. Critics who have complained about his lack of leadership have now been silenced. Even if he ends his term in office in February next year without passage of this bill, growing support for it makes means the next administration will find it hard to back down. President Roh has evidently betrayed his political base, but only to provide Korea new momentum for the next stage of growth.

P.S.

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