Static and Dynamic Consequences of a KORUS FTA

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CONTENTS

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STATIC AND DYNAMIC CONSEQUENCES OF A KORUS FTA

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CONFERENCE Presented by
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Introduction

In important respects this conference reflected two somewhat contrasting perspectives on the just completed U.S.-Korea Free Trade Agreement (KORUS FTA). Those two perspectives, the one dealing principally with specifically economic aspects of the agreement and the other with broader questions of multilateral vs. bilateral efforts, were not immediately evident at the outset of the meeting, but they began to emerge at a midpoint in the conference's three-section agenda.

The first section of the conference was devoted to a KEI special study, *Economic Effects of a Korea-U.S. Free Trade Agreement,* written by Robert M. Stern and Kozo Kiyota. Professor Stern presented the paper, and its two discussants were Jeffrey Schott and Won W. Koo. Their comments, along with comments from other conference participants, adhered closely to subjects implied by the paper's title.[1]

The conference's second agenda section, devoted to the dynamic effects of a free trade agreement (FTA), focused on the paper, "The Payoff to South Korea from Globalization," by Gary Hufbauer and Agustín Cornejo. It was presented by Dr. Hufbauer and, likewise, followed closely the agenda title. Its discussant was Professor Anne Krueger, and it was at a point in her remarks that the conference's second perspective was introduced.

1. The conference convened only weeks after negotiations on the KORUS FTA had been completed, and as of this writing the agreement was awaiting both nations' final legislative approval.

The third agenda topic was the scope for dynamic effects in Korea's economy, and it heard three papers. The first, by Arthur Alexander, likewise adhered to the conference's designated theme: it focused on issues of foreign direct investment (FDI), principally but not exclusively in connection with Korea. The second paper, however, by Sungjoon Cho, built directly on and fully opened the conference's second perspective. His paper, "Is a Free Trade Agreement a Royal Road to Prosperity? Demystifying Trade Regionalism," put into sharp focus the question of whether bilateral or regional approaches to trade liberalization, exemplified by the KORUS FTA, are to be preferred to the global or multilateral approaches exemplified by the World Trade Organization (WTO) Doha Development Round. The final conference paper, "Regional Integration and a Free Trade Agreement among China, Japan, and Korea," continued with that second conference perspective. It was prepared by Professor Kang Hee-joon and in his absence was presented by Professor Yong Kim.

Panel I: KEI Special Study
Economic Effects of a Korea-U.S. Free Trade Agreement

Moderator: Ambassador Thomas Hubbard
Presenters: Robert M. Stern and Kozo Kiyota, University of Michigan
Discussants: Jeffrey Schott, Peter G. Peterson Institute for International Economics, Won W. Koo, North Dakota State University

Professor Robert M. Stern presented the special study and began by first recalling that in seeking an FTA, the United States and Korea have a number of objectives. The U.S. objectives he characterized as a lengthy "myriad" and in Korea's case as a shorter and more limited list. The U.S. focus is on both expanding market access for a sizable number of goods and services and altering Korea's regulatory environment "to conform to U.S. principles and institutions." Korea's goals he characterized as more to "avoid being left out of the general trend of FTAs," with the specific aim to "enhance Korea's global competitiveness" and strengthen its "political and strategic alliances."

Professor Stern then surveyed and briefly analyzed a number of prior studies in economics involving a Korea-U.S. FTA, all based on Global Trade Analysis Project (GTAP) and computational general equilibrium (CGE) models. Professor Stern pointed to what he regards as their limitations, principally that they are not meant to be predictive and that, depending on their assumptions, their results may vary widely. He then introduced the Michigan Model, which in his view avoids those limits.

With reference to prior studies by Cheong and Wang; McDaniel and Fox; Choi and Schott; Lee and Lee; and Schott, Bradford, and Moll, Professor Stern noted as a point of criticism the different welfare gains that each identified. The focus of most was on

Korea and the United States, but in some cases other actors were included. In his Table 10, Professor Stern compared those gains and noted the wide range they reflected. For Korea they "range from 0.4 percent to 3.5 percent" of GDP, and "the results obtained by Schott, Bradford, and Moll are several times larger than all of the other studies."

Professor Stern made a similar observation regarding the studies of the United States. As an example he cited the study by Gilbert and DeRosa: "The United States is shown to experience a [small] decline in economic welfare . . . [and] in all studies, the welfare effects . . . on the United States are very small." In contrast, and in a comment that anticipated the conference's second perspective, Professor Stern noted that his studies "show that multilateral free trade . . . may increase U.S. economic welfare . . . by 3.5 percent . . . and Korea's . . . by . . . 12.8 percent. . . ."

Professor Stern then elaborated extensively on the Michigan Model, in a chapter and presentation that incorporated 13 tables and dealt, inter alia, with global tariff rates, U.S. and Korean bilateral trade and trade with other major partners, Korean and U.S. FDI, and projected trade consequences of the KORUS FTA. The final section of the Kiyota-Stern paper was devoted principally to its single large Table 24, entitled "Computational Welfare Effects of Bilateral FTAs, Unilateral Free Trade, and Global Free Trade." Professor Stern drew attention to its last column, which showed the welfare effects of global free trade, which he summarized in a manner that again anticipated the conference's second perspective:

> The welfare benefits of global free trade are therefore much greater than the benefits to be derived from the bilateral FTAs, regional FTAs, and from unilateral free trade for both the United States and Korea . . .
>
> These calculations clearly show that multilateral trade liberalization offers potentially far greater increases in economic welfare for the United States, Korea, their FTA partner countries, and the other countries or regions that are covered in the global trading system. This is the case even if there would be less than complete free trade globally.

Comments of Discussants, Jeffrey Schott and Won K. Koo

Mr. Schott commented first on the substance of the KORUS FTA although he noted that there was as yet no text available. Even so, he concluded that the absence of agricultural and especially rice issues from the FTA was of minor economic consequence although it might have large political implications. On the Kiyota-Stern paper, he noted that the Michigan Model had certain advantages, but he was critical of the Kiyota-Stern findings on issues of agriculture and services, terming them "unbelievable." He added that their paper distorted his and others' own recent results on agriculture, possibly as a result of a misunderstanding. He reserved his most important point for FDI issues identified in Kiyota-Stern Table 23; he argued that FDI is the most important benefit from any FTA, and he remarked that a 1 percent increase in capital stock from FDI is likely to double the welfare gain.

Professor Won K. Koo, before commenting specifically on the Kiyota-Stern paper, recalled that on recent visits to Korea he had encountered much local awareness of earlier U.S. FTAs and a belief in Seoul that in both Mexico and Canada there had been negative results. He had attempted to reassure doubters on some of those concerns, and in connection with the Kiyota-Stern paper, he was in general agreement with it. He concluded that, compared with the GTAP approach, the Michigan Model provides "much more realistic results."

Professor Koo was, however, critical of the paper partly because its most recent data were from 2001, which he termed "ancient history," especially in the Korean case. He did, however, agree with Schott that it was far from clear why the Kiyota-Stern paper anticipated that the FTA would lead to an increase in Korea's agricultural products. He pointed out that with rising Korean incomes, rice consumption had already decreased and could be expected to decline further as farmers aged and were unlikely to be replaced. Nevertheless, because of likely structural adjustments and greater introduction of technology advances in Korea's farms, he believed that, contrary to some local fears, Korea's agricultural sector would survive in an FTA environment.

Comments of Other Conference Participants

Mr. C. Fred Bergsten also questioned some of the Kiyota-Stern findings, particularly with regard to agriculture and FDI. More broadly, he recalled that the welfare impact expectations of most past FTA studies had generally been surpassed by later real-world experiences, which have been "much greater than predicted results." With regard to the seeming dichotomy in the Kiyota-Stern paper between FTAs on the one hand and the multilateral framework on the other, Mr. Bergsten stressed that they are not to be regarded as "alternatives," but instead as cumulative. In that light, and taking note of recent FTA talks between Korea and the EU, Mr. Bergsten added that, if developments along those lines resulted in such an FTA, it would likely add to the prospects for a Japan-U.S. FTA and "the result of this bilateral deal will spill over [to something] a lot bigger."

Mr. Noboru Hatekayama, from his perspective as a former vice minister responsible for trade issues, reported on his own recent talks in Korea, which had left him with the view that there would not soon be any Korea-Japan FTA. Professor Koo responded that that would likely change if there were a U.S.-Japan FTA, a point forcefully agreed to by Mr. Schott: “I can assure you that all that would change if a U.S.-Japan FTA materialized or began to develop.”

Mr. Claude Barfield returned the discussion to agricultural issues, recalling that under GATT there had been room for agricultural exports to rise in times of “critical shortage” but that provision appeared not to be included in the KORUS FTA.

Mr. Schott responded that, although the precise FTA text was not yet available, the Korean negotiators were aware of related provisions in the U.S. FTAs with Chile and Mexico. The sensitivity of agricultural export issues was recalled by Mr. Hatekayama, who recalled an incident from a time when U.S.-Japan trade ties were tense in which the United States appeared to threaten Japan’s food supply by restricting U.S. soybean exports to Japan.

Professor Stern responded as follows to several points raised by discussants: (1) the gains from any FTA would be marginal compared with a successful Doha Round; (2) when agricultural trade barriers are lowered, demand increases, with resultant positive effects on prices and output; (3) projected welfare benefits from FTAs are always small when compared with multilateral proposals; (4) he was not “really confident” on the possible consequences of enhanced FDI as a result of the FTA; and (5) a serious drawback to any FTA are “rules of origin” (which economists often refer to as ROOS), which historically have acted as bureaucratically complicating limitations on the businessmen responsible for trade.

Panel II: Dynamic Effects of an FTA “The Payoff to South Korea from Globalization”

Moderator: C. Fred Bergsten
Presenters: Gary Hufbauer and Agustín Cornejo, Peter G. Peterson Institute for International Economics
Discussant: Anne Krueger, Johns Hopkins University, Paul H. Nitze School of Advanced International Studies

Mr. Gary Hufbauer began by recalling that Korea’s postwar trade opening had added “around $2,000 per capita additional income,” and he believed additional gains of “around $1,200 to $1,600 per capita” could be realized “from removing the rest of trade and investment barriers between South Korea and its economic partners.” The present paper, focusing on the “payoff to Korea,” grew from an earlier Institute for International Economics publication on the “payoff to America from globalization,” and its methodology had been applied here to Korea. He introduced Table 1, which showed that since 1959 Korea’s opening to trade had added about $2,100 annually to per capita growth.

He turned then to the components of Korea's growth, which he identified as the price and productivity benefits of import and export variety; the importance of "right size" concentrations; and "sifting and sorting," a process under which Korea had greatly changed its export and import profile. He then turned to Table 5, which reflects the several CGE studies that have been undertaken. Going forward, they point to about a $1,600 per capita improvement from global free trade and about $630 per capita from unilateral free trade. If Korea had FTAs with its major trade partners, that would represent something very close to global free trade, which would also lead to about $1,600 per capita growth.

Comments of Discussant, Anne Krueger

Before beginning her discussion of the Hufbauer presentation, Professor Krueger first agreed with Professor Stern that the trade gains for Korea were "on the macro side," and then suggested that Mr. Hufbauer's estimates of past trade gains in Korea had underestimated the effects of what she characterized as "dramatic shifts" in Korea's trade policy. She noted that in the 1960s Korea was the third-poorest Asian economy, and that macro changes, especially governmental policy that encouraged "anybody who could export," had resulted in export growth increases of 40 percent annually for 10 years. She added that "all the numbers I've seen" show that the "contribution of import-competing production to growth in the 1960s and early 1970s was negative," whereas "on the export side, things were booming."

Professor Krueger accepted that Korea's dramatic transformation was not the result of exports alone and that a key factor was the change in import policy. She noted that until 1967 Korea had a "positive list," which included only those items that could be imported, and that the shift to a "negative list," which identified only those that could not be imported, "was itself a tremendously liberalizing thing." Once producers were able to access world markets, they faced a very different environment because the import policy change "obviate[d] the necessity for getting high-cost inputs from domestic firms."

In support of Mr. Hufbauer's reference to a sifting and sorting mechanism, Professor Krueger recalled that in the 1960s, "88 percent of Korea's exports were primary commodities," and there "were no manufacturing exports." Among the other important factors that brought about change was that real wages rose by an average of 8 percent annually for more than 20 years. Overall, she argued, the change in trade strategy was "the absolutely most important factor." Had Korea not made that shift it would today "look like Myanmar, rather than Taiwan." With reference to the KORUS FTA, Professor Krueger called the agreement's exclusion of rice and agricultural products "disappointing," particularly to Korea's consumers. Nevertheless, she agreed with both Stern and Hufbauer that Korea would surely gain from access to the large U.S. market.

Professor Krueger then said the agreement posed a “big question,” which signaled the conference’s second perspective, that is, issues of globalization. The question was “how the rest of Asia would react” to the trade diversion the agreement would bring. If others responded to the KORUS FTA with similar arrangements, that might not be a bad thing, but there would be cost differentials other than from comparative advantage. Those differentials would bring inefficiencies that could be eliminated in a global-multilateral format.

Comments of Other Conference Participants

Mr. Thomas Palley raised a question in the context of Mr. Hufbauer’s reference to the sifting and sorting mechanism, particularly with regard to those who lost their jobs or took jobs with lower wages. He asked how that could be reconciled with the rise in average productivity projected by Mr. Hufbauer. Mr. Hufbauer stated that roughly one-quarter of those affected did end up with substantially lower pay or long periods of unemployment and perhaps another 15 percent ended up with higher pay.

Mr. Barfield asked how much liberalization of services the agreement contained. Mr. Schott responded that while there was some liberalization in telecom and financial sectors, overall there was little liberalization in services. He added that Korean negotiators had services at the center of their focus, but not much detail was available. Mr. Schott also questioned Hufbauer’s Table 1 and suggested that it was the addition of China that had resulted in so much recent trade exposure.

Mr. Alexander commented on the direct cause-and-effect approach taken by earlier speakers, including Stern, Hufbauer, and Krueger. He drew an analogy from recent medical-epistemological findings, which led him to point to recent articles in the economic literature that cast doubt on whether growth has indeed been driven by such traditional economic factors as investment, trade, opening financial markets, and other familiar issues. That literature suggests that growth is instead explained by largely noneconomic factors such as institutions, domestic policies, and a general opening to competition.

Mr. Hatekayama returned to the potential dynamic effects of the KORUS FTA on other current FTA proposals in East Asia, specifically the two centering on the Association of Southeast Asian Nations (ASEAN) as well as the broader Asia-Pacific Economic Cooperation (APEC) format. He asked whether the KORUS FTA would accelerate one or the other of them, especially APEC. He suggested the United States has “not been too happy” with the first two because it is excluded from both ASEAN + 3 (the 3 comprise Japan, China, and Korea) and ASEAN + 6 (which further adds Australia, New Zealand, and India). Thus, his question was whether his speculation was correct that U.S. unhappiness had led it both to the KORUS FTA—about which the United States was "very happy"—and to its new interest in an APEC-based FTA because the KORUS FTA could lead others to a heightened interest in an APEC-based format.

Mr. Hufbauer responded to several discussants' points. He agreed first with Professor Krueger's view that globalization leads to less friction than FTAs. His study had used the gravity model because the "typical CGE models overstate the trade diversion effects." Regarding Table 1, he agreed with Mr. Schott that China's recent role does indeed account for the big expansion in trade. Regarding Mr. Alexander's speculation about "something else" going on, Mr. Hufbauer concluded nevertheless that "trade in fact does cause higher GDP," and as to whether it was "trade policy" or something else, he concluded that trade policy is responsible for about half of trade growth. Professor Krueger added that in the Korean case there was "no way" it could not have been an important factor.

Mr. Bergsten agreed with Mr. Hatekayama's suggestion that, for reasons going beyond Korea, the United States is "very happy" about the KORUS FTA and added that "it's fair to say the United States has become increasingly concerned about Asia-only agreements." In terms of their quality and coverage, however, he differentiated among them: the ASEAN-China agreement is "low quality and highly politicized," whereas the United States will aim for, though may not always achieve, a high-quality agreement. He characterized the Japanese Economic Partnership Agreement model, which excludes agriculture but includes technology, as falling between those poles.

Mr. Bergsten added that the Asia-only agreements are a good concept per se, but for reasons bearing on potential U.S. exclusion from East Asia, they have potentially negative implications. For that reason he had urged continued attention to the Free Trade Area of the Asia-Pacific (FTAAP) concept and believed that President Bush's recent endorsement of the FTAAP approach probably grew from that same concern. He believed both approaches could and should proceed simultaneously and that the KORUS FTA could be a prototype test if it promotes competitive liberalization elsewhere. That will ultimately put pressure on those outside the region, specifically Europe, Brazil, and India, to make progress in the WTO-Doha framework. Mr. Bergsten concluded that this is "the logical progression" from the theory of competitive liberalization; if successful it will have profound effects both on the Asian neighborhood and ultimately on global multilateral free trade, and it may also be the most practical path.

Professor Sungjoon Cho responded that if competitive liberalization is akin to the "building-block approach" that is a good thing because it leads to the universally desired multilateral outcome. But if competitive liberalization stops before that, the result will be "just a sea of small and large FTAs" that bring highly complex and burdensome rules of origin. Adding to a point made earlier by Professor Krueger, he said that those rules of origin hurt international business, now segmented in many niches in the production cycle, and hamper the entry of smaller actors—both companies and national economies. Overall, he expressed doubtful views on both bilateral and regional trade agreements and added that, although trade liberalization is an important part of globalization, it is not everything. In that respect he drew on the Korean case, a society that already had a strong work and educational ethic. Those two factors, along with the impact of globalization on labor productivity and education, had contributed significantly to Korea's economic growth.

Mr. Mustafa Mohatarem responded that rules of origin difficulties had been overstated; in his experience international business adapted, as it had in the NAFTA case and others. Likewise, he was concerned to hear echoes of "10 years ago" when there were fears the world would devolve into three trade blocs: "it didn't happen then and it won't happen now."

Mr. Schott voiced strong agreement with Mr. Mohatarem and added that all the trade-based arrangements now being proposed in East Asia, as well as those such as APEC that came before, have been rooted in political objectives. The same was true regarding the origins of the EU. Moreover, he pointed out that multilateralism in practice has always contained a large dose of bilateralism. He introduced the issue of Taiwan, which indeed is now being discriminated against by the regional and bilateral proposals under discussion. It is included only in APEC, which is an added reason for supporting that approach.

Mr. Bergsten characterized the doubts about bilateralism and regionalism posited by Professor Cho as having raised the fundamental question: How can we be sure the bilateral-regional approach will lead to the multilateral solution? We can't, but the problem represents a management issue for the major countries. He recalled that Professor Cho had been critical of Robert Zoellick's strong support for those regional and bilateral initiatives, and Mr. Bergsten responded that under Robert Zoellick the United States had "taken the lead to keep Doha on track, and the United States can be counted on to continue to do that."

In that context, Mr. Bergsten agreed with Mr. Mohatarem that the continuing central role of the United States is assured because every trading partner, including the EU, is aware of its reliance on the U.S. market. He also agreed with Mr. Mohatarem that the global trading interests of all the trading powers leads them to a global approach, although it is "easier" to do bilateral deals as in Korea, which took less than a year, whereas Doha has after five years produced just a "mouse." We cannot be certain that, although all the tracks will reinforce one another and we recognize that the process of trade liberalization is messy and takes a tortuous course that includes diversion issues such as rules of origin, it reflects the revealed preference of governments around the world. Most important, it is going in the right direction.

Professor Cho, although in general agreement on the ultimate multilateral goal, pointed nevertheless to two aspects of U.S. trade policy practice that were inconsistent with that goal. First, the United States had antagonized others by its emphasis, most evident when Robert Zoellick was United States Trade Representative, on what Zoellick had called the "can-do" countries. Second, Zoellick's emphasis on bilateral deals focused congressional and administration time and energy on single deals that required large expenditures of political capital and diverted from the main multilateral arena.

Mr. Hufbauer added that the issue of rules of origin raised by Professor Cho had been further complicated by security rules, and the net effect was that the losers are "small companies and small countries." Indeed the weight "has moved to large companies, and it is a hyper function." He pointed to Taiwan as one example, and cautioned that if other small countries "don't happen to be on the winning side, they will be left out."

Panel III: Scope for Dynamic Effects in Korea's Economy

Moderator: Jack Pritchard
Presenters: Arthur Alexander, Georgetown University
Sungjoon Cho, Chicago–Kent College of Law
Yong Kim, University of Cincinnati (speaking on behalf of Kang Hee-joon, Indiana University)
Discussants: Claude Barfield, American Enterprise Institute
Choi Nakgyoon, Korea Institute for International Economic Policy

"Dynamic Consequences of a Korea-U.S. Free Trade Agreement:Foreign Direct Investment" by Arthur Alexander

Mr. Alexander's presentation returned the conference's attention to issues relating primarily to the Korean economy, and he set the context by showing patterns of growth relative to FDI. With reference to Japan, Korea, and the United States, he introduced charts that illustrated per capita growth, annual 10-year growth of real GDP per capita, and the share of manufacturing output in GDP. He noted that Korea had been "a laggard" in FDI and pointed out that, as its earlier rapid growth slows, the importance of productivity and hence the need for FDI increases. The importance of the KORUS FTA relates to productivity change, which requires greater openness and greater competition, and in that respect the FTA is coming at the right time for Korea. There were important comparisons with FDI in Mexico prior to and after NAFTA, when FDI shot up following a relatively brief economic crisis. For Korea, now approaching economic maturity, FDI has the potential to be a stimulant to productivity improvements. But Korea will need to guard against FDI restrictions pertaining to domestic content, joint ventures, and technology sharing.

"Is a Free Trade Agreement a Royal Road to Prosperity? Demystifying Trade Regionalism" by Professor Sungjoon Cho

Professor Cho's presentation expanded on the conference's second perspective, first laid out by Professor Krueger. He focused on the legal, governmental, and political challenges posed by the KORUS FTA, and, as the only noneconomist among the paper presenters, Professor Cho said his remarks and paper were from a lawyer's perspective. In that context he recalled four background points: (1) "the global trading system has recently been inundated by a sea of regional trade agreements (RTAs)—176 [of them]—since the launch of the WTO in 1995"; (2) "economists generally believe that RTAs are inherently inferior in trade creation to a multilateral trading system"; (3) all RTAs present tensions to WTO norms, specifically Article 24 of the GATT that "stipulates rather draconic requirements to legalize free trade areas"; and (4) despite those strictures, "not a single RTA has ever been rejected for violating the Article."

In contrast with the view that RTAs "put pressure on nonmembers . . . to conclude broader agreements," Professor Cho suggested that approach "risks depriving nonmembers of the incentives . . . to promote the multilateral trading system." He amplified Professor Krueger's earlier criticisms of rules of origin and said that, if Korean manufacturers produce goods more cheaply in China than in Korea, the KORUS FTA, using complicated rules of origin, "prohibits such trade deflection."

More broadly, he cautioned that China, in the name of "defensive regionalism," will counter America's "bilateralist-regionalist trade policies," and the result "may provide a recipe for economic balkanization [and] political tensions." He added that China and the United States "have enough issues, ranging from China's increasing military spending to Taiwan, to make this speculation plausible." He concluded that, nevertheless, as a fait accompli the agreement should be ratified, that Korea will need to intensify regulatory reforms to deal with it, and that both governments should aim to "multilateralize" their bilateral commitments to other major WTO members. In sum, he argued, "we should manage and contain FTAs, rather than promote them."

"Regional Integration and a Free Trade Agreement among China, Japan, and Korea" by Professor Kang Hee-joon

Professor Kang's paper was presented in his absence by Professor Yong Kim, who outlined the case for a tripartite FTA, which he termed a FEAFTA (Far Eastern Asia

FTA) and which is based on the gravity, or proximity, model. Professor Kim noted that intra–East Asian trade had grown much more rapidly than trade within NAFTA and within the EU, and that each of the three putative participants in FEAFTA has "initiated trade talks towards the establishment of FEAFTA." He concluded that since Korea "will gain the most . . . Korea has the strongest incentive" to embark on a formal negotiation.

Comments of Discussant, Claude Barfield

Mr. Barfield focused principally on the Cho paper and disagreed with its views that bilateralism and regionalism reflected "embedded mercantilism" and that FTAs had brought the WTO Doha Round to a halt. He asserted instead that the Doha Round's problems were intrinsic to the WTO and, despite Professor Cho's concern that nations might "game" the WTO (Mr. Barfield said he and others had issued earlier warnings of this), "it didn't happen that way"; neither had the "spaghetti bowl" effect materialized. He also disputed Professor Cho's discussion of an FTA legal vulnerability to GATT Article 24 and said, "if the [WTO] dispute settlement system tries to screw around with the FTAs, it will destroy the system." He had less disagreement with Professor Cho regarding rent-seeking by pharmaceutical and services sectors in U.S. FTAs, but he concluded that "by and large it goes the other way" and that "it is simply not true that the U.S.A. has been protectionist and isolationist." Separately, Mr. Barfield also disagreed with Professor Kang's paper about the "inevitability" of FEAFTA.

Comments of Discussant, Choi Nakgyoon

Mr. Choi commented first on the paper by Mr. Alexander and, on the basis of his own studies of the KORUS FTA, agreed that under all models productivity will improve and that the effects of FDI are real. He cautioned that for Korea, however, such FDI must enhance spending on research and development and human capital. With regard to Professor Cho's paper, he agreed that the multilateral framework is preferable to FTAs, but he concluded that both approaches are compatible; he also commented approvingly about the inevitability of the FEAFTA concept as described in Kang Hee-joon's paper.

Response of Presenter, Professor Sungjoon Cho

Professor Cho thanked Mr. Barfield for his comments and responded to several points: (1) As a Korean trade negotiator in Geneva, he had observed the diversion of political and administrative resources from multilateral to regional efforts and believed this also affected the USTR; (2) his reference to "embedded mercantilism" was questioned, but the term is not new and the protectionism it reflects affects both multilateral and bilateral negotiations, and, owing to the power difference between the two parties, it is more severe in bilaterals; (3) his reference to "gaming" the WTO system had been questioned, but as a negotiator he had seen it reflected in artificial bargaining chips, timing modalities, and similar examples; (4) the WTO dispute settlement system he had cited and that had led Mr. Barfield to warn it could destroy the WTO had been specifically approved by Uruguay Round negotiators as the method that would be used to resolve Article 24 trade differences; and (5) his reference to U.S. protectionism was questioned, but he recalled that, although U.S. negotiators regularly emphasized America's trade openness (which he did not deny), its trade policy in practice responded to local and specific protectionist initiatives, and he noted that farm subsidies emanated from just 22 congressional districts. Finally, while Mr. Barfield had mentioned nongovernmental organizations, Professor Cho had not; his concern was instead with democratization and was similar to Professor Krueger's earlier published observation that the costs of protectionism would be reduced if more Americans were aware of it.

Comments of Other Conference Participants

Mr. Stangarone, drawing on his congressional staff experience, suggested that in the trade context the concept of "political capital" had been misunderstood. Elected members of Congress, when asked to support several separate small-economy FTAs, face greater challenges than when presented with a single large-economy trade deal. Both may contain labor and environmental objections, but a "substantial deal" such as the KORUS FTA is in the second category. Its upsides are sufficient business opportunity and jobs benefits to which a member can point in order to override those objections, and those upsides provide the political capital on which the member of Congress can draw. And on the often cited slow pace of the Doha Round vs. the relative speed made in the KORUS FTA talks, he concluded that the parties had shifted their resources according to where they believed there was the most potential gain.

Mr. Mustafa Mohatarem recalled that in Korea-China FTA talks, both delegations first stressed categories to be excluded; along with Japan they were principally export oriented. In that context he was still surprised a KORUS FTA had been achieved and that a consequence is that it will force Japan to rethink its stance toward a free trade area with the United States. He also remarked that the FEAFTA plan involving Korea, Japan, and China discussed in Professor Kang's paper had too many political obstacles to move forward and that on the issue of mercantilism all three are mercantilist.

Mr. Hufbauer first jokingly suggested to Professor Cho that, as a professor of law, the complexity he attributed to FTAs might be a good thing because "it keeps the lawyers working." To Mr. Alexander he affirmed again that there is a strong connection between FDI and trade, and that FDI enhances trade growth. On the issue of "gaming the WTO," which had been raised by Professor Cho and questioned by Mr. Barfield, Mr.

Hufbauer said that indeed there was gaming, and it was now being practiced by India at the WTO.

Mr. Stern noted that U.S. multinational corporations had been strong supporters of the KORUS FTA but had not similarly pressed harder for progress in the Doha Round, and he concluded that those multinational corporations believed there was more to be gained, at least in the short run, from FTAs.

Mr. Koo recalled that Lester Thurow at MIT had written on the likelihood of three global regional blocs, and that East Asia, with India later included, would represent the world's largest bloc. This led the United States to promote an FTA with Korea, which would lead Japan to eventually want an FTA with the United States, and that Korea would move for an FTA with China and then with the European Union. He concluded that this wouldn't create global "regionalism" but would promote globalization.

Mr. Schott said he was "disappointed" with the "confusion" and "emotional" content of the discussion on regionalism and multilateralism, and that it was "stunning" that Korean voices had charged the United States with protectionism, while "Korea has done so little to advance Doha." To Professor Cho's view of a disjuncture between U.S. foreign policy and its trade policy, Mr. Schott said an obsession with Iraq had brought it about, but it had not affected East Asia, and for that "you should be grateful." He further agreed with those who had said U.S. business sees little to gain from the Doha Round and therefore has embraced regional and bilateral efforts, and he explained that what has damaged Doha has been a "dumbing down" process that had settled for minimal goals.

Mr. Barfield said Robert Zoellick had recognized the intimate connection in East Asia between trade and security issues, and that the KORUS FTA, which could help avoid Korea's drift from the United States, reflected the connection.

Mr. Choi said the U.S. business community found little reason for confidence in past Korean government actions on trade agreements and, referring to the boneless-beef issue, said there was reason to worry that Korea will not implement fully the KORUS FTA.

Mr. Alexander concluded that indeed FDI does cause growth, and he argued that some prior studies "hold too much constant."

Professor Yong Kim, who had spoken on behalf of the Kang Hee-joon paper, said the FEAFTA concept was a good one but urged that its view of "inevitability" be taken with "a grain of salt."

Professor Cho spoke last and, in response to Mr. Schott, indicated he was not opposed to regionalism per se, but he insisted that the concept of multilateralism was worthwhile and therefore urged that political capital be used on its behalf.

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