

Advancing East Asia's Trade Agenda: A Korean Perspective

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According to the WTO, in 2018 there are 459 regional trade agreements, the most in the institution's recorded history.¹ Countries are now more actively engaged in regional trade agreements as a policy option to achieve their outward growth strategy. In addition to efforts to build up trade and investment links, regional integration is expected to spill over to more complicated socioeconomic issues, covering a wide range of areas such as gender, environment, labor, and cultural exchanges. Given this upsurge, policy coordination within the framework of regional agreements has attracted considerable attention from policymakers and other stakeholders. This is certainly the case in Korea, where the promise of such agreements is widely recognized, and recent challenges are actively discussed in the hope of overcoming them.

Regionalism is a relatively new concept for most East Asian countries.² Through most of the 1990s, East Asian countries generally engaged in regional integration discussions as a pathway to eventual multilateral trade liberalization under the auspices of the ASEAN and ASEAN+ processes. The subsequent proliferation of FTAs was the result of a number of economic and political factors, which had much in common with similar processes in other world regions, but advanced with particular intensity in East Asia and states closely connected to it. Today, all Asia-Pacific economies are involved in the regional economic process and are active participants in the establishment of multilayered FTAs.

The growing interdependence and interconnectedness of the global economy has intensified the need for most East Asian countries, including Korea, to engage in regional economic cooperation and integration. Korea's high dependency on trade explains its preference for the rapid expansion of regional trade agreements. This chapter begins with a review of the trends, key characteristics, and implications of East Asian economic integration, followed by an examination of potential opportunities and challenges facing regional integration. Korea's FTA strategies are then reviewed, and its expected role in advancing the regional trade agenda is addressed.

Regional Economic Integration in East Asia

Proliferation of Trade Agreements in East Asia

Despite remarkable economic and political developments, East Asia was slow to institutionalize regional economic cooperation until the latter part of the 20th century, opting to support the multilateral trading system as did most of the world at this time. Forming free trade agreements (FTAs)/regional trade agreements (RTAs) was not popular until the late 1990s except for the ASEAN Free Trade Area (AFTA) which came into force in 1992. Table 1 shows the number and types of FTAs/RTAs of the 21 APEC member economies. As of March 2017, 141 FTAs/RTAs, both intra- and inter-regional, were in force in East Asia.³

There are two reasons for the proliferation of FTAs/RTAs in East Asia. First, the slow progress in multilateral trade liberalization under the WTO has been responsible for the proliferation of FTAs not only in East Asia, but also in other parts of the world. Despite many years of effort, trade liberalization under the WTO has become increasingly difficult and has come to a halt. Faced with the difficulty of pursuing trade liberalization on a global scale, many countries have opted to form FTAs with like-minded countries. Countries that did not originally sign FTAs feared being left out of accessing foreign markets and quickly

Table 1: Types of FTAs/RTAs in the Asia-Pacific Region								
	Active FTA/RTA				Signed (Pending Ratification)		In Talks	
	Type		Partner		Type		Partner	
	Bilateral FTA	RTA/ Others	Intra-Regional	Inter-Regional	Bilateral FTA	RTA/ Others	Bilateral FTA	RTA/ Others
NORTHEAST ASIA								
China	12	4	11	5			1	
H.K, China	3	1	3	1				
Japan	14	1	12	3			1	2
Korea	13	6	13	6			2	
Chinese Taipei	5	2	3	4				
SOUTHEAST ASIA								
Brunei Darussalam	1	7	7	1				
Indonesia	1	6	6	1				2
Malaysia	6	7	9	4				1
Philippines	1	8	6	3				1
Singapore	12	10	14	8			2	1
Thailand	4	7	8	3				2
Vietnam	3	7	8	2				3
OCEANIA								
Australia	10	2	11	1				1
New Zealand	8	3	10	1			1	
WESTERN HEMISPHERE								
Canada	9	2	3	8	1		2	3
Chile	22	5	12	15				
Mexico	7	8	4	11			1	
Peru	11	6	8	9				
USA	12	2	6	8				1
OTHERS								
P.N.G	1	4	1	4				
Russia	7	4		11			1	2

Note: Partial scope agreements are included in this table.
Source: <http://rtais.wto.org/UI/PublicMaintainRTAHome.aspx>

endeavored to join existing FTAs or create new ones. By doing so, they tried to overcome possible discrimination and secure markets for their exports. By the mid-1990s the world's leading economies except those in East Asia had become members of FTAs. Indeed, both of the world's two largest economic regions—North America and Western Europe—formed RTAs. In order to maintain and expand market access for their exports, East Asian countries have become active in forming FTAs since the late 1990s.

Second, political factors played an important role in stimulating the proliferation of FTAs/RTAs in the region. For example, combining security or other political interests with benefits of trade, serves as a driving force of forming FTAs/RTAs. The rise of China and China-Japan-Korean rivalry in global exports is one example. An intensifying rivalry between China and Japan, Japan and Korea, and Korea and China aimed at maintaining markets made them pursue an FTA strategy to strengthen their relationships with major trading partners. ASEAN and China, Japan, and Korea themselves have come to use FTAs as a means of maintaining their economic influence in East Asia.

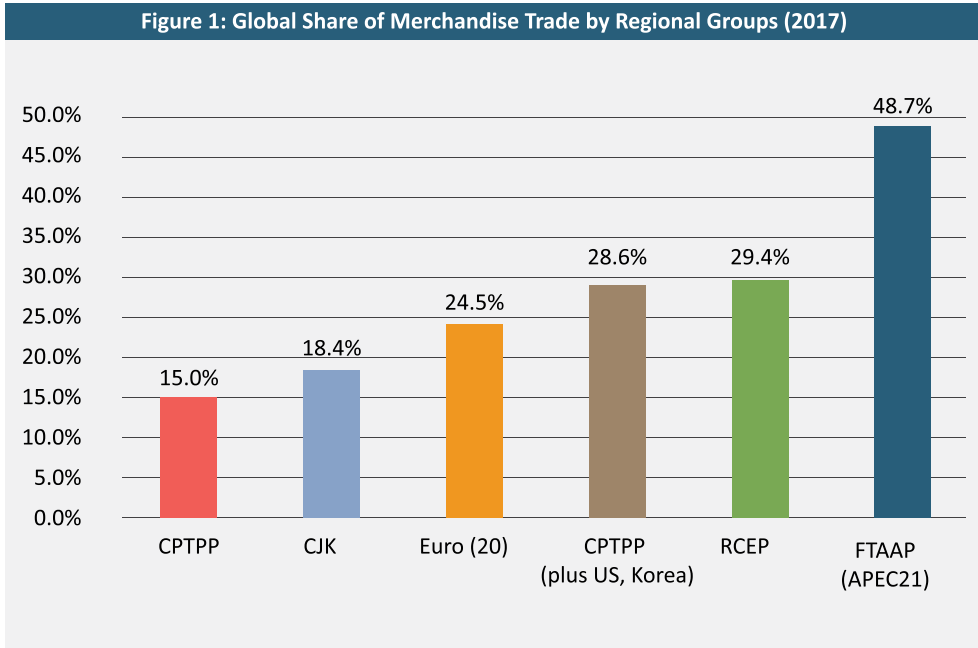
Moving Towards Deeper Regional Economic Integration: Opportunities and Drawbacks

The number of FTAs/RTAs in force in East Asia has increased rapidly. There are also many agreements which involve East Asian countries and the rest of the world. Traditionally, the majority of the ASEAN members, except Malaysia and Singapore, heavily relied on intra-regional negotiations, taking advantage of geographic proximity. However, the region's interest in strengthening inter-regional linkages is rising as information and communication technologies have spurred the restructuring cycle of the global value chains (GVCs), which saves transaction costs and makes geographical distance less important.⁴ GVCs help to avoid regional trade networks from being insulated from one another, and for the Asia-Pacific this means there is less risk of a line being drawn between the eastern and western hemispheres.⁵

In fact, the East Asian region's inter-regional linkage with the rest of the world, especially with the western hemisphere, is being intensified with the completion of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) negotiations, notwithstanding the Trump administration's withdrawal from the Trans-Pacific Partnership (TPP). Japan and almost half of the ASEAN member countries are participating in this ambitious process without U.S. engagement. The Regional Comprehensive Economic Partnership (RCEP) is serving as a hub for five ASEAN + 1 FTAs with the potential of providing options to deepen both East Asia's intra-regional and inter-regional economic integration.

Trade agreements, however, do not always necessarily contribute to a larger positive growth environment. Assessing whether the proliferation of trade agreements in East Asia is desirable for the region requires the agreements to satisfy two conditions. First, they should demonstrate significant trade creation and not trade diversion. Second, the agreements should demonstrate the potential to be consolidated into a larger-scale RTA as a stepping stone—not a stumbling block—towards global free trade.

The consolidated trade share by individual regional groups (China-Japan-Korea—CJK: 18.4 percent; and CPTPP with Korean and U.S. accession: 28.6 percent) is large enough to create a positive trade creation effect. The ASEAN market is developing at a rapid rate. The potential growth rate of the Asia-Pacific (excluding the Western Hemisphere) was around 7.2 percent in 2013-17, about twice as high as the average for other emerging market developing economies.⁶ The combined market share and growth potential of the Asia-Pacific in part meets the first criterion of the agreements being beneficial for the region. The Composite



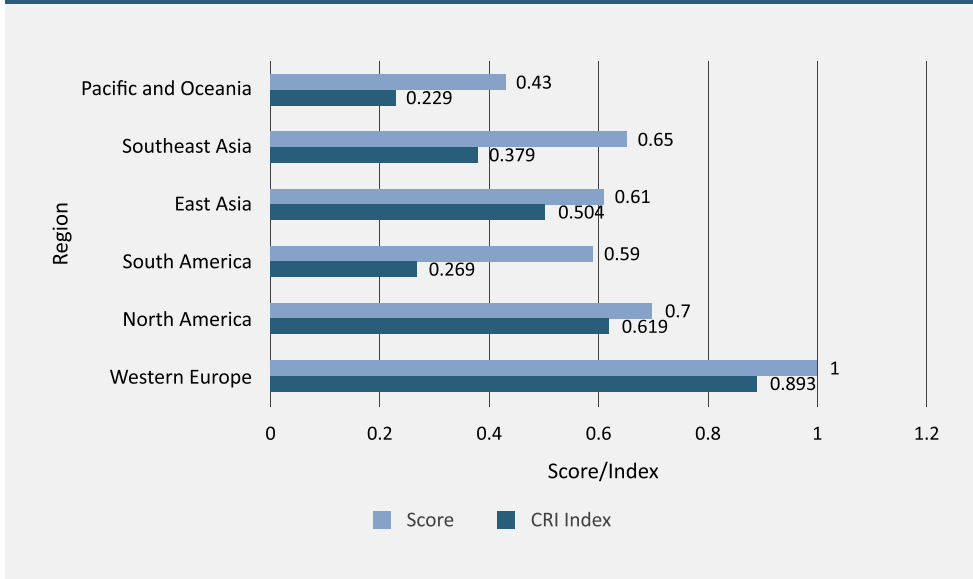
Note: Calculated by author

Source: IMF Direction of Trade (<http://data.imf.org/regular.aspx?key=61013712>)

Regional Integration (CRI) Index may also serve as convincing empirical evidence to support the argument that East Asian markets have great potential to grow into a larger scale market. Figure 2 introduces the CRI Index,⁷ which can be used as the basis for assessing the region's potential for further economic integration. As Figure 2 indicates, the level of economic integration for Western Europe (EU members), North America (Canada, Mexico and the United States), and East Asia is 0.89, 0.70 and 0.50 respectively. If we assume that Western Europe has reached its full potential of integration, with a normalized value (score) of 1, East Asia's normalized score can be calculated as 0.61. If we follow Naeher's argument, East Asia possesses the untapped potential of further integration by 39 percent, based on currently available resources and institutional conditions.⁸ Although we have to be very cautious when dealing with incomplete empirical evidence, taking the missing institutional linkages among China, Japan, and Korea into consideration, we find that the combined capacity of CJK is very high.

As the network of existing trade agreements in East Asia creates a positive growth environment for the region, there is potential to consolidate them into a larger scale RTA, such as the Free Trade Area of the Asia-Pacific (FTAAP). A CPTPP engendering greater openness is one of the most desirable pathways for the region, along with RCEP. The flexibility adopted by the Korea-U.S. FTA (KORUS FTA) in terms of coverage, scope, and timing of tariff elimination may provide a good precedent for the successful implementation of an FTAAP. However, in order to increase the feasibility of an FTAAP, the following obstacles need to be addressed.

Figure 2: Regional Integration Potential, Composite Regional Integration Index



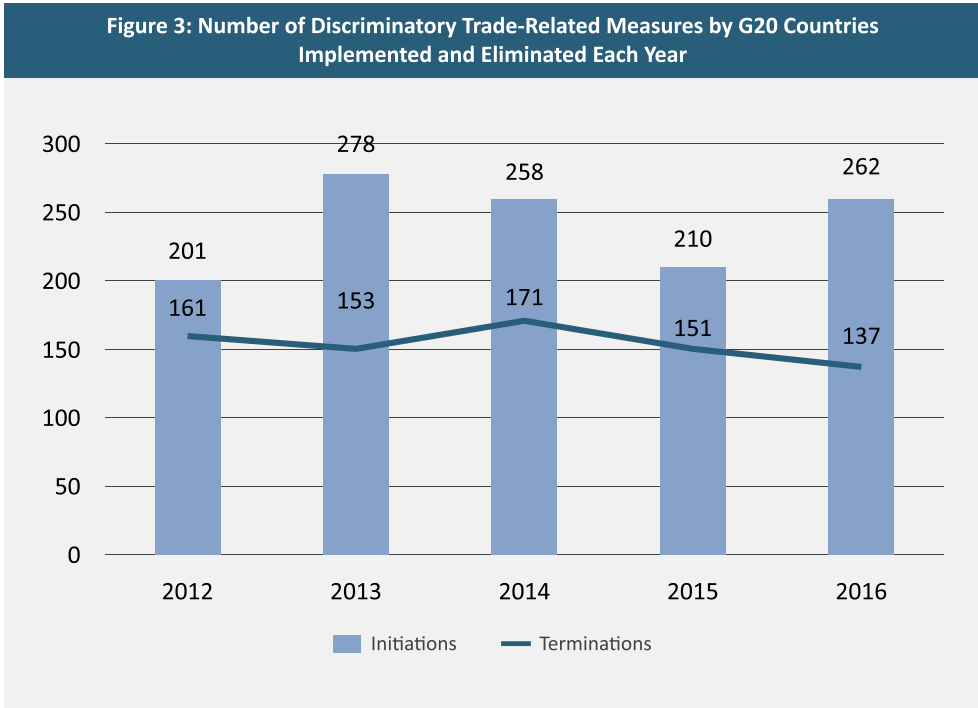
Source: Naeher (2015)

First, the most fundamental obstacle is the heterogeneity among East Asian countries and the lack of community spirit and political leadership, which makes it very difficult to envisage a proper institutional architecture for East Asian integration. Sometimes, domestic issues such as regulation or competition policy and institutional issues are factors that weaken the competitiveness of an economy, which may become an impediment to an FTAAP.

Second, many cooperation agreements have no specific work plan, time schedule, or review mechanism. Recently, East Asian economies have tended to seek high quality and comprehensive agreements. However, there are not many FTAs/RTAs in East Asia containing chapters on next generation issues and behind-the-border reforms. Many agreements include liberalization of trade in services in their agenda but contain few provisions beyond the commitments of the Trade in Services Agreement (TiSA).

Third, complex rules of origin (ROOs) could disrupt the cross-border production networks which have been central to the region's successful integration. Uncoordinated proliferation of FTAs may lead to inconsistent provisions in FTAs—especially ROOs—which could hamper the process of production networking across countries.

Fourth, the spread of protectionism, especially increasing numbers of trade remedies imposed by developed countries (see Figure 3), is a great threat to most East Asian countries and may produce adverse effects for domestic reform agendas. Policy uncertainty imposes a significant additional cost and since the launch of the Trump administration, U.S. economic policy towards East Asian markets and its engagement in the Asia-Pacific integration have become more ambiguous.



Note: Prepared by author
 Source: Data from Table 3.2. WTO-OECD-UNCTAD (2017) Reports on G20 Trade and Investment Measures.

Korea’s FTAs/RTAs Networks and Strategy

Korea’s interest in FTAs began with the conclusion of NAFTA, then grew with proliferation of RTAs in the Asia-Pacific. As of early 2018, Korea has concluded 16 FTAs/RTAs with 52 trading partners,⁹ of which 10 are with members of APEC (Table 2). As shown in Figure 4, Korea’s dependency on overseas markets is very high. As of 2015, 84 percent of the Korean economy is open to international markets. It is also noteworthy that Korea’s trade coverage with its FTA partners was 68.2 percent in 2017, up from 0.6 percent in 2004 when Korea’s first FTA with Chile went into force (see Figure 5).

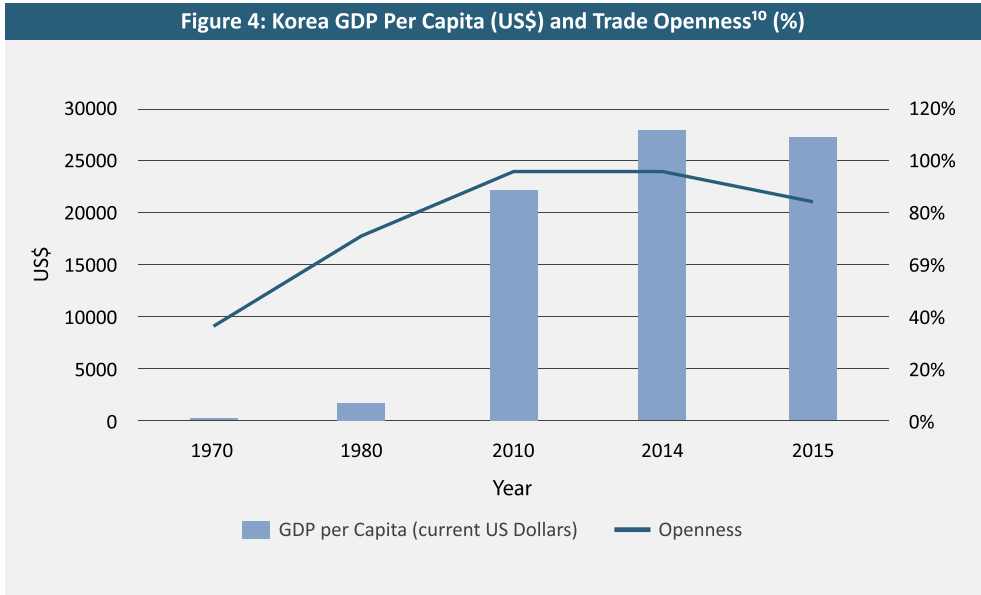
Korea became the first East Asian country to have FTAs with the United States, China, and the EU. Korea’s most recent agreement was signed with Central American countries (Costa Rica, El Salvador, Honduras, Nicaragua, and Panama) on February 21, 2018. The deal is expected to strengthen Korea’s formal linkages with Central America and the Southern Cone. Furthermore, as Korea is currently negotiating four FTAs, including RCEP, Korea’s trade dependency and trade share with its FTA partners will clearly be rising. Behind this backdrop, one of Korea’s strategic goals of participating in regional economic integration activities is to strengthen its economic credentials not only in the Asia-Pacific, but globally.

There are many explanatory factors why Korea has switched its policy stance from a single-track to a multi-track approach to pursuing FTAs. First, FTAs are effective tools to eliminate trade barriers and to promote the restructuring of trade and industrial structures. Second, successful regulatory reforms and conformity to the international rules and standards

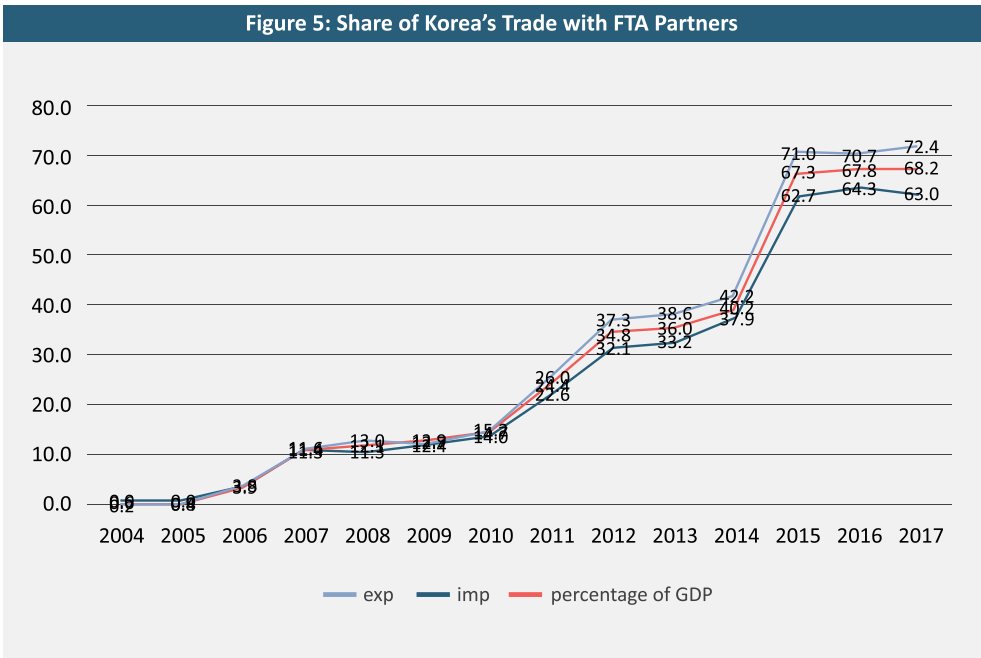
Table 2: Korea's FTAs and Partners	
Name of FTA/Partner	Date Entry into Force
Korea - Chile Free Trade Agreement	1 April 2005
Korea - Singapore Free Trade Agreement	2 March 2006
Korea - EFTA Free Trade Agreement	1 September 2006
Korea - ASEAN Free Trade Agreement	1 June 2007
Korea - India CEPA	1 January 2010
Korea - EU Free Trade Agreement	1 July 2011
Korea - Peru Free Trade Agreement	1 August 2011
Korea - USA Free Trade Agreement	15 March 2012
Korea - Turkey Free Trade Agreement	1 May 2013
Korea - Australia Free Trade Agreement	12 December 2014
Korea - Canada Free Trade Agreement	1 January 2015
Korea - New Zealand Free Trade Agreement	20 December 2015
Korea - Vietnam Free Trade Agreement	20 December 2015
Korea - China Free Trade Agreement	25 December 2015
Korea - Columbia Free Trade Agreement	15 July 2016
Name of FTA/Partner	Date Signed
Korea - Central America Free Trade Agreement	21 February 2018
Under Negotiation	
China-Japan-Korea	
RCEP / Korea - Ecuador SECA / Korea - Israel	
Pending Negotiations	
Korea - Japan / Korea - Mexico / Korea - Mercosur / Korea - GCC / Korea - EAEU	
Number of active and/or signed agreements (15 active, 1 signed)	

embodied in an FTA framework accelerate the restructuring and opening of the Korean economy. The global financial crisis provided an additional rationale for this policy stance. To compensate for contracted export markets, Korea sees the implementation of agreed reforms locked in by FTAs as helping to enhance the resilience of the economy against external shocks and sustain stable economic growth. Third, in contrast to multilateral approaches, the formation of FTAs has offered Korea a quick and efficient prescription to resolve issues with trade partners.

In order to implement its policy goals, Korea has developed the following FTA strategies since it designed the first FTA roadmap in 2003 in its FTA with Chile. First, Korea developed simultaneous negotiation capacity to reduce the costs of putting several deals on the table at the same time to build a multi-track framework. Second, Korea is targeting comprehensive and high-quality FTAs. The KORUS FTA serves as a template for an ambitious trade deal for the region. In addition to chapters related to labor, environment, and corruption issues, it includes provisions to facilitate e-commerce. Third, disseminating FTA-related information to the public and gathering the opinions of interested groups are mandatory at each stage of the process. This helps to ensure support from stakeholders in the Korean industrial and agricultural sectors.



Source: <http://www.kostat.go.kr/portal/eng/index.action>



Source: <http://www.kostat.go.kr/portal/eng/index.action>

Perspective on East Asian Economic Integration and Korea's Contribution

Despite various economic and political challenges in the region, FTAs/RTAs continue to grow into Mega FTAs, such as RCEP and the CPTTP. It is still an open question if East Asian regional FTAs/RTAs could converge successfully into a region-wide FTA, which would incorporate both sides of the Pacific into a single institutional architecture. Korea will continue to play a meaningful role in advancing the trade agenda in East Asia, hoping that any trade agenda can move forward if provided with the right kind of prescription and policy coordination. The following is Korea's perspective on East Asia's regional integration activities and on their expansion towards larger-scale inter-regional Mega FTA envisioned for the formation of an FTAAP.

First, as stated earlier, the formation of high-quality FTAs/RTAs has offered Korea a way to resolve issues that would be more difficult to tackle in the wider multilateral context. Korea pursues comprehensive and high-quality trade agreements encompassing services, investment, telecommunications, and the digital economy, and is open to a deal with any meaningful reform agenda as long as it is mutually beneficial and reinforced. Empirical findings support the benefits of this policy stance; the most comprehensive trade agreements yield the greatest economic benefit. More specifically, Park and Park measure the economic impact of East Asian integration and reported that the benefits are greater if it is converged into a larger scale FTA, which is comprehensive in coverage (Table 3).¹¹ As Table 3 clearly demonstrates, an FTAAP yields positive outcomes but size varies by scenarios. Peter Petri and Michael Plummer attempted to estimate the economic effect of the concluded TPP. They found, under the assumption that it would be fully implemented by 2030, the TPP would increase annual real incomes in East Asian countries by \$203 billion, or 0.4 percent of GDP, and annual exports by \$509 billion, or 4.3 percent of exports.¹² The positive gains from larger-scale, comprehensive, and high-quality FTAs, similar to TPP, are expected to be significant enough to invite all Pacific Rim economies to consider joining, judging solely from economic concerns.

Second, there has been much effort in support of economic integration in East Asia as well as the endeavor to establish region-wide FTAs, i.e. TPP, RCEP and CPTTP. In terms of trade liberalization and elimination of trade barriers, East Asia has achieved a great deal of progress. However, "eliminating trade barriers" is only one aspect of enhancing economic integration, while there is a remaining but still very important arena that requires further cooperation among East Asian countries, which is reducing behind-the-borders impediments. Korea is well aware that promoting and strengthening structural reforms are a prerequisite for achieving sustainable economic growth in East Asia. By improving the functioning of markets, successful reforms would remove impediments to the full and efficient use of resources, helping economies achieve higher productivity and living standards. Reforms establishing transparent and impartial regulatory frameworks would also boost business and investor confidence in an environment of global economic uncertainty. The 1997 Asian financial crisis was attributed mostly to a lack of institutional, regulatory, and structural reforms to enable the economy to successfully manage the challenges presented by economic shocks and market instability.

Table 3: Effects of an FTAAP on APEC as a Whole: Comparison by Models and Scenarios						
		Real GDP	Welfare	Welfare (Million US \$)*	Export	Import
Absolute Effects (% deviations from the Base)						
Static CGE Model	Scenario I	0.10	0.16	57,713	2.16	2.20
	Scenario II	1.24	1.44	493,239	6.21	6.12
	Scenario III	1.28	1.49	511,009	6.38	6.28
Capital Accumulation CGE Model	Scenario I	0.40	0.38	130,001	2.45	2.49
	Scenario II	3.45	3.09	1,057,161	9.31	9.24
	Scenario III	3.54	3.18	1,088,271	9.55	9.48
Relative Effects to Scenario I (Ratio)						
Static CGE Model	Scenario I	1.00	1.00	1.00	1.00	1.00
	Scenario II	12.4	9.0	8.5	2.9	2.8
	Scenario III	12.8	9.3	8.9	3.0	2.9
Capital Accumulation CGE Model	Scenario I	4.0	2.4	2.3	1.1	1.1
	Scenario II	34.5	19.3	18.3	4.3	4.2
	Scenario III	35.4	19.9	18.9	4.4	4.3
Relative Effects to Scenario III with Static CGE Model (Ratio)						
Static CGE Model	Scenario III	1.00	1.00	1.00	1.00	1.00
Capital Accumulation CGE Model	Scenario III	2.77	2.13	2.13	1.50	1.51

*Deviation from the base. / Note: Scenario I: Tariff Elimination / Scenario II: Scenario I + 5% Reduction in Trade Cost by Trade Facilitation / Scenario III: Scenario II + Reduction in Tariff Equivalents of Services by 10%
Source: Innwon Park and Soonchan Park. 2016. "Economic Effects of an FTAAP: CGE Model Analysis. Unpublished paper present to APEC CTI for 2016 APEC Ministerial Meeting.

Third, the successful implementation and expansion of the East Asian trade agenda requires capacity-building for developing countries. Overcoming this big constraint on progress towards structural adjustment and cooperative arrangements in East Asia requires information sharing. Korea's experience as an early adopter of an outward-oriented growth strategy makes it an ideal candidate to share experiences with developing countries. Korea could make tailored policy suggestions in human resource development and other initiatives likely to make a positive contribution to economic integration. This would ensure growing confidence in strengthening collaboration with ASEAN and China-Japan-Korea with a view to sharing the benefits of economic integration among participants and then moving forward to achieve global free trade. In practice, such an outward-oriented policy forces the market to minimize the negative impact of trade diversion and make the regional market more competitive and inclusive.

Fourth, for the East Asian trade agenda to reach critical mass to move forward, the cooperation mechanisms in the region should have the following conditions: 1) the capacity to respond to the challenges and changes facing the region; 2) inclusiveness of interests and agendas; 3) the capacity for harmonizing the roles of other groups in the region; and 4) pursuit of multilateralism and consistency with the WTO. Any individual country

or any single regional cooperation mechanism cannot function perfectly in isolation. For example, although some believe APEC is capable of fulfilling the above conditions, APEC alone cannot serve the interests of all participants in its agenda. This forum should be used to build consensus on global issues (not necessarily limited to regional or local ones) via brainstorming sessions under a non-binding principle. If APEC economies encourage each other to design and implement progressively better policies for economic management and structural adjustment, they could help the G20 to preserve preconditions for sustained improvement in living standards. Many issues, such as rebalancing economic growth, averting disastrous climate change, preserving an open international economic regime, fighting corruption, and making the new wave of technological breakthroughs as inclusive as possible, need global solutions.

Last, several conditions have been advanced to strengthen Korea's competitiveness, adjust its industrial structure to adapt to the 4th industrial revolution, gain greater access to global markets, share the fruits of economic integration, and reform for greater Asia-Pacific co-prosperity. These include revision to the KORUS FTA in March 2018 and the leaders of Korea, Japan, and China agreeing in principle to accelerate the CJK FTA negotiations. In addition, Korea should keep an eye on the progression of the CPTPP while reinforcing its FTA roadmap.

It is premature to assess the economic impact of recent developments concerning North Korean nuclear-related issues on the regional economy. However, if the North Korean nuclear threat is mitigated, then violence on the Korean Peninsula may finally come to an end. This may trigger new opportunities for Korea to play the role of linchpin for East Asia economic cooperation and enable it to become a much larger force in the world economy.

Endnotes

¹ This number indicates all physical RTAs in force, sorted by coverage (goods, services, goods and services). For more details, visit <http://rtais.wto.org/UI/publicsummarytable.aspx>

² East Asian countries refer to members of ASEAN and China, Hong Kong, Japan, South Korea, and Chinese Taipei.

³ With the exception of Asia-Pacific Trade Agreement (APTA) implemented in 1975, the majority of Northeast Asian countries' FTA/RTA negotiations were initiated and concluded in the 21st century, https://www.wto.org/english/tratop_e/region_e/rta_participation_map_e.htm.

⁴ Kim Sangkyom, Park Innwon, Park Soonchan, "Regional economic integration in the Asia Pacific Region: is an FTAAP the catalyst for one community?" KIEP, 2011.

⁵ Fred Bergsten, "A Free Trade Area of the Asia-Pacific in the Wake of the Faltering Doha Round: Trade Policy Alternatives for APEC," in *An APEC Trade Agenda? The Political Economy of a Free Trade Area of the Asia-Pacific*, eds. Charles E Morrison and Eduardo Pedrosa (Singapore: ISEAS, 2007).

⁶“Global Economic Prospects: Economic Outlook for East Asia and Pacific Region,” World Bank, 2018.

⁷Dominik Naehler, “An Empirical Estimation of Asia’s Untapped Regional Integration Potential Using Data Envelopment Analysis,” ADB Economic Working Paper Series, No. 445, August 2015.

⁸For further details of CRI construction and its interpretation see Ibid.

⁹On the number of active FTA partners, <http://www.fta.go.kr/main/situation/fta/main/>.

¹⁰Measured by the ratio of trade to GDP.

¹¹Park Innwon and Park Soonchan, “Economic Effects of an FTAAP: CGE Model Analysis,” Unpublished paper presented to APEC CTI for 2016 APEC Ministerial Meeting.

¹²Peter A. Petri and Michael G. Plummer “The Economic Effects of the Trans-Pacific Partnership: New Estimates” WP 16-2, Peterson Institute for International Economics, 2016.