

## Korea's Elections and the KORUS FTA

BY *Yoon-shik Park*

On April 11, South Korea's ruling Saenuri Party achieved a surprise victory in the National Assembly elections, winning a narrow two-seat majority. Barely a month ago, its main opposition—the Democratic United Party (DUP)—was widely expected to ride a wave of popular dissatisfaction with President Lee Myung-bak's administration to an overwhelming victory. The DUP's election strategy included a promise to unilaterally abandon or at least renegotiate the Korea-U.S. Free Trade Agreement (KORUS FTA) if the party regained the majority.

The National Assembly elections were especially hard fought because the victorious party will likely gain the upper hand in the upcoming and even more important presidential election later this year. The DUP opposition attempted to use the KORUS FTA to stoke latent anti-Americanism among the younger generation, which has only a distant memory of the critical role of the United States in helping Korea during and after the Korean War. In this way, the KORUS FTA became a major referendum issue in the parliamentary elections. The DUP's unexpected defeat means that the agreement will remain a major contributor to closer U.S.-Korea economic and trade relations in the coming years.

### THE MOST IMPORTANT U.S. TRADE AGREEMENT SINCE NAFTA

The KORUS FTA was at last ratified by both the U.S. Congress and the Korean Parliament in late 2011 and was finally implemented just over a month ago on March 15. Although at present the United States has FTAs in force with seventeen countries, KORUS

is the most important FTA for the United States since the North American Free Trade Agreement (NAFTA) entered into force in 1994. Korea is now the fifteenth-largest economy in the world, with GDP of over \$1 trillion, and the country is the United States' seventh-largest trading partner, fifth-largest export market for agricultural products, second-largest market for services in Asia, and tenth-largest market for IT products. The total U.S.-Korea trade volume nearly tripled between 1990 and 2010.

However, the relative importance of U.S.-Korea trade has been declining steadily since the early 2000s. Whereas in 2003 the United States was the world's leading exporter to Korea, today it is battling with Europe for third place, behind China and Japan. Until 2002, the United States was also the biggest market for Korean exports, but it fell behind China in 2003 and behind the European Union in 2005. The past record indicates that U.S. FTAs tend to increase bilateral two-way trading volume significantly. According to 2010 trade data, the United States' seventeen FTA partners account for over 40% of U.S. exports, while contributing 31% of U.S. imports. The KORUS FTA is thus expected to slow down or even reverse the steady decline in the traditionally strong U.S.-Korea trade relationship.

### POTENTIAL IMPACT ON THE TWO COUNTRIES

The United States boasts one of the world's most open economies, and this openness has been a key source of the country's economic strength. Korea, on the other hand, has maintained significant trade barriers over the years. For example, Korea's duties on imported agricultural products average 54%, compared with only 9% in the United States for the same products. On non-farm goods, Korean tariffs average 6.6%, compared with 3.2% in the United States. By eliminating these high tariffs, KORUS will significantly expand U.S. exports to Korea. Under the FTA, 95% of all bilateral goods trade will become

duty free over the next three years, and in ten years virtually all tariffs on goods will be eliminated.

Several studies have assessed the potential economic effects of the KORUS FTA. A 2007 study by the U.S. International Trade Commission (ITC) estimates that if the agreement is fully implemented, U.S. GDP would increase by \$10–\$12 billion (about 0.1%) and U.S. exports would rise by \$9.7–\$10.9 billion. A University of Michigan study commissioned by the Korea Economic Institute estimates that U.S. GDP would increase by \$25 billion (0.14% of GDP). (This estimate is larger than the U.S. ITC result in part because the study included the effects of liberalization in services trade.) Similarly, a study conducted by the Korea Institute for International Economic Policy projected that the KORUS FTA would lead to an increase of 0.42%–0.59% in Korean GDP according to a static analysis and 1.99%–2.27% according to a dynamic analysis. Finally, a 2009 study by the U.S. Chamber of Commerce found that the United States would suffer a net loss of more than 345,000 jobs, \$35 billion in export sales, and \$40 billion in GDP growth if the KORUS FTA is not implemented.

Early indications on the impact of KORUS are positive. Even though the FTA has only been in effect for one month, bilateral trade between the two countries has already seen a healthy increase. Over the past 30 days, Korean exports of auto and electrical parts to the United States registered growth of 12.4% compared to a year ago. Similarly, California wineries report a double-digit increase in their exports to Korea compared to last year, partly helped by the removal of a 15% Korean tariff on wine imports. U.S. firms have also shown greater interest in making direct investments in Korea in order to exploit the closer economic relationship between the two countries and use Korean investments as a potential bridgehead for penetrating the dynamic economies of East Asia.

## THE FUTURE ROLE OF KORUS IN U.S.-KOREA RELATIONS

The parliamentary election victory by the ruling Saenuri Party presages strengthened economic and security relations between South Korea and the United States in the coming years, to the mutual benefit of both countries.

- Because of the KORUS FTA and Korea-EU FTA, which came into force provisionally on July 1, 2011, Korean firms and U.S. firms with a Korean base of operations can now exploit both American and European markets with greater ease than their Asian competition.
- China and Japan are now much more eager to conclude FTAs with Korea. If Korea negotiates FTAs with both countries, Korean firms—as well as U.S. firms with a Korean base of operations—will have enhanced access to the dynamic East Asian markets.
- Closer economic and trade relations between Korea and the United States will promote an even tighter security relationship between the two traditional allies.
- Given the strategic and economic benefits of the KORUS FTA, policymakers in both South Korea and the United States would be well advised to not toy with replacing or renegotiating the agreement as both countries prepare for presidential elections later this year. ♦

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