

U.S.-Japan Free Trade? Lessons from the U.S.-Korea FTA

Wendy S. Cutler

Assistant U.S. Trade Representative for Japan, Korea and APEC Affairs
Office of the U.S. Trade Representative

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Introduction

Thank you to Takeda-san and to the Press Club for this opportunity to be with you today to talk about a topic that I know has received a lot of interest in Japan – the United States-Korea Free Trade Agreement – or KORUS FTA.

The FTA that the United States signed with Korea on June 30 has spurred a great deal of discussion about what impact it may have on Japan – in commercial, economic, political, and strategic terms – and whether it is a harbinger of a future United States-Japan FTA.

These certainly are valid questions – questions that can only be answered over time. What I hope to do today is to offer a useful

perspective on why the KORUS FTA was ultimately successful and then highlight the lessons I believe are relevant from this experience when thinking about prospects for a U.S.-Japan FTA.

Similar Factors, Different Paths

The question at the heart of this discussion is, given the economic similarities between Japan and Korea, why was Korea in a position to conclude an FTA with the United States, while an FTA between the United States and Japan remains elusive?

Both Japan and Korea have strong economic and trade relationships with the United States – around \$208 billion in two-way goods trade with Japan and \$78 billion with Korea. Both countries have heavily protected but small agriculture sectors in terms of their overall relative GDP – approximately 2% for Japan and 3% for Korea. The manufacturing sectors in both countries are export competitive, while their services sectors remain generally overregulated. Both have also benefited greatly

from export-oriented growth over the past half century, and so value the benefits that trade can provide. But both Japan and Korea also recognize that the economic model that they have followed over past decades is not a recipe for continued economic growth in light of the changes underway in the region and the world.

Yet these similarities have not translated into an equal level of readiness or interest in Japan for an FTA with the United States.

Rationale for the KORUS FTA

I think that this difference may be best explained by the fact that Korea realized that despite the challenges associated with entering into a high-quality, comprehensive free trade agreement with the United States, the KORUS FTA would play a critical role in Korea's efforts to open and reform its economy and thereby to achieve its long-term economic goals. Three main factors contributed to this realization.

First, Korea, having already witnessed the positive effects of the FTAs that it had concluded with a few smaller countries, realized just how much it had to gain economically from a larger, more commercially significant deal with the United States.

Second, Korea recognized how an FTA with the United States could assist in carrying out its own domestic economic reforms. Take the services sector, for example. Korea realized that the best way to ensure that it would develop a more competitive services sector was through increased competition and additional liberalization – and what better way to lock in market opening than through an FTA with the United States, which calls for significant opening in this area?

And, finally, Korea understood that if it was going to remain competitive in the global economy going forward, it couldn't let its agricultural sector hold it back. Korea knew that only through a combination of agricultural market opening and provision of assistance to farmers to adjust to this opening would it be able to leverage trade and

investment to remain a vibrant economic force in the years and decades to come.

The KORUS FTA was no case of *gaiatsu*. Korea made the decision on its own that an FTA with the United States made sense, not only because of the preferential access it would gain to the world's largest market, but also because it would support its own long-term economic objectives.

So, that explains why Korea was ready to enter into negotiations with the United States. But, an FTA can't happen if only one side is interested – both partners have to reach the same conclusion.

The United States came to this decision through its own calculations about the potential benefits of a KORUS FTA. First, Korea was a natural fit given its large and dynamic economy. While the United States has concluded FTAs with 16 trading partners since 2001, before Korea few of these FTAs had been with large trading partners –

something for which the Administration has been criticized.

Second, an FTA with Korea was viewed as critical to demonstrating the United States' strong and clear commitment to continual deepening of our economic and trade relationships with key partners in the Asia-Pacific region.

Finally, and importantly, Korea, like Japan, is a strong ally of the United States that shares our values of democracy and freedom.

Lessons from KORUS

For these reasons, both the United States and Korea agreed to embark on FTA negotiations – but much more was needed for the negotiations to come to a successful conclusion.

The United States and Korea were able to bring home a strong, balanced agreement due to several key factors. I believe these factors

can provide useful insights for others that may be considering entering into negotiations with the United States – including Japan.

First, both sides enjoyed strong and sustained political commitments to a positive outcome at the highest levels, which enabled their negotiators to take risks. Without a clear recognition of our top leaders of just how much was at stake in these negotiations, I firmly believe our efforts would have failed.

Second, Korea knew from the beginning that it would have to address its non-tariff barriers if the FTA had any hope of success. This recognition meant that we were able to work together to tackle barriers in a way that made sense for both countries. The final Agreement, I am happy to report, contains provisions that address non-tariff barriers across a wide-range of sectors, notably in the areas of autos, pharmaceuticals, financial services, and telecommunications. In addition, the deal provides commitments related to transparency and regulatory due process that are more far-reaching than in any previous U.S. FTA.

And, third, both the United States and Korea brought the right mindset to the table. Gone were the days when the United States and Korea faced each other as trade policy adversaries. Both parties set aside the “trade friction” mentality of the past and approached the negotiations as partners with the goal of concluding a win-win agreement.

In the end, we concluded a strong, balanced agreement that has gained the attention of our trading partners throughout the world. We are now both working hard to attain approval of the deal by our respective legislatures.

Next Steps: The U.S.-Japan Economic Relationship

In looking at the factors that contributed to the success of the KORUS FTA, it is only natural to examine whether these same elements exist in Japan.

I have heard some interest here in Tokyo over the past couple of days for a U.S.-Japan FTA, and I sense that some momentum is building towards that goal. But, I'm also hearing a frank recognition among my Japanese friends that the time is not ripe and more work needs to be done in Japan to create the conditions necessary for a bilateral FTA down the road.

Clearly, an FTA negotiation between the United States and Japan would be the most ambitious undertaking in the history of our long economic relationship. Expectations for what an FTA negotiation could accomplish would be high – we are the world's two largest economies with a complex economic relationship and a vast range of interested stakeholders. FTA talks would also put our trade and economic relationship under great scrutiny. And, as the world's two largest economies, we would need to conclude an FTA of the highest quality – for us, as well as to set an example for others.

That said, the FTA idea in my mind is a constructive way to keep

focus on the potential gains from a further deepening of our own economic relationship. The work that the private sector, including Keidanren and others, is doing in both our countries to advance the FTA concept is thus quite important, and I hope more will be done to better define the tangible benefits that an FTA between our two countries could bring.

An FTA, of course, is not the only way to deepen our economic relationship. Irrespective of whether or when the conditions are ripe for launching FTA negotiations, we will continue to strengthen our engagement with Japan, wherever possible. Our work in the Regulatory Reform Initiative, for example, is truly cutting-edge and continues to focus on finding mutually beneficial solutions that help create new growth and opportunities. The United States and Japan also remain engaged on resolving outstanding issues – such as beef, where we continue to urge Japan to normalize beef trade in a manner based on internationally recognized science and standards.

Conclusion

In conclusion, I see the KORUS FTA as offering insights into a path forward for Japan – particularly for those who are giving serious thought to how to anchor Japan’s economic future. I also sense the Korea-EU negotiations are also being closely watched in Japan.

The question is when – or some say whether – Japan will be ready to move forward with the same kind of bold steps that led Korea to embark on FTA negotiations with the United States.

These are major, important questions for Japan to face. I’ve identified some key parameters that I see as key to make this kind of next step possible. But what’s critical is that it will be up to Japan on its own to decide whether it is prepared for the next step. That's the only way an FTA can succeed.

Thank you.