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South Korea and China's Power Plays Through Free Trade Agreements with ASEAN

by Yesel Lee

I. INTRODUCTION

Historically, Korea has fought to maintain its identity and international position while sandwiched between two countries, China and Japan, each with their own agendas. With the division of the peninsula, a war-devastated Republic of Korea (hereafter, South Korea) has transformed through export-oriented growth from a developing country to an OECD member, a title it gained in 1996. As South Korea continuously seeks to expand its regional economic influence, China is rapidly increasing its global economic weight, threatening to relegate South Korea's influence. During the Roh Moo-hyun administration, South Korea first combated this under its Northeast Asia Economic Hub (NAEH) policy framework, which confirmed Korea's intentions not to let a powerful China sideline it again. Under the Lee Myung-bak administration, the NAEH strategy shifted to highlighting the importance of trilateral cooperation with China and Japan and used free trade agreements (FTAs) as one of the primary tools in cementing these ties.

This paper examines how South Korea seeks to prevent being a secondary player in the greater Asian region. Specifically, it considers how Korea expands its influence on individual members of the Association of Southeast Asian Nations (ASEAN) and within the association as a whole. How China responded to Korean actions with ASEAN since the Asian Financial Crisis, and vice versa, helps determine how China and Korea seek to establish influence among ASEAN members. More specifically, this paper analyzes the trade agreements that Korea and China seek to establish with ASEAN, the agreements' scope, and the players involved in the proposal of the agreements. Although there are some objections about how vulnerable an FTA can make a nation, this paper does not assess these agreements' merits; instead, this paper uses the context and content of FTAs to analyze how China and Korea attempt to gain influence with ASEAN.

First, this paper assesses the impact of the Asian Financial Crisis. Then, China, Korea, and ASEAN's comparative advantages will be analyzed to determine how each would benefit from an FTA. Next, the sequencing and scope of South Korea and China's agreements are examined to determine their motives for Asian economic cooperation. After evaluating how domestic politics and public opinion can influence these trade negotiations, the paper concludes with policy recommendations for Korea, China, and ASEAN.

II. IMPACT OF THE 1997-1998 ASIAN FINANCIAL CRISIS

The Asian Financial Crisis of 1997-1998 had a significant impact on South Korea, China, and ASEAN countries. The crisis halted growth and integration trends, and its aftermath resulted in large policy shifts to temper long-term effects and prevent potential future crises. These post-crisis changes warrant a brief overview of trade patterns and agreements prior to the crisis in order to better assess the differences in South Korea and China's approach to trade agreements over the past decade. Note that, in ASEAN's case, analyzing trade composition and policy reforms of the individual countries goes beyond the scope of this paper; thus, this analysis will be applied to ASEAN as a whole.

South Korea

According to the IMF, from 1990, Korea's exports to ASEAN increased until a dramatic drop in 1997 when total trade growth to the region fell to 1.47 percent and became negative in 1998 at -25.43 percent. Most South Korean exports to ASEAN consisted of manufactured goods, including both light industry, such as textiles, and heavy industry, such as chemicals and electronics. Raw materials and agriculture were less than 10 percent of all exports to ASEAN, perhaps expected given ASEAN's abundant natural resources.

During this period, South Korea's economy experienced significant upheaval. In the 1990s, Gross Domestic Product (GDP) growth for South Korea was between 5 and 10 percent, dropping to a recession of -5.71 percent in 1998. Due to this recession, South Korea implemented significant economic reforms to prevent a future crisis, mainly by strengthening its economy's legal and regulatory framework and by resuscitating the financial industry, as outlined in a paper by the International Monetary Fund and the Singapore government.

Since the Asian Financial Crisis, Korea's economy rebounded, its GDP and trade grew again, the only exception being -16.82 percent negative trade growth in 2009 owing to large recessions in the United States and the European Union. Having demonstrated tremendous growth pre-crisis and stability since, South Korea has embarked on an economic growth strategy of ensuring future markets and resource access. Furthermore, it went against its tradition of regional economic indifference and embarked on a series of multilateral and bilateral trading agreements. In a 2003 *East Asia* journal article, Hyun Seog Yu argues this was not only to combat the worst of the crisis, but also to come to terms with an economic reality that is no longer as U.S.-centered.

This interest in establishing regional economic ties culminated in the NEAH strategy. On February 25, 2003, President Roh Moo-hyun announced in his

inaugural address that he wanted to develop South Korea as “an economic hub of Northeast Asia.” This strategy has three main goals: (1) establishing inter-Korean economic ties; (2) instituting an integrated Northeast Asian economic system; and (3) developing infrastructure for Korea to be a business hub. However, the NAEH strategy under the Roh administration raised eyebrows in China, whose cooperation is vital to the strategy’s success. Since South Korea has made it clear it is positioning itself to be an economic hub for Asian economic cooperation, China’s reaction will influence the nature of this cooperation and the roles each country will play. Analyzing how South Korea makes its presence felt in Asian regional cooperation should help determine if it seeks new markets for trade or strategic considerations, such as countering China’s growing influence.

China

Like South Korea, China’s trade with ASEAN grew steadily until the Asian Financial Crisis. However, China was slightly more insulated than Korea during the crisis and according to IMF statistics, China experienced trade growth of 18.27 percent in 1997 and -5.55 percent in 1998. As indicative of China’s rapid growth during this period, China’s composition of exports to ASEAN transitioned from traditionally labor-intensive sectors to more advanced sectors, such as electronics and heavy machinery.

Unlike South Korea, China never entered a recession as a result of the Asian Financial Crisis and has grown at least 7 percent since 1991. This was in large part due to China’s proactive policy and reform implementation to counteract and insulate the Chinese economy. Since China’s large population and nominal GDP give it considerable economic influence, it is considered a natural potential leader in the Asian, if not global, economy. China’s economic growth should continue, albeit at a slower pace than in recent years, and its large market make it an attractive trade partner to neighboring countries.

ASEAN

The Asian Financial Crisis started in Thailand, an ASEAN member country, and impacted trade within the association more than trade between the association and China. Like South Korea and China, trade within ASEAN increased in the early 1990s. However, according to the IMF, the trade growth rate fell from 24.46 percent in 1995 to 5.62 percent in 1996, reaching a low of -18.06 in 1998. This pattern indicates the Asian Financial Crisis hit these countries first, with the effects spreading to other countries like South Korea through 1998.

As Nongnuch Tantisantiwong writes in a 2010 *ASEAN Economic Bulletin* article, it is important to note that the countries that were most open to trade

experienced the sharpest economic downturns after the Asian Financial Crisis. These reasons will make it more difficult for the association as a whole to reach a consensus on trade liberalization as countries hit hardest by the crisis may be hesitant to enter into multilateral and bilateral trade agreements. Thus, any ASEAN member country's decision to engage in free trade ties with China or South Korea reflects the positive level of trust the member country has in the two Northeast Asian countries' economic influence. Since both South Korea and China have FTAs with ASEAN, it is clear that all ASEAN countries saw more economic benefit than harm in free trade with these countries. The creation and implementation of the FTAs with South Korea and China will be used to examine how these two Northeast Asian countries are using their strong economic positions to exercise their influence in Asia vis-à-vis ASEAN.

III. COMPARATIVE ADVANTAGE AND FACTOR ENDOWMENTS

When analyzing any FTA, it may be inferred that whichever party had greater influence in the negotiations received the most benefit. In determining China and South Korea's possible positioning efforts, the analysis should also weigh ASEAN's comparative advantages. FTAs that allow China and Korea more access to beneficial resources or markets indicate which of these two countries had more influence when negotiating these agreements. Conversely, if a party of greater influence accepts marginally beneficial trade agreements, it may imply that trade liberalization was not that party's primary goal; rather, it sought to position itself as an economic leader in Asia.

For the past decade, South Korea has shifted from export-oriented economic development to establishing itself as a potential hub for Asian economic cooperation. Until the early 1990s, as South Korea was industrializing, it had a comparative advantage in capital-intensive sectors even though there was a surplus of labor. This has translated to a comparative advantage in electronics, heavy machinery, and other technological goods vis-à-vis China. However, China's rapid growth has enabled it to surpass the comparative advantage that South Korea had in what the OECD classifies as low-technology sectors. Meanwhile, China has lost its comparative advantage in labor-intensive industries vis-à-vis ASEAN. Nevertheless, Jung Taik Hyun and Jin Young Hong have determined in their 2011 study, "Comparison of Comparative Advantage of Korea and China by Technology Level," that South Korea has maintained a comparative advantage in high- and medium-high technology products over China.

Conversely, in a 1993 *ASEAN Economic Bulletin* article, Dean DeRosa finds that ASEAN as a whole continues to have a comparative advantage in labor-intensive industries and in natural resources, stemming from its large tropical

land area. Due to this reason, it is in ASEAN's best interest to expand trade with industrialized countries that have significantly different factor endowments. Thus, South Korea's trade agreements with ASEAN would be mutually beneficial if an agreement allowed Korea freer access to labor-intensive goods and ASEAN access to manufactured or capital-intensive goods. As South Korea still maintains a comparative advantage in high-technology products over China, it would also be mutually beneficial for Korea and ASEAN to allow free trade of these products. Similarly, as China no longer has a comparative advantage in labor-intensive sectors, especially compared to ASEAN, it is mutually beneficial for China and ASEAN to allow freer trade of low- and medium-high technology products and labor-intensive products.

IV. SOUTH KOREA AND CHINA FREE TRADE AGREEMENTS

As Table 1 shows, six of South Korea's thirty-one FTAs, either proposed or implemented, involve only ASEAN countries. Although South Korea and China have additional FTAs involving ASEAN countries, these other multilateral FTAs are not exclusive to ASEAN, and for the purposes of this paper, I will analyze the interactions between South Korea and China and ASEAN, as individual members and as a whole. As shown in Table 2, of China's twenty-six FTAs either proposed or implemented, three involve only ASEAN countries.

Table 1. South Korea-ASEAN Free Trade Agreements

	Proposed by:	Date proposed:	Date signed:	Date in effect:
ASEAN-Korea Comprehensive Economic Cooperation Agreement (AKFTA)	South Korea	October 2003	August 2006	June 2007
Korea-Indonesia FTA	South Korea	May 2011	July 2012 (negotiations)	
Korea-Singapore FTA	South Korea	October 2003	August 2005	March 2006
Korea-Thailand FTA	South Korea/ Thailand	October 2003		
Korea-Vietnam FTA	South Korea	June 2010	August 2012 (negotiations)	
Malaysia-Korea FTA	South Korea	May 2011		

Table 2. China-ASEAN Free Trade Agreements

	Proposed by:	Date proposed:	Date signed:	Date in effect:
ASEAN-People's Republic of China Comprehensive Economic Cooperation Agreement (ACFTA)	China	November 2001	November 2002	July 2005
People's Republic of China-Singapore FTA	Singapore	August 2006	October 2008	January 2009
People's Republic of China-Thailand FTA	Thailand		June 2003	October 2003

China has only initiated one FTA in Southeast Asia, the ASEAN-China Free Trade Agreement (ACFTA) in 2005, which Korea followed two years later with its own proposal of a free trade area with ASEAN countries. Meanwhile, South Korea initiated all six of its FTAs, highlighting the active steps it has taken in building economic interdependence with Southeast Asia. Furthermore, South Korea has pursued bilateral agreements with individual ASEAN countries, demonstrating initiative to gain early influence and possible first-mover advantage vis-à-vis China in those countries. Given the number of FTAs Korea has pursued since ratification of ASEAN-Korea Free Trade Agreement (AKFTA) in 2007, it is clear that South Korea seeks to establish itself in Asia, the region former president Lee Myung-bak characterized as Korea's "economic territory," in his 2011 speech. Combined with President Roh's NEAH strategy, it is clear South Korea intends to play a prominent role in Asia's economic development and emergence.

Since China has shown no inclination to pursue additional FTAs with ASEAN, one might infer they are not concerned with South Korea's efforts in the region. In contrast, Korea proposed all of its FTAs after China proposed the ACFTA. It is debatable how much this decision was influenced by the free trade potential of ASEAN and ASEAN member countries versus the fear of falling behind China in regional influence and advantage. With the exception of the People's Republic of China-Thailand FTA—since this is limited to reducing tariffs on agricultural goods—both China and South Korea's ratified trade agreements are with the same trading partners. Singapore's decision to pursue a trade agreement with China after it already had one through the ACFTA, and South Korea's decision to pursue an FTA with Singapore suggests potential trade partners in ASEAN consider China to have higher promise compared with South Korea.

V. SCOPE OF FREE TRADE AGREEMENTS

Analyzing the agreements already in force should demonstrate whether these FTAs are regional maneuvers for influence or motivated by genuine trade interests. For South Korea, the applicable agreements are the AKFTA and Korea-Singapore FTA. For China, these would be the ACFTA, People's Republic of China-Singapore FTA, and People's Republic of China-Thailand FTA, but as the latter only applies to agricultural goods, this agreement will not be analyzed.

South Korea

South Korea's largest ASEAN agreement, AKFTA, consists of an agreement with all ASEAN members, and the tariff reduction schedule generally mirrors the ACFTA. During negotiations, Thailand initially deferred from signing because of a disagreement over agricultural provisions, believing that these especially, but also the agreement as a whole, would not benefit its economy. However, Thailand signed on in February 2009 only after it negotiated with Korea for an extension on tariff reductions for certain products and tax reductions on goods such as cosmetics, steel, and leather.

As will become apparent in the next section, Thailand's behavior and successes during negotiations indicate the relatively lower stature vis-à-vis China that Korea had with Thailand, if not all of ASEAN. Provisions on tax and tariff reduction, which were sufficient for the other members of the ASEAN 6, were too few for Thailand, which negotiated a separate tariff reduction schedule. In light of South Korea's comparative advantage in high-technology and Thailand's advantage in agriculture, the two economies are complementary and both would benefit from freer trade. However, Thailand's late entrance and the concessions Korea gave indicate that Korea had a greater desire to enter into a comprehensive trade agreement than the ASEAN countries themselves, especially Thailand.

In terms of provisions accounting for dispute settlements and intellectual property (IP), South Korea's most comprehensive FTA is with Singapore, which places great importance on potential markets and benefits from trade integration through this agreement. Korea's FTA with Singapore is the only one out of the four analyzed here that has IP provisions. In recent years, China has aggressively sought to acquire high-technology knowledge from other countries, to the point of not enforcing piracy laws. However, Singapore and South Korea's decision to include provisions for encouraging high-technology research between the two countries demonstrates an attitude of cooperation instead of competitiveness, which embodies these FTAs' original intent. In the context of South Korea's comparative advantage over China in high-technology products, Korea and Singapore's cooperation may indicate Korea's desire to maintain a lead in these

industries. Singapore's comparative advantage in both labor-intensive industries and natural resources manifests in the tariff reduction schedule which further points to economic cooperation that maximizes benefits for each country. Singapore and Korea also demonstrated their cooperation by liberalizing standards for government procurement, the only agreement out of the four that includes any such provisions.

China

China proposed its FTA with ASEAN two years after its 2001 WTO accession and early in its economic liberalization. Like the AKFTA, the ACFTA has tariff reductions on two schedules, one for the ASEAN 6 and one for the remaining four nations. Unsurprisingly, the ACFTA focuses on the benefits ASEAN gains in accessing China's vast markets. Accordingly, other provisions in the ACFTA are not elucidated, left to be negotiated at later dates. For example, the Trade in Services Agreement of the ACFTA says that all countries will enter into negotiations and commit to liberalization in the trade of services. (An Agreement on Trade in Services was signed in January 2007.) Similar to South Korea, China holds a comparative advantage in low- to high-technology sectors over ASEAN, making free trade between the two mutually beneficial.

Less than a year after the first provisions of the ACFTA came into effect, Singapore proposed a bilateral agreement with China. China's bilateral agreement with Singapore goes beyond China's agreement with ASEAN and accelerates the tariff reductions outlined in the ACFTA. China and Singapore's complementary economies, in terms of their respective comparative advantages, significantly benefit from the tariff reduction schedule and freer trade. Singapore's proposal of a bilateral agreement and its emphasis on an accelerated tariff reduction timeline indicate the country's desire to increase trade in China's huge market. Provisions of the ACFTA that were not comprehensive or were lacking are detailed in the China-Singapore agreement. For example, the investments provision, which points to the provisions of the ACFTA Investment Agreement, details more commitments for the two countries in terms of what actions each is prohibited from taking in service sectors. It is interesting to note that the China-Singapore agreement does not have any provisions for IP, as the Korea-Singapore agreement does. This may be a result of China's increasing aggressiveness in seeking to acquire technology secrets, often to its trading partners' dismay. It also indicates the larger technological gap between China and Singapore than between South Korea and Singapore. Since South Korea and Singapore have closer technological capabilities, IP provisions are more likely to encourage the free flow of ideas and research. On the other hand, allowing its research and development to be freely shared with China, a country with significantly greater manufacturing capabilities and global market reach, puts Singapore at risk of losing intellectual property.

VI. DOMESTIC POLITICS AND INTERNATIONAL ECONOMIC COOPERATION

South Korea has expanded its zone of economic cooperation through FTAs; however, domestic public opinion has not always agreed with government intentions. The best example is perhaps the Korea-United States Free Trade Agreement (KORUS), which resulted in protests by the opposition party campaigning to renegotiate the agreement. Domestic politics and public opinion can stand in the way of mutual economic benefits. Although there is no commensurate or even visible reaction to the FTAs with ASEAN or individual ASEAN members, public opinion in China and South Korea could affect future cooperation or competition between themselves and the extension of their regional economic influence.

China and South Korea are much more likely to build stronger economies by creating agreements their citizens are more likely to support, for instance with regional powers like each other. Their economies are already highly integrated, and their geographic proximity suggests increasingly strong economic ties. However, their political history and China's relationship with North Korea may impede economic growth.

As China's economic influence grows, how South Koreans will react to China's maneuvers largely depends on current issues. Overall, the populations in both countries view each other the same way—economically positive, but sensitive to cultural and historical issues. In his article “Disillusionment and Dismay: How Chinese Netizens Think and Feel About the Two Koreas,” Peter Gries states that Koreans view China as an economic partner and hope to grow alongside China. Furthermore, Chung Jae-ho finds that Koreans see China as a global heavyweight that can be leveraged against Japan and other global powers. However, South Korean views change when China's actions concern Korean security, such as incidents related to North Korea, or relate to historical national identity, such as controversies involving Goguryeo or the dragon boat festival. Similarly, while Chinese generally view South Korea positively as an economic partner, their opinions change drastically when it comes to thorny historical or national identity issues involving Korea.

Public opinion in South Korea regarding former president Lee's policies was that Korea could gain more by cooperating with China than by competing against it. Accordingly, President Lee assuaged Chinese and Japanese concerns and furthered Roh's NEAH strategy with a tone of cooperation, encouraging China and Japan to invest in Korea. By aligning itself as the hub, this policy ensures that Korea is in a cooperative position for both China and the United States. Given Korean views of China as an economic partner, promoting cooperation

with both China and the United States prevents public opinion from interfering with free trade benefits. The Lee administration has made it clear that it actively pursued FTAs as a strategy for economic growth, and Lee highlighted the fact that Korea is now in FTAs with 45 countries and 61 percent of the world market. Seeing China as an economic ally, Korea's pursuit of FTAs intends to capitalize on their economic benefits, not to challenge or compete with China. How the Park Geun-hye administration will continue with these economic and trade strategies remains to be seen.

VII. POLICY RECOMMENDATIONS

As South Korea cannot compete with China in size and economic strength, its role in the Asian economy must be oriented toward its comparative advantages. As China shows signs that its economic growth rate will be declining, it will continue to grow in size and influence. As it closes in on the comparative advantage that South Korea has in high-technology products, Korea's interest will be to expand trade in these industries as much as possible and establish itself as a leader in these products. Since one of the results of free trade is growing interdependence, Korea can utilize the current lead it has over China in high-technology products to expand its access to these markets, while also providing a market for ASEAN's labor-intensive and low-technology goods.

Since China is already the second-largest economy in the world and is likely to continue growing, it will remain an attractive trading partner. China knows this. It does not need to actively seek trading partners, and it has increased clout when negotiating FTAs.

For South Korea, this means that it must find a place in the Asian economy other than a leadership role. Its current comparative advantage in high-technology is likely to be matched by China, which implies that South Korea must establish its clout in the region beyond free trade. One way it can do this is to pursue the NAEH strategy, but how feasible this is, given China and Japan's initial resistance, is questionable. One way to overcome this would be to highlight how economic cooperation could be more beneficial than economic competition. If South Korea were to shift its focus from the United States toward Asia, the increased trade could bring more growth to the entire region. Demonstrating how this would be beneficial for the Asian economic bloc, especially to China and Japan, would give South Korea a chance to gain the political and economic support it needs to fully pursue such a program.

China's WTO accession has significant implications for its economic policies. For the first nine years after its accession, China demonstrated wholehearted economic liberalization efforts following WTO guidelines. However, since 2010,

China's assertive actions in acquiring high-technology and use of influence to skew trade and investment to its advantage could lead to a decrease in its attractiveness as a trading partner. For China to maintain good will in the global market, it must demonstrate its willingness to acknowledge and address the concerns of its current and potential trading partners.

It would also be in ASEAN's interest to expand and diversify its economic interdependence as it continues to develop. If ASEAN focused solely on China, it would be very susceptible to changes in the Chinese economy; integrating their economies with multiple countries would allow the ASEAN countries to maintain their independence and possibly develop a significant role in the region despite China's shadow. As an independent bloc, ASEAN's diversity in membership and development levels can contribute to the group's total growth. It would be interesting to analyze individual countries' comparative advantages and how they complement each other as part of the ASEAN free trade area. Not only would it provide evidence of how each country contributes to the development of ASEAN as a whole, it could also shed light on how individual comparative advantage could be used in developing similar agreements worldwide. As ASEAN plays a more significant role in the Asian and world economy, the diverse economic ties it forms now in the region will give it an advantage and can contribute to its economic development.

VIII. CONCLUSION

South Korea's rebound and economic growth since the Asian Financial Crisis prove that it can play a major role in Asia's economy. As China's economy continues to grow, South Korea does not intend to play a secondary role in the Asian economy. Implicitly it has done this through its proposal of an FTA with ASEAN and subsequent proposals of trade agreements with Singapore, Malaysia, Vietnam, Indonesia, and Thailand. Explicitly, the announcement of the NAEH strategy gives a definitive outline to Korea's hopes for its future role in expanding Asian economic cooperation. By integrating with the ASEAN economy, Korea is showing a concerted effort to improve trade relations and encourage economic interdependence. Since China has shown no response or reaction, Korea appears to be pursuing these policies not necessarily to counteract China's influence or to compete with China, but to expand its regional economic cooperation.

China's size and influence in the Asian economy make it an attractive trading partner for other Asian countries. This means it does not have to assert its leadership role in Asia. Since China is a natural leader in Asia, it has focused on how it can become a leader in the world economy, a goal it has pursued by seeking to expand its competitiveness in high-technology industries. However, its size gives China the luxury of not having to concern itself with economic

positioning and active integration as Korea has. Although President Lee's comment about "economic territory" demonstrates South Korea's desire for economic authority in the region, it will not be able to expand its influence if it alienates or raises suspicions in those that can be its closest trading partners. If South Korea wants to establish a role for itself outside of China's shadow, the most feasible way would be to prove that economic cooperation would benefit its natural regional partners, China and Japan.



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