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CANADA-KOREA FREE TRADE: A WATERSHED IN ECONOMIC INTEGRATION WITH ASIA*

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If there is one thing to question about the recently signed free-trade deal between Canada and South Korea, it is this: What took us so long? South Korea is a long-time trading partner with Canada, with a democratic political system and a rapidly expanding free-market economy offering strong protections for commercial rights. The country is an excellent place for Canada to begin a deeper economic integration with the larger Asian market.

The details of the deal itself are certainly worth celebrating. Certainly Canadian consumers will save money on Korean-made products, such as cars. But Canadian companies exporting to South Korea have also, in recent years, found themselves increasingly unable to compete with exporters from the E.U. and U.S., who have already established free-trade deals with Seoul. Since the Americans signed their deal, U.S. exports to South Korea have soared, while the value of Canada's exports to the same market have dropped by 30 per cent, as Canadians were left facing tariffs as high as 269 per cent.

The Canada-Korea Free Trade Agreement levels that playing field for Canada, something that will especially benefit firms exporting agricultural products (tariffs on Canadian beef, for example, were a punitive 72 per cent) and professional services. Even automakers may find that whatever increased competition comes from cheaper Korean car imports are offset by the opportunity to more easily sell Canadian-made vehicles in the much-larger Asian marketplace. There is a wealth of economic opportunity waiting in that burgeoning market; this free-trade deal is a pivotal first step for Canada to start fully capitalizing on it.

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ACCORD DE LIBRE-ÉCHANGE CANADA-CORÉE : UN TOURNANT POUR L'INTÉGRATION ÉCONOMIQUE AVEC L'ASIE*

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RÉSUMÉ

S'il y a une question à poser sur l'accord de libre-échange récemment signé entre le Canada et la Corée du Sud, c'est celle-ci : pourquoi avoir tant tardé? La Corée du Sud est un partenaire commercial de longue date du Canada et son système politique démocratique et son économie de libre marché en pleine expansion offrent de fortes protections pour les droits commerciaux. C'est un excellent endroit pour accroître la pénétration du vaste marché asiatique par le Canada.

Les détails de l'accord proprement dit sont certes cause de réjouissance. Les consommateurs canadiens économiseront sur des produits fabriqués en Corée, comme les voitures. Quant aux entreprises canadiennes qui exportent vers la Corée du Sud, elles ont, au cours des dernières années, éprouvé de plus en plus de difficultés à concurrencer les exportateurs de l'Union européenne et des États-Unis, qui ont déjà établi des accords de libre-échange avec Séoul. Depuis que les Américains ont signé leur accord, les exportations américaines vers la Corée du Sud ont grimpé en flèche, tandis que la valeur des exportations canadiennes vers le même marché a chuté de 30 % (les Canadiens devant payer des droits de douane sur leurs produits dont les taux pouvaient atteindre 269 %).

L'Accord de libre-échange Canada-Corée place dorénavant le Canada sur un pied d'égalité, ce qui sera particulièrement avantageux pour les entreprises qui exportent des services professionnels et des produits agricoles (le taux des droits de douane sur le bœuf canadien étaient de 72 %, entre autres). Même les constructeurs d'automobiles canadiens seront dédommagés pour la concurrence accrue — provenant des importations de voitures coréennes moins chères — par la possibilité de vendre plus facilement leurs véhicules dans l'énorme marché asiatique. Un marché en plein essor qui regorge de débouchés économiques dont le Canada pourra tirer pleinement profit grâce à l'accord de libre-échange.

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This past week in Seoul, South Korea, the Canadian and South Korean governments announced the successful conclusion of the Canada-Korea Free Trade Agreement (CKFTA). This is a historic deal for Canada and one that will see the eventual elimination of 98.2 per cent of South Korean tariffs on Canadian goods, which currently average a rate of about 13.3 per cent, and the elimination of 97.8 per cent of Canadian duties, with an average rate of 4.3 per cent. Not only is this a historic agreement, but it was absolutely critical for Canada to make significant progress in advancing trade with the growing Asian market. This agreement is an important first step in that process.

Although Canada's current trade and investment flows with South Korea are relatively small, this historic agreement should be celebrated as an important success in Canadian foreign affairs for four key reasons: 1) South Korea is a sizable and rapidly growing economy in its own right; 2) Canada is catching up with the U.S. and E.U. in terms of access to this growing market; 3) this will position Canadian firms in the global value chain and provide an important gateway into the Asian region; and 4) this is Canada's first successful agreement with an Asian economy and may help pave the way for future successful negotiations with other countries in the region. It certainly sends the message to other Asian countries that Canada is serious about expanding commercial relations in the region.

Moreover, Canadians gain from free trade. Canadian consumers will see some reduction in prices, including automobiles. Producers in several industries, including agricultural goods, will benefit from greater access to South Korean markets.

The deal in context

The South Korean economy consists of just over 50 million people, with a GDP of over \$1 trillion, and ranks about 26th globally in terms of population and size. In terms of GDP, it ranks just behind France and Israel. The International Monetary Fund (IMF) projects that South Korea's GDP will soon surpass that of Japan. Korea has a burgeoning middle class with a high-growth, rapidly advancing market that offers strategic importance for Canada.

Canadian and South Korean trade and investment flows are relatively small, but the two countries are established trade and investment partners. According to the Department of Foreign Affairs, Trade and Development (DFATD), Canadian merchandise exports to South Korea were \$3.7 billion in 2012, and Canada's merchandise imports from South Korea were \$6.4 billion. In 2011, Canadian foreign direct investment (FDI) in South Korea was \$365 million, while South Korean FDI in Canada was more than \$6 billion. South Korea is about Canada's seventh-largest trading partner overall, and is Canada's third-largest Asian trading partner behind China and Japan. The deal is expected to boost Canada-Korean trade by 32 per cent.

This trade agreement has been almost 10 years in the making. The two countries announced that they would explore an agreement on Nov. 19, 2004. Bilateral negotiations commenced on July 15, 2005. Negotiations were delayed by a trade dispute over beef in 2008, after South Korea banned Canadian beef imports following a discovery of mad cow disease in Canada. Importantly, talks were also delayed by concerns raised by the Canadian auto sector. The beef ban was lifted in 2012 and negotiations commenced again in November 2013. During this time, South Korea made significant progress in forging ahead with regional trade agreements with other large western partners. It has signed important bilateral agreements with the United States, the European Union, Australia, the Association of South East Asian Nations, and others.

Canada missed out on benefits from a trade agreement that were available to American and European firms that had already improved trading relations with South Korea. Since the implementation of the Korean-U.S. Free Trade Agreement (KORUS), U.S. and E.U. auto exports to South Korea more than doubled, albeit from a very small base (the U.S. only exported 24,000 cars, worth \$800 million, to South Korea in 2013). According to International Trade Minister, Ed Fast, Canada's exports to South Korea have dropped by \$1.5 billion, or about 30 per cent, since the Americans signed a free-trade pact with Seoul. Canada's share of Korean fresh, chilled and frozen pork imports dropped from 14.2 per cent in 2010 (i.e., before the implementation of the U.S. and E.U. deals with Korea) to 8.9 per cent in 2013, representing a loss in export value of \$22 million. During the same period, U.S. and E.U. market share increased by 10.2 per cent to reach 76.3 per cent.

The Canada-Korea Free Trade Agreement (CKFTA) will secure Canada's position in the South Korean economy and eliminate the tariff difference between Canadian producers and those from the United States and Canada. Below, I shall take a closer look at the sectors that will be most affected by the agreement.

The gainers and losers

Canadian consumers will benefit with access to duty-free goods from South Korea. As mentioned, Canada has an average tariff of just over 13 per cent on goods coming from South Korea, with much higher tariffs on some products. Most of these tariffs will be reduced immediately and some will be phased out over three, five or 10 years. Canadian consumers will benefit with more access to lower-cost consumer products.

Canadian firms also stand to benefit from the agreement. The benefit for firms comes from improved market access to the South Korean economy, which will allow Canada's agriculture and service sectors to compete with those from countries such as the United States and the European Union that already have free-trade agreements with Korea.

The Canadian auto sector and the Ontario government have been vocally opposed to the agreement. The auto sector argues it stands to lose jobs in the sector and that the deal will not deliver market access to Canadian automakers because the South Koreans are notorious for protecting their manufacturing sector with non-tariff barriers, even if tariffs are eliminated. However, the Canadian government has negotiated provisions in the agreement to help the auto sector adjust.

Although the auto sector was asking for a seven-year phase-in of the tariff reductions, the agreement provides only a three-year phase-in period. However, the CKFTA does include important provisions that will help the auto and other sectors adjust. The agreement lowers tariffs and includes provisions addressing non-tariff barriers such as standards-related measures. It also includes a dispute-settlement procedure and provides safeguard provisions to protect against import surges. The safeguard provisions allow Canada to take action if faced with a surge in auto imports.

Another key and contentious issue in the agreement is the agri-food industry. In fact, a key motivation for Canada's signing was levelling the playing field with E.U. and U.S. suppliers in this important sector. Canadian agricultural exports to South Korea face exorbitant tariffs, which averaged 52.7 per cent in 2012. Beef and most processed beef products face a tariff of up to 72 per cent on exports to South Korea. Tariffs on unroasted barley malt are 269 per cent.

The CKFTA will eliminate tariffs on 86.8 per cent of agricultural goods. This was contentious in light of the trade dispute over beef, but Canadian pork and beef producers stand to gain considerably from this agreement. Until now, they have been competing with E.U. and U.S. producers that do not face the same tariffs getting their product to the Korean market. Alberta and other western provinces stand to gain significantly from access to the Korean market. South Korea ranks fifth among Alberta's most important export destinations.

Canada also stands to gain significantly with access to the growing services sector in South Korea. Canada obtained significant improvements and new sectoral market access, which go well beyond South Korea's obligations under the WTO's General Agreement on Trade in Services (GATS). This includes Canada's export interests in professional services (e.g., foreign legal-consultancy services, commercial education and training, and research and development), environmental services, business services and services incidental to manufacturing, mining and wholesale trade. This outcome is commensurate with KORUS and the E.U.-Korea FTA.

Conclusion

A bilateral free-trade agreement (FTA) with South Korea should deliver significant commercial benefits across many sectors of the Canadian economy. In addition to generating benefits for Canadian consumers, an FTA with South Korea would better enable Canadian companies to tap into global value chains, take advantage of increased export opportunities, and employ South Korea as a strategic base for expanding their presence in Northeast Asia.

Although the auto sector in Canada is worried, this agreement could be a significant boost to that sector as well. Canadian automakers are concerned about competing with South Korea's Hyundai Kia. But the agreement also offers improved access to the Korean market for Canadian-made automobiles — and, more importantly, provides an opening to the vital and burgeoning wider Asian automobile market. This was a cornerstone of the U.S.-Korea Free Trade Agreement, which was finally approved by both the U.S. Congress and the South Korean parliament in late 2011 and has been in effect since March 15, 2012. Think about how important it is to gain access to the Asian auto market — arguably the most important automotive market in the world. Korea is strategic for Canadian firms wanting to do business in Asia. It is centrally located, has a democratic political system and a capitalist economy with strong protections for property rights and a commitment to free trade. Korea is the perfect choice to launch Canada's move to deeper economic integration with Asia. What have we been waiting for?

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About the Author

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