PUBLIC CITIZEN

215 Pennsylvania Avenue, SE • Washington, D.C. 20003 • 202/546-4996 • www.citizen.org

REPORTERS' MEMO

March 16, 2011 Contact: Bryan Buchanan, 202-454-5108

Previewing Ways and Means Chair Camp's Request for USITC Analysis of the December 2010 Korea FTA Supplemental Auto Deal

The U.S. International Trade Commission's (USITC) official study of the Korea "free trade agreement" (FTA) found that it would increase the overall U.S. trade deficit and the automotive trade deficit with Korea and the world.[1] Given that the USITC uses similar equilibrium models on all of its trade pact analyses and that past studies have been improbably optimistic,[2] the USITC study has been unhelpful to efforts to pass the FTA. The USITC found 24 sectors that would suffer increased trade deficits under the Korea FTA, including motor vehicles and parts, other transportation equipment, electronic equipment, metal products, textiles, apparel and iron-containing metals.

Earlier this year, Ways and Means Committee Chair Dave Camp (R-Mich.) requested that the USITC prepare a study covering changes to auto sector provisions agreed upon during December 2010 supplemental negotiations. **The USITC was slated to release the Korea FTA auto sector study to Camp on Tuesday.** Now, Camp must decide if it will be made public. It will be critical to review both the USITC's findings and methodology. We urge Camp to make the study public, rather than release selective quotes from it.

Korea FTA: Selected Losing U.S. Industrial Sectors

(Data from U.S. International Trade Commission Study)	Increase in U.S. global trade deficit by sector (millions of dollars)	
	Low	High
Motor vehicles and parts	($531)	($708)
Other transportation equipment	($340)	($293)
Electronic equipment	($790)	($762)
Metal products	($169)	($187)
Textiles	($169)	($190)
Apparel	($56)	($74)
Iron-containing metals	($65)	($75)

What the USITC concludes will be interesting. **The Korea Automobile Manufacturing Association (KAMA) celebrated the December 2010 supplemental deal: "The deal wiped off uncertainties in the world's largest automobile market and is forecast to drive up South Korean automakers' market share in the U.S. ... Small and mid-size auto parts makers will also benefit from the elimination of tariffs."**[3]

Koreans have not been purchasers of foreign cars. Given both strong "Buy Korean" social preferences and various non-tariff barriers, *total* import penetration is four percent. If the USITC now finds that the Korea FTA's auto trade deficit is less than its original estimates, it is likely based in part on an unrealistic assumption that Korean consumers are as likely as U.S. consumers to buy imported cars. In formal comments to the USITC a month ago, Public Citizen urged the agency to incorporate more realistic assumptions about Korean consumer preferences.

Only timelines for tariff phaseouts were altered: The supplemental deal extended the phaseouts of both Korea and U.S. tariffs but still results in zero tariffs upon full implementation. T**he original USITC study was based on full implementation**. **Thus, there were no tariff changes in the supplemental that should alter the original USITC findings that the FTA will increase the U.S. trade deficit generally and the automotive trade deficit with Korea and the world specifically**.

Low 35 percent auto rule-of-origin not changed: The supplemental deal also did not change the FTA's 35 percent domestic content rule that allows duty-free treatment for vehicles with 65 percent of content sourced from China, Mexico or other nations. Thus, even if the United States were to export more cars to Korea, it would not likely translate into more jobs for U.S. workers in auto parts, steel, glass, tire and rubber. This explains why the unions representing workers in these sectors oppose the FTA, including the Steelworkers, Machinists, Teamsters, IBEW, IBB and CWA-IUE. More U.S. workers are employed in the auto supply chain industries than in auto assembly.[4] The domestic content rule for the EU-Korea FTA negotiated at the same time is 55 percent. The North American Free Trade Agreement (NAFTA) had a 50 percent domestic content rule for autos. Under NAFTA, our auto sector deficit with Canada and Mexico almost doubled from $18 billion to $30 billion.

Calling the agreement's "rule-of-origin" and "duty drawback" provisions "highly problematic" in a September 2010 statement, the United Auto Workers warned that "the U.S. and Korea are effectively signing an automotive free trade agreement with the world."[5] The statement notes: "Workers and their unions in Korea are opposed to the KORUS FTA, in part, because it would encourage Korean manufacturers to significantly increase the sourcing of production to low-wage nations of Asia, including China … Thus, Hyundai, for example, could source the production (and employment) of up to 65 percent of the value of its vehicles to China or elsewhere, import these parts and components back into South Korea for final assembly, and then export the finished vehicle to the United States duty-free." Also, under the FTA, Korea is allowed to refund 100 percent of duties on imported parts. The EU-Korea 55 percent auto rule of origin requires a majority of value to come from the trade pact partners, and duty drawbacks (refunds) are capped at five percent.

Non-tariff barriers: The supplemental deal included a four-year waiver of Korean auto fuel efficiency and emission standards for U.S. imports as well as a waiver of Korean auto safety standards for up to 25,000 U.S. autos per U.S. Big Three maker – if there were demand for such cars. (That is to say that there is no guaranteed access for 75,000 additional U.S. cars.) Other Korean policies identified by the industry and United Auto Workers as posing significant non-tariff barriers to entry were not waived.

It will be important to analyze how the new USITC study deals with the non-tariff issues. For instance, given that Korean consumers' strong preference for domestic cars is connected to a perception that they are safer,[6] will the USITC reduce the likelihood of increased Korean consumer demand as it considers how the waiver could affect auto trade? Moreover, the USITC could assume a scenario that will never exist. The fuel economy exemptions expire in 2016,[7] and tariffs would go to zero in 2022.[8] However, in its modeling, the USITC assumes full implementation – zero tariffs. Will it take into account that the exemptions will not be in effect for most of the tariff cutting period, much less at the zero tariff phase?

Putting aside the conflict between the Obama administration's rhetoric about strong environmental standards in trade agreements and its effort to pressure Korea to waive environmental standards for imports, this approach does not help the U.S. auto sector compete and win the future – which is unquestionably in the direction of cleaner cars.

What does the ITC assume about continuation of U.S. Korean 'transplant' assembly lines here? The elimination of U.S. auto and truck tariffs and the low rule of origin requirements raise the question of whether Korean auto firms now producing cars in the United States would continue their operations. The average hourly earnings of American workers in the auto industry was $23.61 in 2008, 9.2 percent greater than the average hourly earnings of all workers employed in the private sector ($21.62). According to the U.S. Bureau of Labor Statistics (BLS), total hourly compensation per worker, which includes both wages and benefits, was $36.35 for American workers in the auto sector and $23.30 for Korean workers in the auto sector in 2007, so compensation for American auto workers is about 56 percent higher.

The bigger picture: President Barack Obama campaigned and won on overhauling our unfair trade policies. Instead, what Americans face with the Korea FTA is the same Bush NAFTA-style agreement, with slightly altered auto tariff schedules. The Korea trade deal is still projected to increase the overall U.S. trade deficit and cost 159,000 U.S. jobs.[9] The Korea deal requires the kind of financial deregulation that contributed to the economic crisis. The FTA's labor chapter still contains Bush's ban on reference to the International Labor Organization conventions when enforcing its weak labor standards. This agreement even allows South Korean goods to be given the benefits of the agreement even if such goods contain inputs or parts from North Korea, despite our sanctions on trade with that country. And it still has sovereignty-eroding, public-interest-policy-chilling rules that allow multinational corporations to sue governments in private, foreign tribunals for taxpayer money.

ENDNOTES

[1] U.S. International Trade Commission. "U.S.-Korea Free Trade Agreement: Potential Economy-wide and Selected Sectoral Effects." USITC Publication 3949. September 2007, Corrected printing March 2010, at Table 2.2 and 2.3 on pages 2-8 and 2-14.

[2] For example, a 1999 USITC study using roughly the same model estimated that China's WTO accession tariff offer would increase the U.S. trade deficit with China by only $1 billion. (U.S. International Trade Commission, "Assessment of the Economic Effects on the United States of China's Accession to the WTO," August 1999, at xi.) In reality, the trade deficit with China skyrocketed by $167 billion between 2001 and 2008. (Trade flow data from the USITC DataWeb. Deficit calculated on a domestic-imports-minus-imports-for-consumption basis. Figures inflation-adjusted to 2009 using the CPI-U-RS.)

[3] "S. Korean automakers hail KORUS FTA," Yonhap, Dec. 5, 2010.

[4] Based on data from the Center for Automotive Research, Ward's Auto, and the Commerce Department, as cited in "The Ripple Effect: Why Failure of the Big 3 is not an Opinion," Office of Representative Carolyn B. Maloney, 2008, Available at: http://maloney.house.gov/documents/economy/employment/The%20Ripple%20Effect%20(2).pdf.

[5] UAW Statement, September 14, 2010, page 3. See International Metal Workers Federation http://www.imfmetal.org/files/10102608591310005/UAW_KORUS_FTA_ENGLISH.pdf Johanne.

[6] Jeffrey J. Schott, Scott C. Bradford, and Thomas Moll, "Negotiating the Korea–United States Free Trade Agreement," Institute for International Economics, Policy Brief No. 06-4, June 2006, Available at: http://www.iie.com/publications/pb/pb06-4.pdf. Jane Han, "Korean Consumers Turn Backs on Toyota," Korea Times, February 4, 2010, Available at: http://www.koreatimes.co.kr/www/news/biz/2010/11/123_60302.html.

[7] U.S. Trade Representative, "Agreed Minutes on regulations pertaining to automotive fuel economy and greenhouse gas emissions," February 10, 2011, Available at: http://www.ustr.gov/webfm_send/2555.

[8] U.S. Trade Representative, "Exchange of Letters between U.S. Trade Representative Ron Kirk and Korean Trade Minister Kim Jong-Hoon," Available at: http://www.ustr.gov/webfm_send/2557.

[9] Robert E. Scott, "Trade Policy and Job Loss," Economic Policy Institute, Working Paper #289, Feb. 25, 2010, Available at: http://www.epi.org/publications/entry/trade_policy_and_job_loss/, at 10, Table 5.