

**THE PROS AND CONS OF ENTERING  
INTO NEGOTIATIONS ON FREE TRADE  
AREA AGREEMENTS WITH TAIWAN,  
THE REPUBLIC OF KOREA, AND  
ASEAN, OR THE PACIFIC RIM  
REGION IN GENERAL**

Report to the Senate Committee  
on Finance on Investigation  
No. TA-332-259 Under Section  
332 of the Tariff Act of 1930

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## EXECUTIVE SUMMARY

On August 4, 1988, the U.S. Senate Committee on Finance requested the U.S. International Trade Commission to provide a summary of the views of recognized authorities on United States-Pacific Rim trade relations on the pros and cons of entering into negotiations for free trade area agreements (FTAs) with Taiwan, the Republic of Korea, and ASEAN<sup>1</sup>, or the Pacific Rim region in general. In response to the Committee's request, the Commission instituted investigation No. 332-259 on September 9, 1988.

The Committee requested the Commission to solicit and summarize views on "the feasibility and desirability" of using FTAs "to develop a more comprehensive and fruitful approach" to trade with countries in the Pacific Rim. The kind of FTAs the Committee wished to be considered were those that "could include, in addition to the eventual complete elimination of all tariffs and other restrictive regulations of commerce on substantially all trade between the United States and these countries, the removal of barriers to investment and trade in services, and the guarantee of adequate protection of intellectual property rights." The Committee also asked the Commission to present problem areas that, according to experts, would render the completion of these FTAs less than ideally effective, as well as experts' suggestions for alternative policy approaches for the United States. Persons whose views were obtained by the Commission included U.S. and foreign trade negotiators and other government officials, U.S. and foreign private sector representatives active in business or trade between the United States and Pacific Rim countries, academics with relevant country-specific or regional expertise, and executives of industry associations and other nongovernmental organizations.

Several themes emerged from the views put forth by the many representatives of governments, private industry, and academia who participated in the study. Several advantages, disadvantages, and other considerations were presented as common to any FTA, regardless of which country or areas are addressed. These observations are summarized as follows:

- Although participants' definitions of an FTA varied somewhat, there was widespread consensus that any FTA should be GATT-consistent and fairly broad in coverage, including not only general market access issues, but also protection for intellectual property rights and the removal of barriers to investment and services.
- The majority of participants expressed support for the multilateral trading system and indicated that the United States should first concentrate its energy and resources on successfully concluding the Uruguay Round before resorting to another FTA to achieve liberalization objectives. If the Uruguay Round does not prove to be fruitful, the United States might then want to consider FTAs with other countries that have expressed an interest. Moreover, many participants cautioned that embarking on an FTA approach now could derail the Uruguay Round and weaken the multilateral system.
- A widely held perception among participants was that an FTA between the United States and a country or areas that are significantly less economically advanced (including the newly industrializing economies) could not fully achieve free trade among the partners for both economic and political reasons.
- Regarding individual country FTAs, many participants suggested that the markets of any one country or area under consideration in the region might not be large enough in terms of potential benefits to be worth the price the United States would have to pay in trade concessions.
- Although the Pacific Rim region as a whole offers a large market and huge potential benefits resulting from an FTA, negotiations with so many diverse economies at once would not be workable.
- Many participants agreed that the current U.S. negotiating approach with Pacific Rim countries is not effective and cited a need for some alternative approach—although not necessarily an FTA—to foster greater cooperation and coordination of trade policy with these countries.

<sup>1</sup> The member countries of the Association of Southeast Asian Nations (ASEAN) are: Brunei Darussalam, Indonesia, Malaysia, the Philippines, Singapore, and Thailand.

## United States-Taiwan FTA

Taiwan authorities expressed strong interest in a bilateral FTA with the United States. Many U.S. participants interpreted Taiwan's interest as a political maneuver to gain de facto recognition in the absence of formal diplomatic relations with the United States. A large number of participants raised questions about the legal mechanism the United States could use to enter into negotiations with Taiwan. Taiwan authorities and Taiwan businessmen generally favored the notion of an FTA with the United States. However, many U.S. participants were skeptical about the feasibility of an FTA with Taiwan.

Advocates of a United States-Taiwan FTA listed several arguments in support of such an agreement. They foresaw favorable results such as improvements in the negotiating atmosphere, U.S. access to the Taiwan market, and in the bilateral trade imbalance. They also favored the idea because, as Taiwan is not a member of the GATT, United States-Taiwan trade disputes cannot be addressed in that forum.

Participants cited several disadvantages to an FTA with Taiwan. Their arguments sometimes hinged upon the belief that the present approach to trade relations with Taiwan has been successful for meeting U.S. trade policy goals. Some predicted that trade disputes would not abate even under an FTA nor would an FTA alone be successful in increasing U.S. exports to Taiwan. At the same time, they feared Taiwan would seek exceptions to U.S. trade laws and that several important sectors or issues might be excluded from an FTA.

### *Advantages*

Some of the advantages of a United States-Taiwan FTA cited by participants were that it would:

- avoid an "issue-by-issue" or "piecemeal" approach to handling trade disputes and thereby help improve overall relations and resolve a broad range of trade disputes;
- provide both sides with greater predictability and less acrimony in the bilateral trade relationship through comprehensive consideration of trade issues and establishment of a dispute settlement process for future trade issues;
- help rectify the trade imbalance;
- grant the United States the exclusive benefit of Taiwan's tariff reductions;
- improve U.S. access to Taiwan's market at a relatively low cost in concessions by the United States because Taiwan already enjoys a high level of access to the U.S. market;
- serve as a model for other bilateral FTAs in the region, and provide the United States with an important economic foothold in the region to the benefit of U.S. trade with other economies of East Asia; and
- provide a necessary forum for bilateral trade negotiations with Taiwan since Taiwan is not a GATT member and cannot participate in that forum.

### *Disadvantages*

Some of the frequently cited disadvantages of a United States-Taiwan FTA were that it would:

- be unnecessary because the current approach to trade disputes is effective in persuading Taiwan to make tariff cuts and liberalize its market;
- not end bilateral trade disputes because there will always be contentious bilateral trade issues to be dealt with, with or without an FTA;
- allow Taiwan the opportunity to seek an exception to section 301 actions, or, at a minimum, Taiwan would want special treatment regarding the antidumping and countervailing duty provisions of U.S. trade laws;
- require a very long and difficult process for Taiwan's implementation of negotiated changes, because Taiwan's economy would require significant structural reform;



- provide the United States with very little expanded market access in Taiwan because of the relatively small size of Taiwan's market; and
- contain exemptions of certain significant sectors, insisted upon by both the United States and Taiwan. Taiwan, because of structural adjustment problems, would likely try to exclude sectors of interest to the United States—such as agricultural products and services. Similarly, there could be pressure for exclusion of some U.S. sectors, such as textiles and footwear, from an FTA. The end result would be that few important sectors would be left for inclusion in the agreement.

### **United States-Korea FTA**

Although the majority of participants believed that the idea of a United States-Korea FTA is premature, some U.S. participants stated that the United States could gain increased exports and create a less confrontational atmosphere for negotiations. However, most of the participants believed that the possible negative political effects of an FTA with Korea would outweigh economic gains. Many thought that FTA negotiations would probably not be well received by either the Korean Government or its people at the present time because of the current political climate in Korea. The majority of participants agreed that the current negotiation approach with Korea is characterized by a lack of predictability and prioritization but predicted that an FTA would not likely be any less contentious.

#### *Advantages*

Some of the advantages of a United States-Korea FTA mentioned by participants were that it would:

- lead to a more constructive and less emotional atmosphere for negotiations;
- result in the establishment of a regularized dispute settlement mechanism which might introduce more certainty and predictability into bilateral trade negotiations;
- increase U.S. access to the Korean market for certain agricultural products and services; and
- hasten implementation of the Korean Government's scheduled tariff cuts and other liberalization measures.

#### *Disadvantages*

Some of the disadvantages raised by participants were that an FTA would:

- reinforce or increase anti-American sentiment and perpetuate the negative image of the United States held by some government officials and other Koreans;
- not reduce tensions or the high visibility associated with bilateral trade issues;
- allow Korea to stall on trade negotiations or liberalization;
- fail to address certain nontariff barriers and issues, such as investment, subsidies, etc., that currently inhibit U.S. exports;
- prove difficult to implement because of structural differences in the two economies;
- fail to gain wide political support either in the Korean Government or among the Korean population at the present time; and
- send mixed signals about U.S. commitment to the multilateral process.

### **United States-ASEAN FTA**

The majority of U.S. and foreign participants did not think a United States-ASEAN FTA would be workable. They believed that an agreement with ASEAN would be difficult to initiate and to monitor because of the diversity of the ASEAN member economies, cultures, and political systems. In addition, most participants did not believe that an FTA with ASEAN would improve the atmosphere for negotiations or offer many economic benefits to the United States.

Most of the participants who supported the notion of a United States-ASEAN FTA did so provisionally. They felt that the United States should continue its liberalization efforts through bilateral negotiations currently underway, through multilateral efforts in the context of the Uruguay Round, and through the use of the new super 301 authority before taking serious steps toward the FTA option.

As an alternative to a United States-ASEAN FTA, a number of participants suggested that a U.S. agreement with Singapore might be workable and appropriate since Singapore is a free trade nation. Other participants disagreed, partly because, in their view, the United States already has relatively open access to Singapore's markets and not much more in terms of economic benefits could be gained.

### *Advantages*

Some of the advantages of negotiating a United States-ASEAN FTA cited by participants were that it would:

- provide political benefits in terms of improved relations;
- encourage GATT negotiators to push for success in the Uruguay Round and send a "warning shot across the bow" to U.S. trading partners who appear to be foot-dragging that the United States is considering alternatives;
- establish a forum to address a broad range of issues and eliminate the need for the often contentious issue-by-issue approach;
- improve the trade balance by allowing the United States to tap a large and important market; and
- help spur the economic development of the least developed members of ASEAN.

### *Disadvantages*

Among the most frequently cited disadvantages of a United States-ASEAN FTA were that it would:

- be difficult to monitor because of technical problems that would arise involving such issues as rules-of-origin;
- become an irritant; something the United States would have to continually struggle over and change to accommodate the diverse nature of ASEAN members;
- be difficult to negotiate because the ASEAN members themselves are so diverse in terms of size, cultures, levels of development, economic structures, and regulatory and political systems;
- not necessarily improve the negotiating atmosphere because politically sensitive issues, such as nontariff measures, would still need to be addressed on an issue-by-issue basis;
- not necessarily benefit U.S. trade. Many exclusions and exceptions are likely in areas of importance to the United States because of the long-term structural adjustments the ASEAN members would need to make; and
- not improve intra-ASEAN trade.

### **United States-Pacific Rim Regional FTA**

Few participants expressed unqualified support for the idea of a U.S. regional FTA with the Pacific Rim. Those who found the idea attractive in principle noted potential advantages, but tempered their views with warnings on the disadvantages. Even among those participants who saw benefits to be gained, few thought the benefits of a regional accord could outweigh those of a successful Uruguay Round and stronger GATT.

The idea of a regional agreement brought on negative reactions such as "unworkable," "impossible," "ridiculous," "too big," and just "plain dumb." The

overall perspectives of those opposed to a regional FTA varied. Some preferred bilateral agreements rather than a regional grouping. Some opposed both regional and bilateral agreements, attributing similar disadvantages to both. A few participants noted that a regional FTA might be a better alternative than bilateral FTAs because it offers the advantages of economies-of-scale. Some opposed a regional approach as an idea that was premature, but did not dismiss its usefulness at some time in the future.

### *Advantages*

Some of the advantages of a United States-Pacific Rim regional FTA cited by participants were that it would:

- foster improved regional cooperation;
- serve a variety of U.S. interests in the region including military, strategic, and other economic concerns, such as debt and monetary matters. One participant suggested that a regional agreement could also coordinate monetary and fiscal policies;
- provide great potential economic gain because the region is an area of rapidly expanding markets;
- avoid trade diversion, enhance comparative advantage, and provide economies-of-scale, more so than under bilateral arrangements;
- achieve greater specific gains than can be achieved in the GATT by raising the "lowest common denominator" possible in multilateral negotiations and could even augment the GATT; and
- benefit most of those U.S. industries that are open to virtually unrestricted foreign competition but confront significant trade barriers abroad, such as services, telecommunications, and aerospace.

### *Disadvantages*

Some of the disadvantages attributed to a United States-Pacific Rim FTA were that it would:

- be difficult to negotiate with several countries at once, and would result in a regional agreement that could not accomplish its objectives;
- have the political risk of yielding disappointment and poor acceptance both in the United States and in other Pacific Rim members if it cannot achieve truly free trade conditions;
- not avoid the global economic cost of trade diversion and distorted comparative advantage;
- injure certain U.S. industries that are sensitive to imports from Asian countries, such as rubber footwear, textiles, leather and plastic goods, and mushrooms, and yet provide only limited prospects for balancing trade concessions within industry sectors;
- harm political relations with countries not included in the arrangement and further stimulate formation of competing and protectionist trade blocs; and
- harm economic relations because, by leaving significant parts of the world out of the arrangement, it would ignore important global trading interests of the United States and its Pacific Rim trading partners.

### *Alternative Regional Approaches*

Many participants acknowledged the need for some kind of forum or mechanism for enhanced consultation, coordination, and/or cooperation with the Pacific Rim countries. These ideas were manifested in several kinds of proposals. Some suggested loosely knit consultative mechanisms, such as the "Shultz Initiative" and Senator Bradley's "PAC-8" proposal that have been publicly aired in the past year. A few proposed making better use of already existing international organizations such as the Pacific Economic Cooperation Conference. Some thought more formal institutionalization, either an OECD- or GATT-like arrangement, was called for. One participant proposed that the United States should limit itself to an FTA with the "four tigers" of the region—Hong Kong, Korea, Singapore, and Taiwan.

### **Implications for the Multilateral Trading System**

The majority of participants supported the multilateral trading system and the Uruguay Round as the best current vehicle for trade liberalization. A large number of persons thought that the United States should concentrate its attention and resources on bringing about a successful conclusion to the Uruguay Round before embarking on any additional FTAs. A number of participants suggested that it is appropriate and desirable to study the idea of FTAs while the Round is ongoing, as this could provide incentive to the negotiators to reach a successful conclusion. Conversely, others suggested that the "threat" of a U.S. agreement with one or more countries/areas in the region could also be interpreted as another signal that the United States is abandoning multilateralism for bilateralism.

## INTRODUCTION

The Asian Pacific Rim region has been the subject of increasing attention in recent years as its overall trade and its trade surplus with the United States has grown.<sup>1</sup> Many countries in the region are viewed as potentially large and expanding markets with promise for increased U.S. exports. Alternatively, U.S. traders see increasingly fierce competition from these countries at home and abroad, and encounter trade barriers that prevent U.S. products from gaining "free and fair" access to Pacific markets. Although the Pacific countries have made some progress in liberalizing trade barriers, the U.S. Congress and business community have been frustrated with the slow pace of change. At the same time, Pacific trading partners have been frustrated with U.S. demands for reform and the threat of increasing U.S. protectionism. This backdrop has led to new tensions in the relations between the United States and some of its Asian Pacific Rim trading partners and to a desire to seek new solutions to trade conflicts, including the negotiation of free trade area agreements (FTAs).

Since 1985, the United States has taken more aggressive action against unfair trading practices. As part of this overall policy thrust, section 301 cases were pursued more vigorously against Pacific Rim countries such as Korea and Taiwan.<sup>2</sup> The United States also intensified bilateral discussions with other Pacific trading partners, such as Singapore and Thailand, to improve protection of intellectual property rights and to liberalize trade in services. Also since 1985, numerous countervailing duty and antidumping cases against Taiwan, Korea, and some Association of Southeast Asian Nations (ASEAN) members have been filed.<sup>3</sup> In 1987 and 1988, the U.S. Treasury Department expressed concerns that several Asian newly industrializing economies (NIEs) were manipulating foreign exchange rates to keep their currencies undervalued vis-a-vis the U.S. dollar.<sup>4</sup> Effective January 1989, the Reagan administration graduated four Asian NIEs—Taiwan, Korea, Hong Kong, and Singapore—from the list of beneficiaries eligible for duty-free treatment of imports under the U.S. Generalized System of Preferences (GSP), citing their economic successes as a basis for the move.

Concern about the direction of U.S. trade policy has been heightened in the Pacific Rim countries, not only as the United States has more persistently leveled trade complaints against them, but also as it has embarked on what they perceive as a trend toward greater protectionism in U.S. laws and practices. Section 301 cases, as well as antidumping and countervailing duty cases, widely reported in the local press, are often interpreted as near harassment by many in these countries. They are concerned about repeated attempts in the United States to pass a restrictive textile bill and other legislation that might severely impact their exports. They face a U.S. trade regime that offers high levels of protection to certain sectors that are important markets for the Pacific countries' products (footwear, textiles, and steel, for example). They are uncertain how the 1988 omnibus trade bill, with its expanded and stronger powers, particularly under "super 301," will affect them. Free traders like Hong Kong and Singapore believe they are undeservedly caught up in the U.S. campaign against the unfair trade practices of others. Other Pacific countries believe that the United States is making them the scapegoat for its seemingly intractable problems with the European Community (EC) and Japan, while failing to recognize the competitiveness of their products and inadequately addressing macroeconomic roots of the U.S. trade deficit.

These and other trade tensions, the conclusion of FTAs with Israel and then Canada, concerns about Europe's "1992" integration scheme, Japan's seemingly immutable

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<sup>1</sup> The question of which countries may be considered part of the Pacific Rim region is addressed in ch. 4. Within the context of this investigation, and as used in this report, the term "Pacific Rim" does not include Japan unless specifically noted. Considerations regarding Japan were the subject of an earlier Commission study: see, *Pros and Cons of Initiating Negotiations with Japan to Explore the Possibility of a U.S.-Japan Free Trade Area Agreement*, Report to the Senate Committee on Finance on Investigation No. TA-332-255 Under Section 332 of the Tariff Act of 1930, USITC Publication No. 2120, Sept. 1988.

<sup>2</sup> Cases regarding Korea initiated in 1985 involved insurance practices and intellectual property rights and in 1988 involved cigarettes, beef, and wine. Cases regarding Taiwan initiated in 1986 involved export performance requirements; beer, wine, and tobacco sales practices; and customs valuation.

<sup>3</sup> Since 1985 a total of 22 countervailing duty (CVD) cases and 37 antidumping (AD) cases have been filed: Taiwan, 5 CVD and 16 AD; Korea, 6 CVD and 10 AD; Singapore, 3 CVD and 6 AD; Thailand, 3 each, Malaysia; 4 CVD and 1 AD; and the Philippines, 1 each.

<sup>4</sup> Treasury's "Report to Congress on International Economic and Exchange Rate Policy" pointed to such problems with Singapore, Taiwan, and Korea in 1987 and with Taiwan and Korea in 1988.

protectionism, and the need to negotiate with liberalizing centrally planned economies are all factors leading to the idea that the United States needs to pursue alternative approaches. To many U.S. policymakers, FTAs appear to be an attractive option. The current interest in FTAs is also nourished by a perception of the inability of the General Agreement on Tariffs and Trade (GATT) to quickly and effectively enforce its rules and to adequately cover the full range of trade concerns encountered today. Some U.S. decisionmakers suggest that the time has come to supplement or even supplant the multilateral approach with an approach tailored to specific trade problems with particular countries.

U.S. trading partners have also considered exploring the FTA option with the United States, most fundamentally for "protection against U.S. protectionism." Consequently, the idea of an FTA offers a certain appeal on both sides of the Pacific. It is seen as a possible way to better handle trade tensions and market access problems, and to deal with issues, such as intellectual property rights and services, that the GATT does not yet adequately address.

What is an FTA? Although the particulars of each FTA and individual conceptions may vary, a common yardstick is found in the GATT. GATT article XXIV defines an FTA as an agreement under which signatories remove trade barriers on "substantially all the trade" between themselves "within a reasonable length of time," thus setting out some of the conditions an FTA must meet to be consistent with article XXIV and the GATT.<sup>1</sup> It provides that the purpose of an agreement should be to facilitate trade between FTA signatories, not to raise barriers to trade with other GATT members. Essentially, article XXIV exempts FTA partners from the requirements of the most-favored-nation principle of the GATT (article I) that would otherwise require them to apply the same trade concessions equally to all other GATT members.

#### The Finance Committee Request

On August 4, 1988, the Commission received a request from the Senate Committee on Finance to provide the Committee with a summary of views of recognized authorities on United States-Pacific Rim trade relations on the pros and cons of entering into negotiations on FTAs with Taiwan, the Republic of Korea, and ASEAN, or with Pacific countries in general under an arrangement that "interested market economy members could join."<sup>2</sup> The Commission was specifically requested to summarize the views on an FTA that "could include, in addition to the eventual complete elimination of all tariffs and other restrictive regulations of commerce on substantially all trade between the United States and these countries, the removal of barriers to investment and trade in services, and the guarantee of adequate protection of intellectual property rights." The Committee also asked the Commission to present problem areas that, according to experts, would render the completion of these FTAs less than ideally effective, as well as experts' suggestions for alternative policy approaches for the United States. In response to the Committee's request, on September 9, 1988, the Commission instituted investigation No. 332-259 under section 332 (g) of the Tariff Act of 1930.<sup>3</sup>

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<sup>1</sup> GATT Article XXIV:8(b) defines a free-trade area as a "group of two or more customs territories in which duties and other restrictive regulations of commerce . . . are eliminated on substantially all the trade between the constituent territories in products originating in such territories." An FTA differs from a customs union in that a customs union is "the substitution of a single customs territory for two or more customs territories" and "substantially the same duties and other regulations of commerce are applied by each of the members of the union to trade of territories not included in the union" (Article XXIV:8(a)).

FTAs, like the GATT, once may have been interpreted as addressing mainly tariffs or other border measures between countries, but even the GATT; by including "other restrictive regulations" in its description of FTAs, leaves the door open to broader interpretations. Today, both multilateral agreements (e.g., the Tokyo Round Codes) and bilateral agreements, including the United States' FTAs with Israel and Canada, address a wide range of nontariff measures that restrict trade and can involve countries' domestic regulatory affairs. Existing bilateral FTAs extend to services, investment, and intellectual property rights protection, subjects that Uruguay Round negotiators are also seeking to bring under GATT coverage.

<sup>2</sup> A copy of the Committee's letter of request is contained in appendix A.

<sup>3</sup> See appendix B for a copy of the *Federal Register* notice announcing the study.

## **Methodology**

As directed by the Committee, the Commission sought the views of recognized authorities and knowledgeable officials who have worked in the area of United States-Pacific Rim country relations. Persons whose views were obtained included: U.S. and foreign trade negotiators and other government officials, U.S. and foreign private sector representatives active in business or trade with in the Pacific region, academics with relevant country-specific or regional expertise, and executives of industry and other nongovernmental associations.

The Commission obtained views through interviews, formal submissions, and hearing testimony. Direct interviews, the primary research method, were conducted by the Commission with a total of 187 individuals in the United States and in Singapore, Indonesia, Taiwan, Hong Kong, and Korea. Commissioners Rohr and Eckes also traveled to Australia, Indonesia, New Zealand, Singapore and Thailand to meet with high-level foreign government officials and others for the purpose of gathering information relevant to the investigation.<sup>1</sup> The Commission received 40 written submissions, and conducted a public hearing on the matter on November 29, at which 10 panels of witnesses presented their views (see appendix C for a list of the written submissions and witnesses at the Commission hearing). Individuals interviewed, submitting written statements, or testifying at the Commission hearing, are hereinafter collectively referred to as "participants" in the investigation.

Participants interviewed by Commission staff were requested to provide frank and personal opinions rather than official or formal positions of the governments, agencies, associations, or firms by which they were employed. The Commission obtained views on the basis of nonattribution in recognition of the fact that this would be the best method of obtaining the candid opinions desired. The report therefore employs a minimal level of attribution to protect the confidentiality of participants. However, some identification of the group or background of individuals expressing a particular view has been provided when such delineations were possible and meaningful.

A standard questionnaire was not used in this investigation. Generally, participants were asked to define their understanding of what an FTA entails, their assessment of U.S. trade relations with the countries/areas concerned, their opinions of advantages and disadvantages of the FTA approach, and to discuss any other consideration they thought relevant to the subject. With numerous countries/areas and issues involved, the direction of staff questions and the answers provided in interviews generally depended on the particular expertise and experiences of the individual respondent. Frequently recurring opinions and considerations offered by participants were identified by the Commission, forming the basis for the summary of views. For example, although participants' conceptions of an FTA varied somewhat, there was widespread consensus that any FTA should be GATT-consistent and fairly broad in coverage, including not only general market access issues, but also protection for intellectual property rights and the removal of barriers to investment and services.

## **Organization of the report**

Chapters 1 through 4 of this report summarize participants' views regarding the advisability of FTA negotiations with Taiwan, Korea, ASEAN, and the Pacific Rim region. In general, each chapter provides background on merchandise trade with the United States, summarizes certain other relevant considerations raised, summarizes the advantages and disadvantages of entering into FTA negotiations, and discusses suggested alternative approaches and implications for relations with third countries. The fifth chapter of the report summarizes participants' views on the implications for the multilateral trading system. The report does not purport to provide an independent assessment by the Commission on the pros and cons of entering into negotiations regarding an FTA with any or all of the areas or countries covered.

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<sup>1</sup> The breakdown of interviews by group includes: U.S. executive branch, 33; Congressional staff, 3; U.S. academics, 9; Foreign authorities and Government officials, 40; U.S. private sector, 28; other nongovernmental experts, 13; foreign academics, 14; U.S. Government officials overseas, 24; and foreign private sector, 23.





## Chapter 1

### Summary of Views on a United States-Taiwan FTA

This chapter summarizes the views presented by experts in interviews with Commission staff, in formal submissions to the Commission, or in the Commission's public hearing on the possible advantages and disadvantages of the United States entering into bilateral FTA negotiations with Taiwan.

#### Background

##### *United States-Taiwan trade*

In 1988, Taiwan was the 6th largest U.S. export market, and 4th largest source of U.S. imports. U.S. exports to Taiwan consist largely of agricultural products and certain manufactured goods, such as electronic tubes, parts of office machines, digital CPUs and automobiles. From 1985 to 1987, total U.S. exports to Taiwan rose from \$4.3 billion to \$7.0 billion. A majority of U.S. imports from Taiwan are manufactured goods, such as footwear, office machines, machines, furniture, electrical equipment, and textiles and apparel. U.S. imports from Taiwan rose from \$16.4 billion in 1985 to \$24.6 billion in 1987 (see appendix D, for details of United States-Taiwan trade).

The bilateral trade deficit with Taiwan rose from \$12.0 billion to \$17.6 billion over the same period. According to U.S. trade statistics, the U.S. trade deficit with Taiwan has improved during 1988. The deficit with Taiwan was \$9.5 billion during January-September 1988, compared with \$13.8 billion during the corresponding period in 1987. The shrinkage of the deficit is attributable almost entirely to increased U.S. exports, weighted heavily by Taiwan's gold purchases. Subtracting Taiwan's substantial purchases of U.S. gold from U.S. export statistics during January-September 1988 (\$2.5 billion), the trade deficit during the corresponding period in 1988 was about \$11.9 billion. During the first 9 months of 1988, the dollar value of U.S. exports to Taiwan totaled more than \$9 billion, more than double the level of the corresponding period in 1987, whereas Taiwan's exports to the United States remained nearly constant at about \$18 billion. As a result of its impressive economic performance, effective January 1989, Taiwan was no longer eligible to have some of its exports to the United States enter under duty preferences of the Generalized System of Preferences.<sup>1</sup>

<sup>1</sup> For a discussion of Taiwan's graduation from the U.S. GSP Program, see *Operation of the Trade Agreements Program, 39th Report, 1987*, p. 4-41.

##### *Taiwan's trade with the world*

In 1987, according to Taiwan trade statistics, 44 percent of Taiwan's exports went to the United States, 15 percent to Western Europe, and 13 percent to Japan. Thirty-four percent of Taiwan's 1987 imports came from Japan, 22 percent from the United States, and 15 percent from Western Europe. During 1985-87, Taiwan's imports from all sources rose by 71 percent, and Taiwan's exports to all sources rose by 74 percent. Total imports rose from \$19.3 billion in 1985 to \$33.0 billion in 1987. Over the same period, Taiwan's total exports rose from \$30.5 billion to \$53.2 billion. Taiwan's trade surplus with the world was \$11.2 billion in 1985, and \$20.2 billion in 1987.<sup>2</sup>

##### *New Taiwan dollar exchange rate*

The exchange rate of the New Taiwan (NT) dollar relative to the U.S. dollar has been a source of bilateral tension between the United States and Taiwan for some time. Although the NT dollar has been appreciating since the September 1985 Plaza Agreement<sup>3</sup>, the United States argues that Taiwan has intentionally intervened in currency markets and uses other methods to keep the value of the NT dollar artificially undervalued. In 1985, the NT dollar averaged about 40 NT/U.S. dollar, and by late 1988 and early 1989 was being traded at approximately 28 NT/U.S. dollar. In a recent report to the Congress, the U.S. Treasury Department warned that progress toward reducing the bilateral United States-Taiwan trade deficit is being hampered by Taiwan's manipulation of its exchange rate. The report concluded that Taiwan is "manipulating its exchange rate," which is preventing effective balance of payments adjustment and providing Taiwan with an "unfair trade advantage" for its exports to the United States. It said:

Taiwan's underlying economic fundamentals strongly suggest that further appreciation would occur if capital and exchange restrictions were dismantled and market forces were given freer rein.<sup>4</sup>

Moreover, the report stated that such manipulation, "coupled with a lack of structural reforms to strengthen domestic demand and numerous trade restrictions, have frustrated multilateral efforts to reduce global imbalances."<sup>5</sup>

<sup>2</sup> Trade data from *Financial Statistics*, The Central Bank of China, Sept. 1988, pp. 4-5.

<sup>3</sup> During a September 1985 meeting at the Plaza Hotel in New York, finance ministers from the major industrialized countries essentially agreed to support realignment of their currencies in an effort to achieve more balanced trade and economic performance.

<sup>4</sup> U.S. Department of Treasury, "Report to the Congress on International Economic and Exchange Rate Policy," Oct. 15, 1988, pp. 16-17.

<sup>5</sup> *Ibid.*

The United States seeks to ensure that Taiwan "regularly and promptly" adjusts the exchange rate between the NT dollar and the U.S. dollar to facilitate balance of payments adjustments and eliminate unfair trade advantages. In response to the U.S. criticism, Taiwan authorities point out that the NT dollar has appreciated about 44 percent against the U.S. dollar since the Plaza Agreement of September 1985, whereas the South Korean Won has appreciated only 29 percent in the same period.

## Overview

Three main issues were mentioned in the comments of numerous participants who discussed a United States-Taiwan FTA. First, many individuals interpreted Taiwan's goal of an FTA with the United States as a political ploy to gain de facto recognition in the absence of formal diplomatic relations. While not ruling out an FTA for this reason, many of these individuals said that this political issue—real or not—would have to be considered by the United States prior to deciding whether to pursue FTA talks. Second, a large number of participants raised the question as to what legal mechanism the United States could use to conclude an FTA with Taiwan. The wide variety of comments offered on this subject are summarized below. Third, participants, both from Taiwan and the United States voiced criticism of the current approach to United States-Taiwan trade relations. Such criticism, however, was not necessarily an endorsement of the FTA approach to trade relations, but rather an expression of hope that a different, more prioritized approach to handling bilateral trade issues could be found, regardless of the mechanism.

Few groups of participants expressed similar views on the subject of a United States-Taiwan FTA. Taiwan authorities favored the approach. Many U.S. participants, however, were skeptical of the idea of a bilateral FTA, with a number of them suspicious of Taiwan's motives in seeking an FTA with the United States. Taiwan businessmen tended to favor the idea, while many U.S. businessmen questioned its practicality. In general, academics in the United States and Taiwan expressed reservations about the feasibility of an FTA.

In addition to the subject of a United States-Taiwan FTA, a large number of participants commented on the subject of a regional trade grouping. Many participants believed that a regional arrangement including Taiwan would not be feasible, arguing that the various levels of economic development, and political reasons would prevent concluding any regional FTA. They pointed out that if a regional

FTA were negotiated, Taiwan would not want to be excluded. However, U.S. officials and Taiwan authorities both said that Taiwan is fearful of the development of possible trading blocs in the world, such as the EC, North America, or some other regional grouping. Several participants speculated that the future will see regional trade blocs develop, particularly in the East Asia region, with or without the United States.

A number of participants commented on whether the United States has the negotiating resources that may be required to negotiate one or several FTAs. Several said that the United States would need more negotiating resources than it has at present to conclude effectively an FTA with Taiwan. Some questioned how effectively the United States could negotiate with the Uruguay Round in progress. One former U.S. official said that negotiating resources would not be a problem.

## Perceptions about the Political Consequences of United States-Taiwan FTA Negotiations

Several U.S. Government participants felt that there is a large political question involved when discussing the advisability of United States-Taiwan FTA negotiations. These individuals felt that Taiwan's chief motivation for seeking an FTA with the United States is to help reduce its diplomatic isolation and gain some political legitimacy internationally. According to one U.S. Government official, "the original reason for supporting an FTA by Taiwan was 99.9 percent political." A few participants from the U.S. private sector saw no political motivation by Taiwan in seeking an FTA. Several individuals from Taiwan said that an FTA would help Taiwan maintain its economic strength, which would, in turn, help the United States keep the peace in the region. One Taiwan source, alluding to the People's Republic of China (China), pointed to a combined political and economic advantage to Taiwan for establishing an FTA with the United States:

The signing of an FTA will definitely protect our market and strengthen our long term trade relations with the United States. It will also increase the U.S. investment in our economy and serve so that the fundamental interests of the United States will intertwine with our political and economic stability.<sup>1</sup>

Most Taiwan authorities said that China would have little or no reaction to a United States-Taiwan FTA. They argued that the United States and Taiwan have negotiated over 30 bilateral agreements since derecognition of

<sup>1</sup> "Suggestions and Plan on Sino-American Free Trade Agreement." *Economic Daily News*, Jan. 27, 1987.

Taiwan in 1979 without concern by China, and that an FTA could be one—or a series—of such agreements. They also argued that as long as an agreement were kept economic in nature and negotiated through the existing American Institute in Taiwan-Coordination Council for North American Affairs (AIT-CCNAA) framework,<sup>1</sup> there would be no cause for concern by China. Taiwan authorities speculated that the form of any agreement would be of more concern to China than the substance. For example, they said that negotiations that included an act of Congress could be interpreted by China as a sign of a long-term United States-Taiwan institutional arrangement and the Chinese Government would likely protest.

Many U.S. officials were less certain about how China might react to a United States-Taiwan FTA, but did say that a series of AIT-CCNAA agreements could be used to conclude an FTA with Taiwan. These officials speculated that China might react to a United States-Taiwan FTA by seeking some quid pro quo from the United States in terms of market access or some other economic arrangement. One U.S. official said that China might seek some "Caribbean Basin Initiative-type" preferences as compensation for a United States-Taiwan FTA. As a worst-case scenario, another U.S. official suggested that China might react to a United States-Taiwan FTA with something like a Chinese equivalent of the Arab boycott. A U.S. academic said that:

Taiwan would readily agree to an FTA with the United States. They would see it as a guarantee of their security by the United States. An FTA with Taiwan would be an impediment to U.S.-PRC relations. The PRC feels it has bent over backwards to accommodate the United States in regard to Taiwan. It would view the FTA as an attempt to keep Taiwan out of its hands. It would feel betrayed.

One U.S. official said that China has not criticized Taiwan for having close economic relations with the United States in the past, and therefore might not react very strongly to a United States-Taiwan FTA. He added, however, that an FTA would have to be careful not to accord officiality on Taiwan. Another U.S. official stated that:

We could do it [an FTA] but Taiwan is not the problem; the PRC is the pro-

<sup>1</sup> When the United States established diplomatic relations with the People's Republic of China in 1979, two separate unofficial agencies were set up pursuant to the Taiwan Relations Act to continue administering unofficial relations between the United States and Taiwan. The U.S. government created AIT and Taiwan authorities established CCNAA.

blem. It would vastly complicate our dealings with a billion people if we entered into negotiations with Taiwan and I'm not sure we want to do that.

A former U.S. negotiator said:

It is hard to envision an [FTA] agreement with Taiwan without having a fallout with the PRC. That is a simple fact of life any administration must take into account.

In a formal submission, the Government of the People's Republic of China expressed opposition to the idea of the United States negotiating and FTA with Taiwan. The submission, a letter from the Ambassador of the People's Republic of China to the United States, stated that in three U.S.-China Joint Communiques:<sup>2</sup>

... the United States recognizes that "Taiwan is a part of China", and that "the Government of the People's Republic of China as [sic] the sole legal Government of China" and that "Within this context, the people of the United States will maintain cultural, commercial, and other unofficial relations with the people of Taiwan. . . . As called for by the spirit and principles contained in the three Sino-US Joint Communiques, the U.S. Government can establish and develop governmental relations only with the Government of the People's Republic of China. To enter into any official contact with the Taiwan authorities on the ground of resolving trade or other issues constitutes a violation of the three Joint Communiques. Naturally, the Chinese Government is firmly opposed to such contacts, to say nothing of concluding a governmental "agreement" with the Taiwan authorities.

The letter concluded that so long as both the United States and the People's Republic of China "strictly adhere to the spirit and principles of the three Joint Communiques, the Sino-U.S. relations [sic] will continue to develop steadily."

Additionally, a participant from the Government of the People's Republic of China said an FTA must be a governmental, official agreement. He said that a United States-Taiwan FTA would hurt, and could have serious consequences to, the bilateral United States-China relationship. He emphasized that whether an agreement were considered official or unofficial, the Government of China would see it as "invalid and illegitimate." He further stated

<sup>2</sup> Joint Communiqué of Feb. 28, 1972; Joint Communiqué on the establishment of diplomatic relations between the United States of America and the People's Republic of China, Jan. 1, 1979; and Joint Communiqué of the United States of America and the People's Republic of China, Aug. 17, 1982.

that the Taiwan Relations Act (which governs the United States-Taiwan relationship) is a part of U.S. law and not international law; hence it is not recognized by the Chinese Government.

Several other participants said that the United States need not be greatly concerned about the reaction by China to a closer economic relationship with Taiwan. One former U.S. official said that the United States greatly overestimates China's reaction to a U.S. agreement with Taiwan and other issues, "to an irrational degree." Another participant, familiar with Chinese protestations about the United States-Taiwan relationship, characterized China's submission as "standard boilerplate language."

Many participants stated that negotiating an FTA with Taiwan as a treaty would not be possible because the United States does not have formal diplomatic relations with Taiwan. However, as one U.S. official said, if the idea of pursuing an FTA were considered on purely economic grounds and found to be in the economic interest of the United States, then the United States would find a suitable mechanism for such an agreement. According to some participants, executive agreement—negotiated through AIT-CCNAA—could, in theory, provide the legal basis for an FTA. These individuals noted that the specific legal entity for an FTA may depend on the particular elements contained in a bilateral FTA, but mentioned the following options. First, a United States-Taiwan FTA—negotiated "not as a treaty"—could be sent to Congress to act upon after its completion. The purpose of this method would be to get Congressional approval in some sui generis manner, while side-stepping the use of a treaty. Second, it was suggested that an FTA could take the form of an executive agreement, like all previous United States-Taiwan agreements negotiated through the auspices of AIT-CCNAA. One participant suggested this option would be suitable for an FTA, and any future United States-Taiwan agreements, "until the courts decide otherwise." Third, it was suggested that the United States may be able to use existing bilateral trade agreement negotiating authority for a United States-Taiwan FTA. A fourth option mentioned was that an agreement could be negotiated but the term FTA should be avoided, as it implies a formal, governmental agreement, an implication to which the Government of China may object. It was suggested that terminology such as "comprehensive economic agreement" could be used instead, with such an agreement negotiated through AIT-CCNAA.

### **Perceptions About Cultural Differences**

Some participants speculated that the cultural differences between Taiwan and the United States were so great as to effectively preclude

FTA negotiations. They pointed out that the United States and Canada, with economies much more similar than those of Taiwan and the United States, encountered numerous difficulties in negotiating and approving a bilateral FTA, and speculated that such problems would be much worse between the United States and Taiwan. One former U.S. official said, however, that Taiwan is "not as worried about being eaten alive by the United States" as was Canada so the issue of cultural differences may not be a problem. Another U.S. official noted that perhaps the sizeable cultural differences were significant enough to ensure that neither would fear being diluted by the other.

Some participants said that certain cultural differences between the United States and Taiwan, such as business practices of private individuals, would not be addressed by an FTA. They speculated that these differences might be significant enough to impede achievement of significant FTA results. For example, a U.S. policy analyst said:

In most Asian countries, the operating principle has been a distinct preference for domestic sourcing and the nature of the business relationship is often based on strong personal relationships that are difficult to break—and this would be difficult to address in an FTA. Because of these differences, U.S. businessmen would wonder why they are getting little new business if an FTA went into effect and might think a lot of collusion exists. The Asian response to this criticism would likely be "That's just the way we operate."

### **Perceptions About the Current Negotiating Approach**

Observers on both sides of the bilateral relationship stated that the United States' current approach to trade relations with Taiwan, driven largely by use and threat of use of Section 301, is ineffective and can become counterproductive. For example, many participants said that with every bilateral trade dispute that arises, U.S. negotiating resources are concentrated on resolving the particular issue without consideration of the overall economic relationship. A U.S. businessman in Taiwan spoke about what he perceived to be the problem with the current approach to trade disputes:

The danger of the current approach is that you lose goodwill in Taiwan over small items like turkey, cigarettes, etc. It is absurd that an item like that can dominate the news and become a significant negative factor. The U.S. comes across as a whining bully.

This individual also stated that bilateral trade friction is caused in part by the U.S. Government

speaking with many voices (the administration and Congress, for example), which can confuse U.S. trade partners about U.S. trade policy intentions. One U.S. official summed up the view expressed by many participants both in the United States and Taiwan regarding the current negotiating approach:

The current "fire in the in-box" approach of trying to solve bilateral trade problems by using threats of section 301 does not lend itself to an overall strategy or prioritization of what's important in trade relations. For example, there are several major infrastructure projects underway in Taiwan, but the United States emphasizes things like turkey parts. This has a deleterious spillover effect on entire economic relations, it colors the relationship. If an FTA could help us prioritize issues to prevent small disputes from coloring the entire economic relationship, then it would be advantageous. We should be pushing for the \$1 billion contracts for rail cars Taiwan is trying to buy, and instead we're arguing over \$1 million worth of trade in turkey parts.

Several participants said that the United States needs to rectify its budget and trade deficits before concerning itself with any new approach to trade relations. Some individuals said that the goal of reducing Taiwan's trade surplus with the United States should not be addressed through an FTA, but rather through the United States rectifying its domestic budget imbalances. One Taiwan academic stated that:

Although the United States has succeeded in browbeating those of her trade partners that have developed trade surpluses because of the overspill of the U.S. excess expenditures into appreciating their currencies by 45 percent or more, its trade deficit is still far from being eliminated. Unless the root cause of the trouble, i.e., the tendency of the United States to overspend its national income, is eradicated, the imbalance in its trade will not be cured with or without FTAs.

One U.S. official stated his views more bluntly:

Concentrating on an FTA is a cop-out from facing the real problems of our economy, which have been created at home. One of the biggest problems is our budget deficit.

### **Advantages of the FTA Approach With Taiwan**

The following section summarizes the major advantages of a United States-Taiwan FTA as

described by participants during the course of this study. In addition to conducting interviews, the Commission received a number of formal submissions advocating a United States-Taiwan FTA. These submissions advocated a United States-Taiwan FTA for many of the reasons contained in the following sections.

#### *More comprehensive, less piecemeal approach to trade relations*

A large percentage of participants both in the United States and Taiwan stated that an advantage to FTA negotiations would be for the two trading partners to get away from an "issue-by-issue" or "piecemeal" approach to handling trade disputes. Some participants argued for a more "common sense" approach to trade issues with Taiwan. Several U.S. officials questioned the logic of committing U.S. negotiating resources to successive bilateral disputes and mentioned that the FTA approach of considering issues all at once with some prioritization would be more efficient. One participant suggested that an FTA could be thought of:

... as an omnibus trade pact. It would not be a piecemeal approach, but would lump everything together. This would be more efficient. All tradeoffs could be made at once.

Some individuals on Taiwan see an FTA as a constructive alternative to the current method of handling trade disputes. The United States, it was said, pressures Taiwan into a near-continuous cycle of urging market liberalization but remains unsatisfied with the results. An FTA is seen by many of its advocates on Taiwan as a preferable alternative to this approach. The cycle of trade negotiations was viewed by some participants as having a detrimental effect on Taiwan that goes beyond trade relations. One Taiwan businessman said:

Taiwan has a sense of insecurity. They [Taiwan] feel like they need total control. By liberalizing they feel like they are losing control. If they had an FTA they would feel like they had some permanency. When the U.S. pushes Taiwan, it aggravates this sense of insecurity. Taiwan resists and tries to find another cover by sending [trade] delegations to the Soviet Union. The U.S. pushes [Taiwan] in that direction. The U.S. needs a long-term strategy in the Pacific Region.

#### *Would improve U.S. trade and bilateral relations*

From 1985 to 1987, the U.S. trade deficit with Taiwan rose from \$12.0 billion to \$17.6 billion. Many participants who supported the concept of a United States-Taiwan FTA suggested

it would help rectify the trade imbalance. These individuals argued that improvements in market access for the United States under an FTA would mean increased U.S. exports and a reduction in Taiwan's trade surplus with the United States. For example, one participant from Taiwan said that in order to reduce the bilateral U.S. trade deficit, Taiwan has made "every effort such as applying lower import duties on U.S. products, increasing quantity on procurement of U.S. goods and removing nontariff barriers. However, your government still does not find the result satisfying." The participant viewed a bilateral FTA as the "most effective solution" to that problem.

Several individuals in both Taiwan and the United States said that one reason for concluding a United States-Taiwan FTA was that it would provide the United States with the exclusive benefit of Taiwan's tariff reductions. Many Taiwan and U.S. individuals noted that at present, the United States pressures Taiwan to provide market access in specific product areas on a most favored nation (MFN) basis, and after Taiwan agrees to open its market, Japanese and European firms take the majority of the market share. An FTA, these individuals argue, would provide the United States with the exclusive benefit of the tariff cuts. A Taiwan businessman made this point with the following illustration:

Right now, MFN tariff cuts made by Taiwan at the insistence of the United States allow other countries to benefit and gain market share thanks to U.S. efforts. In the case of chocolate, for example, the United States pushed for Taiwan to liberalize its import protection of chocolate. Taiwan agreed to do so, cut the chocolate tariff, and who got the market share? Switzerland and Japan did. So Taiwan would like to make exclusive tariff cuts so only the United States and not Japan or other countries would reap the benefit of the tariff cuts. So an FTA would be beneficial to the United States. It would help U.S. products sell in Taiwan.

Echoing this viewpoint, a U.S. academic said that in his view, every market opening negotiated by the United States in East Asia is followed by "Japan stepping in and grabbing the market. An FTA would solve this problem by guaranteeing U.S. access. Taiwan already has unlimited access to U.S. markets; an FTA can only help us."

An advantage frequently mentioned by Taiwan authorities is that, in their view, an FTA would provide Taiwan with predictable, ensured access to the U.S. market. This would give Taiwan a secure market for more than 40 percent of its exports, and provide opportunities for export expansion. Taiwan would also have better

access to the U.S. market than Singapore, Korea or other countries. One Taiwan authority stated that Taiwan would hope for some "insulation from U.S. protectionism" with an FTA and that this was Taiwan's greatest incentive for concluding such an agreement.

Numerous participants suggested that a United States-Taiwan FTA would put an end to the frequent United States-Taiwan disputes. A comprehensive consideration of trade issues under an FTA, along with establishment of a dispute settlement process for future trade issues, many argued, would provide both sides with greater predictability and less acrimony in the bilateral trade relationship. One Taiwan authority stated that with an FTA, Taiwan would be "a part of the U.S. domestic market, just like California and Texas are," and that all bilateral trade problems would be solved.

#### *Would benefit the United States at a relatively low cost*

Several U.S. businessmen said that with a bilateral FTA, the United States would gain access to Taiwan's market at a relatively low cost because Taiwan already enjoys a high level of access to the U.S. market. These individuals noted that the U.S. market is already very open and U.S. tariffs are lower overall than Taiwan's tariffs. For these reasons, they suggested that removal of U.S. tariffs on imports from Taiwan would not cause a flood of Taiwan exports to the United States. In both Taiwan and the United States, some participants said that there would be some possibility for expanded U.S. exports to Taiwan with an FTA, particularly as Taiwan's middle class grows, the standard of living rises, and consumers there seek to purchase more imported consumer goods.

One submission detailed the potential effect on major U.S. industries under an FTA with Taiwan. In terms of U.S. export industries, it stated that several sectors, such as agriculture and processed foods, precision instruments, primary metals, leather, transportation equipment, lumber and wood products, and miscellaneous manufactured items (e.g., toys, games, and costume jewelry) would benefit from an FTA that reduced Taiwan's tariffs for U.S. exports in these sectors. In certain other industries, the submission stated that U.S. export interests, such as electronic equipment and components, chemicals, and machinery, could realize a competitive advantage in Taiwan over other foreign, largely Japanese, suppliers if preferential tariffs were negotiated for these industries under an FTA. The submission also stated that including a provision to reduce service barriers would be beneficial to the United States.

#### *Would facilitate Taiwan's structural adjustment*

Many participants supporting a United States-Taiwan FTA emphasized that, in their

view, Taiwan needs to liberalize and restructure its economy, particularly the agricultural sector, and undertake other "necessary" structural adjustments. These participants speculated that Taiwan could liberalize its economy with fewer domestic political problems with an FTA as the reason for the changes than without one. One participant from Taiwan said that Taiwan needs the "push to change its economic structure" that an FTA would require. Another view was that although an FTA would create more economic disruption in Taiwan than in the United States, such economic change "neatly tracks the Taiwan authorities plans to restructure the economy and shift domestic production and exports to higher-value goods." One Taiwan source noted that although some currently protected industries in Taiwan might suffer from import liberalization mandated by an FTA, in the long term, "they will benefit from the higher efficiency and competitiveness forced by competition."<sup>1</sup>

A Taiwan businessman expressed a view common among others from Taiwan when he implied that Taiwan cannot work on restructuring its economy while also dealing with any bilateral trade disputes that may occur:

Give Taiwan time to adjust to an FTA without the threat of retaliation and an FTA probably would be beneficial. Taiwan is tired of trade negotiations every 2 or 3 months about doing this or that. We can't do business with these little disputes cropping up. This is not good for Taiwan's industry. It's a good idea if Taiwan's industry can be left alone for a while and be allowed to adjust.

Another Taiwan businessman also commented on what he identified as the need for structural adjustment by Taiwan, and the possible disruptions in the agricultural sector that an FTA might cause, stating that "[Taiwan's] farmers will be adversely affected, but can Taiwan keep the status quo even without an FTA?"

*Would provide a model for other FTAs and regional U.S. economic base*

A few participants suggested that one advantage of a United States-Taiwan FTA would be as a model for other bilateral FTAs in the region. A model FTA, it was argued, would demonstrate the feasibility of negotiating similar agreements both to the United States and to other trade partners in the region interested in FTAs. These individuals also mentioned that the United States could use an FTA with Taiwan as an important economic foothold in the region to the benefit of U.S. trade with other economies of East Asia. A Taiwan businessman suggested the

United States should consider a United States-Taiwan FTA as a "pilot project" for future U.S. FTAs with leading economies of the region:

There is not much in an FTA for the United States in terms of gains in dollars, but if you looked at it as a pilot project for the Asian Pacific it makes sense. Asia is not an EC, it is not a common market. Only one or 2 leaders will emerge in the region . . . If the U.S. wants to keep its position in the Asian Pacific, it should seek allies and get a foothold [there]. There isn't any possibility of [Taiwan] concluding an FTA with Japan. It makes a lot of sense politically and economically [for the United States] to conclude an FTA with Taiwan. As a starter and as a base for further expansion. It's not feasible economically or politically with other countries.

A few other participants suggested that negotiating an FTA could be a useful experience and could lead to the future establishment of a "Pacific Free Trade Zone." Another Taiwan source suggested that a United States-Taiwan FTA could serve as a model for other countries that have trade relations with Taiwan, and could promote similar agreements with Taiwan.

*Would substitute for lack of GATT membership by Taiwan*

Many participants suggested that an important reason for negotiating a United States-Taiwan FTA is that Taiwan is not a GATT member. Although Taiwan seeks to join the GATT, many participants in the United States and Taiwan speculated that Taiwan's effort to join the GATT is a long-term goal with an uncertain outcome. In a submission, one participant stated that Taiwan is the largest U.S. trading partner outside the GATT system, and therefore should be subject to a more formal bilateral arrangement than the present approach. The participant noted several factors that support the concept of a United States-Taiwan FTA:

The fact that Taiwan is currently not a GATT member is another major reason for the establishment of an FTA with the United States. Otherwise, the U.S. trade relations with such an important partner would not be fully regulated and would not fall under any framework. This is especially necessary in light of the expected Uruguay Round discussions which will lead to policies governing areas of international trade which have not been regulated in the past. In addition, the bilateral approach would help the United States further its multilateral goals. It will stimulate recalcitrant trade partners at the same time it will showcase new trade concepts and approaches that

<sup>1</sup> "Suggestions and Plan on Sino-American Free Trade Agreement." *Economic Daily News*, Jan. 27, 1987.

can be used as precedents for later implementation in the multilateral arena.

### **Disadvantages of the FTA approach with Taiwan**

The following section summarizes the major disadvantages of a United States-Taiwan FTA ascertained during the course of this study. In addition to conducting interviews, the Commission received a number of formal submissions opposing a United States-Taiwan FTA. These submissions opposed a United States-Taiwan FTA for many of the reasons contained in the following sections.

#### *The current approach is effective*

Many U.S. officials said that a United States-Taiwan FTA is unnecessary because the current approach to trade disputes is effective in persuading Taiwan to make tariff cuts and liberalize its market. They point out that U.S. pressure on Taiwan has resulted in numerous market opening initiatives by the Taiwan authorities that would have been absent but for U.S. pressure and the threats of section 301 action. "Success will come from continued pressure" of this type, one U.S. official said, although he went on to say that some overall framework to handle and prioritize trade relations would be convenient. Also speaking in favor of the current approach to trade negotiations, one participant noted that "maybe the squeaky wheel needs to be heard." A U.S. official said:

Section 301 will work better under the new provisos. It should now be quicker and less cumbersome. In the past it has been cumbersome. We have to wait and see. Some things we raise hell about are not that big a deal. I don't agree that we hurt our overall relationship with the trade issues. This is a contest between U.S. agencies. There are trade partners that the State Department doesn't want us to beat up on.

A number of participants suggested that FTA talks with any of the Pacific Rim trade partners would be premature at this point. One said that it would not be productive to focus on bilateral discussions on possible FTA talks until "many more" of the outstanding trade issues are resolved. Some participants suggested that the United States should exhaust bilateral and multilateral efforts, including use of "super 301" provisions, before taking any serious steps toward FTAs with trading partners like Taiwan and Korea.

#### *Would not end trade disputes*

Some participants said that an FTA would not mean the end of bilateral trade disputes. These

persons, both in the United States and Taiwan, pointed out that, in their view, there will always be contentious bilateral trade issues to be dealt with, with or without an FTA. One individual in Taiwan noted that the existence of dispute settlement provisions in the United States-Canada FTA recognizes the likelihood of continued bilateral trade disputes under the agreement. A U.S. businessman in Taiwan, commenting on the possibility of future trade disputes under an FTA, said:

Taiwan isn't as bad as Japan in terms of nontariff measures, but they [NTMs] aren't low here [in Taiwan] either. It is still a difficult system to compete in. Even an FTA wouldn't solve all the trade problems.

A U.S. Government official reasoned that the differences between the United States and Taiwan could be significant enough to preclude reaching a meaningful FTA, and could mean increased trade conflict. He said that:

The United States and Taiwan societies are very different culturally and organizationally. This can mean a great deal of change on their side to adjust to an FTA, since nobody seems to be suggesting that the United States would try to conform to Taiwan's regulatory regimes with an FTA. This could mean more bilateral conflicts and demands, not less. These complications would multiply with the number of countries we would try to negotiate bilateral agreements with. We could just end up with some lowest common denominator for an outcome; a very general statement with little meaning to it.

#### *Taiwan would seek exemption to U.S. trade laws*

Many participants speculated that Taiwan would be likely to seek an exception to section 301 actions under an FTA. A few others suggested that at a minimum, Taiwan would want special treatment regarding the antidumping and countervailing duty provisions of U.S. trade laws. For example, in reference to Taiwan and Korea, one U.S. academic said that these two trading partners:

... think an FTA might counteract American unilateralism. Given the vehemence with which these two react to Section 301, they would almost certainly look for U.S. concessions on use of Section 301 and dumping laws.

Also on the subject of exceptions to U.S. trade laws in an FTA, one U.S. official added that:

The biggest disadvantage is in manufacturing. The U.S. will be gravely hurt by even more imports from the



region, which would result from the FTAs relaxation of our countervailing duty laws. This relaxation is a major goal of Korea and Taiwan.

One U.S. official speculated, however, that Taiwan might not seek exemption to section 301 since "presumably the FTA would eliminate the barriers that 301 normally fights."

#### *Would be difficult to implement in Taiwan*

Observers both on Taiwan and in the United States suggested that the different levels of economic development between the United States and Taiwan mean that any changes negotiated under an FTA would require a very long and difficult process for implementation by Taiwan, particularly in the areas of most interest to the United States, such as agriculture, protection of intellectual property rights, and services.

Some participants suggested that there may be strong political support for exclusion of such areas from any FTA, because the structural adjustment that the inclusion of these areas would require of Taiwan could be too great to be supported in there. Similarly, they mentioned that there could be pressure for exclusion of some U.S. sectors from an FTA with the end result being, they argued, few areas left for inclusion in an FTA. One U.S. official, for example, said that Taiwan would want to exempt agriculture from the negotiations and the United States would want to exempt textiles and footwear. One advocate of a United States-Taiwan FTA said:

As in the two previous FTAs the United States negotiated, the Multifiber Arrangement would undoubtedly remain in force, protecting the industry even as its tariffs are reduced—and slowly at that.

One Taiwan academic suggested that the United States wait until after Taiwan's 1989 elections before deciding whether to pursue the FTA approach. After that election, he said, the voting intentions of the farmers on Taiwan will be better known, and the Taiwan authorities will be able to decide on the right course to follow. Until then, he said, trade and FTA issues should be kept low key because "Taiwan is opening up politically and it can't disregard totally the public opinion and protests of the farmers."

Taiwan's agriculture, automobile, and high-technology sectors were frequently identified as being vulnerable to U.S. competition under an FTA. In this light, some U.S. officials said that economically Taiwan is not ready for the changes that would be asked of its economy in an FTA. Some observers said there is too much structural adjustment needed by Taiwan—particularly in the agricultural sector—for the United States to expect increased access through an FTA. U.S. Government and Taiwan sources both stated that

Taiwan's agricultural sector and automobile industry in particular would suffer under increased competition from the United States under an FTA. Another Taiwan participant, speculating that agriculture and high-technology industries would be unfavorably affected by an FTA with the United States, said:

If U.S. agricultural goods enter Taiwan freely without any customs duty, only the labor-intensive and some special products can survive. Others, particularly the extensively cultivated products like corn, beans, and perhaps even rice, cannot compete with the United States, and the life of 4 million farmers will be seriously threatened. Unless industry can absorb 1.3 million laborers from agriculture, the [authorities] should be very cautious about the possible political and economic consequences after the establishment of an FTA.<sup>1</sup>

On the subject of high-technology industries in Taiwan, the participant continued:

Accelerating the development of science and technology is the key for the future economic growth and the survival of tech-related industries. So far, Taiwan is far behind the United States in its capability to develop science and technology. If it opens to the United States under such circumstances [an FTA], some young tech-related industries will be destroyed and those waiting to be developed will never [do so].<sup>2</sup>

A Taiwan academic, referring to anticipated difficulties in negotiating about agriculture in FTAs with Taiwan, Japan, and Korea, stated that "perhaps the U.S. will tolerate some exceptions to full free trade principles in the case of agriculture. Otherwise, "it might be rather difficult to reach agreement" with those trade partners in FTA negotiations. Another Taiwan individual stated that "some occupations such as finance, insurance, etc., which are still under government protection will sustain heavy impact [with an FTA] because of the gap in quality and service. Whether we should let the United States take over these occupations and how serious it will damage us are questions waiting to be answered."<sup>3</sup>

#### *Would not significantly improve U.S. trade*

Some U.S. officials said that Taiwan would stand to gain a lot from the United States with an FTA, particularly if Taiwan were to obtain exemption from some U.S. trade laws or

<sup>1</sup> "The Advantages and Disadvantages of Establishing Sino-American Free Trade Zone." *Economic Daily News*, Jul. 20, 1985.

<sup>2</sup> *Ibid.*

<sup>3</sup> "The Advantages and Disadvantages of Establishing Sino-American Free Trade Zone." Broadcast in Taiwan, Sept. 13, 1988.

relaxation of import restraints in areas such as steel or textiles. These officials speculated that the United States would gain very little expanded market access in Taiwan. To support this view, they pointed to the relatively small size of Taiwan's market (20 million) and said that many areas of interest to the United States—such as agricultural products and services—would most likely be exempted, at least initially, from an FTA. Some participants speculated that Taiwan would probably seek expanded market access in sensitive areas currently restricted by the United States, such as steel and textiles. In addition, some individuals in Taiwan noted that Taiwan's sporting goods and footwear sectors could significantly gain U.S. market share with an FTA.

Some observers in Taiwan and the United States speculated that an FTA may increase trade, but would not eliminate Taiwan's bilateral trade surplus. They argued that Taiwan's imports from Japan are price inelastic, so that a United States-Taiwan FTA would probably mean trade creation with the United States without trade diversion from Japan, hence a worse United States-Taiwan trade deficit. Several participants said that there would be little room for more agricultural imports from the United States to Taiwan without high political cost in Taiwan but that Taiwan's exports to the United States would grow. One Taiwan businessman speculated that with increased Taiwan exports to the United States, "with an FTA, Taiwan will have near total reliance on the U.S. economy". He asked rhetorically, "Does Taiwan want this?"

Regarding Taiwan's agriculture market, several participants in the United States and Taiwan speculated that the United States would gain little in terms of increased agriculture exports to Taiwan. One participant summarized his views as follows:

This is the single largest area of problems for Taiwan. There is uneven distribution of income in Taiwan. An agreement favoring Taiwan's manufacturing sector at the expense of the agriculture sector would be difficult to justify. But even if the agricultural sector were opened totally, there would be little benefit to the United States. Taiwan already imports a lot of agricultural products from the United States. There is not much room for expansion. Any expansion would be at a big price politically in Taiwan. . . . But this is not so problematic as to foreclose the FTA option. The sector is not too big. There is pollution of some farmland; some farmers are selling their land to golf course developers. . . . The question is not yes or no for the sector alone, but rather, what kind of deal can be made for farmers.

A Taiwan academic observed that in many agricultural commodities, U.S. goods already dominate Taiwan's imports.<sup>1</sup> He said that this dominance is partly due to existing preferences for U.S. products in Taiwan. He speculated that "these imports from the United States will probably not respond very sensitively to further elimination of tariffs alone."

Several U.S. industry groups registered their opposition to negotiating an FTA with Taiwan or other trading partners in formal submissions to the Commission. These industries expressed concern that an FTA with Taiwan and/or other trading partners in the region could mean increased U.S. imports, fairly or unfairly traded, at the cost of lost production and employment in the competing U.S. industry. Some of these organizations also expressed disappointment with the past U.S. negotiating record with Pacific Rim trade partners. One participant suggested that an FTA that provided equal or better tariff preferences to Pacific Rim trading partners than to Caribbean countries and Mexico would, in effect "dilute or erase altogether" trade benefits of such existing U.S. programs as the CBI and the maquiladora program with these neighboring trade partners.

Some participants said that even with tariff preferences under an FTA, U.S. firms would not necessarily increase their market shares in Taiwan because of, for example, "historical preferences." They said that Taiwan purchasers consider not only price when buying imported products, but also quality and other factors, such as after-sales service. These individuals noted that other countries, such as Japan, are very competitive in such nonprice matters. In addition, one U.S. businessman said that a problem with FTAs in general is that bilateral FTA tariff preferences create "insulation from competition" that can harm U.S. competitiveness in other export markets.

Some U.S. businessmen offered other possible reasons why, in their view, FTAs may not increase U.S. exports. Some said that with one or more FTAs, U.S. imports from the region would increase without substantial increases in U.S. exports because, U.S. firms are not sufficiently export oriented compared with their East Asian counterparts. Another U.S. businessman said that:

If all of the trade barriers were removed in Asia, Europe and Japan would benefit. The United States can't compete with their export financing packages. Until those facts change, U.S. exports won't improve in the region.

<sup>1</sup> To make this point, the participant gave examples of U.S. export shares to Taiwan in oil seeds (84.1%), grains (79.7%), tobacco (79.5%), papermaking materials (55.0%), and leather (49.8%).

## Effects on Third Countries

Many views were offered regarding the possible effect of a United States-Taiwan FTA on third countries. A common view was that such an accord would compel other U.S. trade partners in the region to seek similar arrangements with the United States, particularly those with economies that compete directly with Taiwan for the U.S. market.

Several views were offered regarding the possible reaction by Korea to a United States-Taiwan FTA. For example, one U.S. government official speculated that Korea might view a United States-Taiwan FTA as a means for Korea to gain greater entry into the Chinese market, assuming a United States-Taiwan FTA would disrupt U.S. trade and political relations with China as well as indirect trade between Taiwan and China. A U.S. businessman in Taiwan said that a United States-Taiwan FTA would alarm Korea the most, which "looks at Taiwan as a direct competitor [for the U.S. market]. Japan is in a different league." From the perspective of a U.S. businessman in Korea, a United States-Taiwan FTA would probably persuade Korea to seek an FTA. He cautioned, however, that:

...one way to decide about an FTA is to go slow, see what happens with Canada and see what [trade] patterns develop. If it goes well with Canada, then we should do it with other countries. It would be dumb to negotiate with many countries simultaneously.

Other participants speculated that a United States-Taiwan FTA would induce Korea to seek a similar arrangement with the United States. For example, an academic at a Korean Government think tank said that "negotiating an FTA with Taiwan would scare Korea."

Several participants suggested that a United States-Taiwan FTA would create a strong reaction within ASEAN countries. An Indonesian academic speculated that a United States-Taiwan or U.S.-Korea FTA would be "to the detriment of ASEAN. Our [U.S.] market shares are far below those of Korea and Taiwan. It would force ASEAN to take a common stance. It would galvanize ASEAN." A U.S. businessman in Singapore said that if an agreement with Taiwan or Korea were done, but not an agreement with ASEAN, "the effect on Singapore would be substantial. . . it would be perceived as a real blow to Singapore. You would see the effect on the shifting of manufacturing and

investment patterns." From the perspective of representatives of the private sector in Singapore, U.S. FTAs with Taiwan or Korea "could have a major negative effect on ASEAN" since these countries are major competitors of ASEAN for the U.S. market. A U.S. businessman in Indonesia echoed this statement, observing that "the graduation of Singapore from GSP has stimulated a lot of investment in Indonesia."

Other individuals speculated about the reaction of Japan to a United States-Taiwan FTA. It was noted that trade and investment ties between Taiwan and Japan are quite high. One U.S. Government official speculated that Japan would be "very concerned about being shut out of a United States-Taiwan arrangement." A U.S. businessman in Taiwan, however, suggested that a logical Japanese reaction to a United States-Taiwan FTA would be increased Japanese investment in Taiwan export industries to take advantage of U.S. tariff preferences.

## Alternatives to FTA approach

A few individuals suggested alternatives to both the current approach to United States-Taiwan trade relations and to a bilateral FTA. One individual said that it would be useful for the United States to have a more long-term, comprehensive basis for trade negotiations than at present, similar to the Market-Oriented Sector Selective (MOSS) talks held with Japan in recent years, for example. He said:

The United States doesn't have a long-term perspective in its negotiations. We negotiate on a product-by-product basis, reacting to 301 cases, not by selecting sectors we think are appropriate to increasing long-term objectives of improving trade. Tackling a sector and all barriers has the medium to long-term goal of increasing international competitiveness, and tradeoffs within the sectors are possible.

Another alternative suggested was that the United States and Taiwan establish some sort of dispute settlement mechanism by which trade problems can be discussed in a less confrontational, more predictable manner than at present. Also regarding an alternative to the current approach to trade negotiations, a U.S. businessman in Taiwan said that whether or not there is an FTA, the United States and Taiwan need a comprehensive trade framework that would contain "principles, targets, and dates" for resolving trade issues.



## Chapter 2

### Summary of Views on a United States-Korea FTA

This chapter summarizes the views presented by experts in interviews with Commission staff, in formal submissions to the Commission, or in the Commission's public hearing on the advisability of the United States entering into negotiations for a bilateral FTA with the Republic of Korea.

#### Background

Since 1986, Korea has experienced dramatic and rapid changes in both its political system and economy. Korea achieved double-digit economic growth over the past 3 years and recorded its first trade surplus with the United States in 20 years in 1986. In 1987, Korea's real GNP grew by 12 percent, and predictions ranged from 7 to 10 percent for 1988. Per capita GNP reached \$2,800 in 1987, or about one-half the level of most OECD members. As a result of its economic performance during the 1980's, effective January 1989, Korea was among the four NIEs graduated from the list of developing countries eligible for duty-free treatment of exports under the U.S. Generalized System of Preferences.

In 1988 there was a historic transfer of political power in Korea from authoritarian rule to direct popular election of the president and the emergence of a relatively powerful opposition party in the legislative body. The combination of democratic reforms and strong economic performance raised public expectations and demands for greater participation in the Korean policy making process. Numerous labor union strikes and student demonstrations occurred during 1986-88 as disputes over wage rates, the transfer of political power, and other domestic issues erupted.

Along with Korea's economic success have come increasing pressures from the United States to reduce its trade surplus by restricting exports and allowing greater market access for U.S. products. The United States has urged Korea to adopt macroeconomic reforms and to liberalize its capital and currency markets.

In the past, the U.S. approach to trade with Korea has focused on product-specific issues. The United States has pursued section 301 cases on a wide range of issues, including cigarettes, insurance, beef, wine, and intellectual property protection. In official statements and documents, the Korean government has recognized the inevitability of accepting more international economic responsibilities, reducing its current account surplus, and reforming its agriculture

policies. However, from the United States' perspective, progress has been slow in some key areas, such as currency revaluation and agricultural reform. Since 1986 the United States has attempted to move its trade discussions with Korea away from the specific issue orientation to cover a broader framework.

#### *U.S. trade with Korea*

Korea was the United States' seventh largest trading partner in 1987. The U.S. trade deficit with Korea rose by 119 percent from \$4.3 billion in 1985 to \$9.4 billion in 1987. During January-September 1988, the U.S. bilateral trade deficit was \$7.2 billion compared with \$6.9 billion during the corresponding period for 1987. The deterioration in the U.S. trade balance with Korea during 1985-87 resulted mainly from greater growth in imports than exports. U.S. imports from Korea increased by 69 percent, from \$10.0 billion in 1985 to \$16.9 billion in 1987, while U.S. exports there rose by 32 percent, from \$5.7 billion in 1985 to \$7.5 billion in 1987.

The majority of U.S. trade with Korea consists of manufactured goods (SITC categories 5, 6, 7, and 8). U.S. exports of such goods to Korea increased from \$3.1 billion in 1983 to \$4.3 billion in 1987, or by 41 percent. U.S. imports of manufactured goods from Korea amounted to \$16.4 billion in 1987, representing an increase of 136 percent over those in 1983.

The largest category of U.S. imports from Korea during 1987 was passenger motor vehicles. U.S. imports of passenger motor vehicles from Korea increased dramatically from \$5.8 million in 1985 to \$2.1 billion in 1987. During January-September 1988, imports of passenger motor vehicles totalled \$1.9 billion. The second largest category of U.S. imports from Korea during 1987 was footwear, excluding military or orthopedic. Imports of this category of products rose from \$1.1 billion in 1985 to \$1.7 billion in 1987.

The leading categories of U.S. exports to Korea during 1985-87 were hides, electronic components, seed corn, cotton and soybeans. Aircraft parts and wheat were also large export categories at \$217 million each in 1987. (See appendix D for details of United States-Korea trade).

#### *Trade and Exchange Rates*

During 1983-87, the won weakened against the dollar from 775.75 to 822.57, or by 6 percent. In January 1988, the International Monetary Fund urged the Korean Government to allow the won to appreciate more rapidly against the U.S. dollar in order to reduce its current account surplus. The won appreciated 6 percent against the dollar during the first three quarters of

1988 from 771.46 in the first quarter to 722.97 in the third quarter.<sup>1</sup>

## Overview

The majority of both U.S. and Korean participants believed that to enter into FTA negotiations with Korea would be premature because of the political transition currently occurring in Korea. In addition, rising anti-Americanism, disparities in the structure of the Korean and U.S. economies and the fact that Korea already has a blueprint in place for liberalizing its markets were also cited as factors making an FTA with Korea at this time inappropriate.

Although the majority of those interviewed indicated that "now is not the time for an FTA with Korea," they also indicated that an FTA could be reconsidered once Korea had time to resolve its current domestic political situation and has moved forward on its own liberalization plans. In addition, many suggested that the outlook for a bilateral FTA with Korea or other Pacific Rim countries could hinge on successful implementation of the United States-Canada agreement. If this effort is successful or if the Uruguay Round process stalls and the United States appears to be moving towards other Pacific Rim arrangements, Korea might be more interested in an FTA. Most participants suggested that a regional agreement would be better than a bilateral FTA with the United States, but that multilateral negotiations were preferable to either bilateral or regional arrangements. As one U.S. expert said, "From the Korean perspective, the first choice would be a stronger GATT, secondly a regional FTA, and thirdly, an FTA with the United States." The political drawbacks of an FTA with Korea may outweigh the economic advantages, according to many participants.

A majority of U.S. and Korean officials, businessmen, and academics indicated that the current piecemeal approach for resolving bilateral trade issues has been detrimental to overall United States-Korean relations and that there are many "nasty battles ahead." One Korean academic noted that "the 301 process is out of control." However, some U.S. Government officials and businessmen said that despite the frictions associated with the "squeaky wheel" approach, some progress has been made in areas such as cigarettes, insurance, and computers. Korea has already reduced tariffs on many items

<sup>1</sup> In an October 1988 report to Congress, the U.S. Department of the Treasury said, "Korea is considered to be manipulating its exchange rate. Given Korea's strong underlying economic fundamentals, further exchange rate appreciation within a framework of liberalized trade, exchange, and capital controls is clearly required."

of interest to the United States.<sup>2</sup> In addition, forums such as the U.S.-Korean economic consultations and the U.S.-Korean Trade subgroup talks have also been useful in obtaining tariff reduction and automatic approvals for import licensing on a number of products.

Some participants offered alternative suggestions for handling bilateral trade issues which ranged from improving the current negotiating approach through closer U.S. government/business cooperation to simply not pressing Korea on trade liberalization for awhile. Others suggested approaches that included establishing a dispute settlement mechanism independent of an FTA agreement or broadening the scope of trade talks to include a wider range of trade and economic issues.

## Perceptions About Market Access in Korea

Most U.S. officials, businessmen, and academics indicated that although Korea currently maintains rather high average tariffs (17 to 18 percent) by industrialized country standards, Korea does plan to reduce its tariffs over the next few years. Other major trade barriers for U.S. products cited during interviews and in written submissions are import taxes;<sup>3</sup> bans on certain items, such as beef, poultry, and fresh oranges; import licensing restrictions; local content rules; and other nontariff measures.<sup>4</sup> Cultural and historical factors, such as an almost "xenophobic" export mentality among Korean businesses and the view that "importing is bad," present difficulties for U.S. firms attempting to penetrate the Korean market. One academic said that "Korea is a rare country in which everyone is protectionist and protectionism is related to nationalism and patriotism." However, some U.S. officials and Korean academics predicted that such attitudes will change over time and pointed to the government's educational efforts to promote imports.

Many participants said that Korea is a "developed country with a developing country mentality" and as such uses the protection of

<sup>2</sup> For example, during 1987, tariff rates were reduced by an average of 7 percent on 289 products. Tariff reductions on 128 manufactured and four agricultural items occurred on Jan. 1, 1988. These tariff cuts ranged from 5 to 10 percent.

<sup>3</sup> Some U.S. businessmen and Government officials referred to the negative effect of Korea's import taxes assessed on the dutiable values of the imported goods. For example, in a written statement to the Commission, one U.S. company stated that "fruit juice products containing less than 100% juice are subject to a 40% duty plus a 25% commodity tax. The 65% effective duty rate has inhibited expansion opportunities . . ."

<sup>4</sup> For example, one association for U.S. almond growers stated that 1) high tariff rates (currently 40 percent); 2) requirements that offers made by U.S. sellers to Koreans be notarized; 3) requirements for government approval on all letters of credit; and 4) slow customs procedures have all limited U.S. exports of almonds to Korea.

infant industries argument to justify some of its restrictions. One U.S. Government official said:

Korea is the toughest nut to crack. They are worse than the Japanese. . . . Korea and Taiwan think of themselves as poor underdeveloped countries with big problems. For example, Korea still talks about its foreign debt problem. That shouldn't even be a factor in discussions anymore. . . . The U.S. is their rich brother and Korea is the poor brother. But the advantages flow in their direction.

Conversely, Korean government officials generally, and a few U.S. businessmen, believed that many sectors of the Korean economy are relatively open and others are being liberalized. Tariffs on manufactured goods are scheduled to be reduced to OECD levels in the next 5 years, and by the early 1990's, reportedly the only remaining restrictions will be in the area of a few agricultural items. As one Korean Government economist said:

By the late 1990's Korean agriculture policy will be more open without an FTA. It will be more open than Japanese agriculture will ever be. . . . At the highest levels, the Korean government realizes it has to open up its agriculture.

A large number of U.S. businessmen in Korea and some officials in the United States believed that the problems with market access in Korea are not formal or informal barriers, but instead they are partly due to a lack of U.S. competitiveness and commitment to the Korean market. Most participants felt that unless these problems were addressed, an FTA would not result in increased exports to Korea. Some participants noted that Koreans have a greater propensity to buy American products than do the Japanese, but only if the U.S. product is perceived to be of higher quality. However, these participants said that U.S. goods frequently do not meet quality standards or expectations in terms of suitability for the market, delivery time, or after-sales servicing.

Some U.S. businessmen in Korea noted that there is a distinct lack of marketing efforts by American firms in Korea. Most participants also noted that the Japanese have a much greater competitive advantage in the Korean market because of their geographic proximity and cultural and historical ties. One Korean businessman said:

Japanese firms are closer to Korea than American firms and they follow up with their sales. U.S. firms don't think of Korea as a major market and don't make a big effort to sell in Korea. . . . Korea has to beg from the United States. We [Korean firms] have to go to the United

States to buy from American companies. . . . the Japanese we may want to buy from are right here in Korea. They make it much easier for us to buy from them than do American companies.

### **Perceptions on the Timing of an FTA**

A majority of U.S. and Korean Government and business officials said it would be "premature" to raise the issue of an FTA with Korea right now for both economic and political reasons. A U.S. official said:

The Koreans might be interested in an FTA if we were concluding FTAs with others, but the timing right now is premature. The Koreans are going through a period of political transition and self-definition right now.

One Korean Government official said that the Korean economy currently has "weak points" and that Korea would have to do a lot of economic and structural adjustment before it is ready for an FTA with the United States.

Some Korean Government officials seemed to be "caught off guard" by the Commission study and indicated that Korea had not really given the FTA idea much thought. One Korean industry association official said, "If the United States urges Korea to negotiate an FTA, Korea will be in big trouble. Right now there is no government position on an FTA." A majority of Koreans interviewed echoed the view of one businessman who said that "With Korea's changes in its exchange rate and market liberalization, Korea hopes for more patience from the United States before it tries to make regional blocs." Another theme frequently heard in Korea was, "Come back in 10 years, after we make our adjustments." Many U.S. and Korean participants suggested that a lot of study would have to be done before an FTA could be considered.

### **Perceptions on the Current U.S. Negotiating Approach**

Many participants offered comments about the current U.S. negotiating approach toward Korea as a means of explaining, supplementing or supporting their views on the advisability of FTA negotiations. The majority (including U.S. and Korean Government officials, businessmen, and academics) characterized the current U.S. approach with one or more of the following descriptions: lacking priorities, unpredictable, unilateral, and politically insensitive. However, many participants also concluded that the United States has succeeded in achieving increased market access despite these drawbacks. A number of U.S. officials and businessmen, in particular, spoke in favor of the current

approach, including the use of section 301, and claimed that this was the only effective means of dealing with Korea.

#### *The current approach lacks priorities*

A majority of participants both in the United States and Korea indicated that the current issue-by-issue approach to trade negotiations has raised bilateral tensions over trade. However, most of these persons did not believe that an FTA would be any less contentious than the current approach or would eliminate the need to address trade problems on an issue-by-issue basis.

Many negotiators and businessmen in the United States and Korea cited cigarettes, photo albums, wine, and beef as examples of "politically sensitive, but economically meaningless" issues that the United States has pursued in bilateral negotiations and the 301 process with Korea. A Korean government official said, "The U.S. concentrates its negotiating efforts on markets that are trivial in Korea [in economic terms]. For example, wine is politically sensitive in the United States and Korea, but economically insignificant in Korea's trade." One U.S. expert said, "We've mostly argued about trivial issues. . . . Beating the Koreans on cigarettes was the dumbest."

The lack of prioritization in trade policy with Korea was referenced by one U.S. businessman when he stated, "Our trade policy has followed the squeaky wheel approach. We need to prioritize trade issues. The trade bill was supposed to help do this." Korean businessmen claimed that the lack of prioritization contributes to an ambiguous relationship because Koreans are uncertain why particular issues are targeted for action by the United States.

#### *The current approach is inconsistent*

Several Korean officials alluded to the "contradictory and unpredictable" nature of current U.S. trade policy and also questioned how serious the United States is about negotiating FTAs in the Pacific region. One Korean official said:

The United States sends mixed signals on trade. On the one hand, there is the Omnibus Trade Bill. On the other hand, there is talk in the United States about FTAs. The trade bill has protectionist elements; the FTA idea promotes free trade. It seems like the idea of FTAs is in high fashion in the United States right now and I don't know if that fashion could last long.

Another Korean businessman said, "With or without an FTA, predictability, a schedule of trade policy changes would be useful. Uncertainty exists now; this could mean serious trouble."

The majority of Korean participants viewed the current U.S. negotiating approach as unilateral and unfair. They indicated that the United States appears to constantly demand concessions and policy changes, but offers nothing in return. These participants believed that this would not change under an FTA. Conversely, some other Koreans suggested that their country is not ready to be treated as an "equal" in economic relations. One Korean businessman commented:

Korea is not in a position to deal with the United States at the same level. The trade surplus is a new trend for the Korean people. . . . Korea is willing to change, but not as fast as the United States would like. Korea's main concern is that the U.S. Government treats Korea just like Japan, but Korea can't compete like Japan in terms of trade.

#### *The current approach has been successful and 301 works*

From the viewpoint of several U.S. businessmen and Government officials, the United States has been successful under the current approach in opening the Korean market even though it has caused frictions. Many of these participants claimed that the "carrot and stick" approach is the only effective means for dealing with Korea. One U.S. businessman in Korea noted, "The threat of 301 cases makes Korea take notice and take actions." Another U.S. businessman said he would advise the Government to use section 301 rather than enter into FTA negotiations:

If you don't do that you won't accomplish anything. . . . There are many ways to retaliate. The U.S. should do it in a way that is meaningful and hurts. We retaliated on photo albums. It did not mean zip. The Koreans were livid about us picking on the little guys. We should retaliate against big companies instead.

A couple of participants felt that as the world's largest market, the United States' ultimate leverage in negotiating trade issues is to restrict access or to shut out foreign countries. One U.S. businessman said, "Our leverage is our market. Korea respects power. Let's not throw away our two-by-four's [section 301]. We need to have consistent pressure, shrewdly applied in areas where we have the most at stake."

### **Perceptions About Negotiating Resources**

There were mixed views on whether the United States has the negotiating resources to conduct bilateral FTAs in the Pacific generally or with Korea in particular. Some participants believed that U.S. negotiating resources are



already being strained by the Uruguay Round and that FTA negotiations would further overload the system. However, one U.S. official indicated that although he would have to switch employees from other assignments to work full-time on an FTA and it would place a stress on his agency's resources, it would be possible to prepare for FTA negotiations. Several participants noted that although the United States has enough negotiators to begin FTA talks, the real problem is continuity. One U.S. businessman said:

Continuity is a bigger issue than resources because a substantial part of any success of negotiations depends on personal relationships built up with the opposite negotiator. . . . These personal relationships are only built up over time. We need a professional cadre of trade negotiators with the prestige and income to stay on the job, and not go off to the private sector to make more money lobbying for the other side.

### **Advantages of the FTA Approach With Korea**

The following section summarizes the major advantages of a United States-Korea FTA as described by participants during the course of this study. In addition to information obtained during interviews, the Commission received several formal submissions citing some benefits to a United States-Korea FTA.

#### *Would improve the negotiating atmosphere*

A few U.S. Government officials, Korean businessmen, and academics felt that FTA negotiations might allow trade conflicts to be settled in a less confrontational manner than the current method of resolving bilateral disputes. By setting up a schedule for liberalizing specific product categories under an FTA, some participants suggested that there would be fewer and less serious disputes. As one participant said, "The item-by-item approach is not good. It would be easier to handle trade issues with an FTA than piecemeal."

Only a few participants suggested that FTA negotiations could help alleviate anti-American feelings in Korea. However, one U.S. Government official said that an FTA might help alleviate resentment towards the United States because the negotiations would be mutual rather than unilateral and the United States would also be forced to make concessions.

#### *Would provide a framework for negotiations*

Moreover, a bilateral dispute settlement panel created by the FTA, was viewed by many participants as a positive development for improving trade relations. According to one U.S. expert, a dispute settlement mechanism would

reduce the visibility of trade conflict and would commit both countries to free-trade rules. Neither country would be able to resort to protectionism without violating the spirit of the agreement. A dispute settlement mechanism was viewed as a tool to counter domestic demands for protectionism.

#### *Would increase market access in Korea*

Most U.S. and Korean Government officials who supported the idea of an FTA with Korea believed there would be more for the United States to gain than lose from the agreement in economic terms. With the exception of certain sectors, such as textiles and steel, the U.S. economy was perceived as being more open than the Korean economy. As such, some participants thought imports from Korea would not increase much, even in such labor-intensive sectors as textiles, in which Korea has lost some of its competitive advantage to other developing countries.

Some participants suggested the United States could make gains in terms of increased market access in the areas of agriculture, including beef, fruit, and processed foods, but cautioned that the gains might not be significant. One U.S. agriculture official said:

The areas where we could do better in these countries [Korea and Taiwan] are higher value products, such as fruits and nuts, and meat products, such as poultry and beef. Access is now good for bulk commodities, but not on these others. If these countries really had free trade they couldn't compete with us in certain agriculture products. We wouldn't be giving up much of anything in agriculture to the other countries, but we wouldn't gain a lot.

Other areas mentioned in which the United States could be expected to make gains were services and intellectual property rights. Some participants suggested that an FTA would be beneficial to the United States as Korea's economy continues to expand. One U.S. negotiator said:

Korea has a large market which [is] worth penetrating. The standard of living is increasing. As this continues, Koreans will be better able to purchase consumer goods, hopefully U.S. exports. It should become a market for high-quality food and agricultural exports as the standard of living increases. Korea would also be a good partner for collaboration to penetrate other markets in the region. . . . So we would probably benefit from an FTA with Korea. The question is, is Korea willing to put agriculture and services on the table to get what they want, i.e., predictability of access to the U.S. market?

*Would ensure that liberalization plans are carried out*

A minority of participants suggested that FTA negotiations could help accelerate Korean liberalization measures already scheduled to occur during the next few years. A few Korean participants said that a United States-Korea FTA could support the government's own goals of opening up the economy. An FTA might be used to "sell" liberalization plans to weaker sectors of the economy that might otherwise be resistant to such moves.

### **Disadvantages of the FTA Approach With Korea**

The following section summarizes the major disadvantages of a United States-Korea FTA as described by participants in the study. In addition to information obtained from interviews, the Commission received a number of formal submissions opposed to a United States-Korea FTA.

*Would adversely affect the political relationship*

Some participants noted that in Korea, bilateral economic issues have a greater spillover into political areas than in many other countries because of the strong U.S. military presence there. A Korean academic with close ties to the government noted:

The United States is losing its footing in Korea. This is starting with the military process. Many want the military here, but others are starting to want it out. Market opening efforts cause problems, like the burning of the USIS office. This is a new type of problem. Korea has been the most friendly country in the world to the United States. Over the last 3 to 4 years, a change of mood has totally taken place regarding the perception of the U.S. . . . The United States picks on everything that's different in the economy of Korea from the U.S. economy and calls it a barrier. They keep bugging Korea all the time about these so-called barriers. This leads one to think that someday the United States will lose its footing in Korea. This will lead to the end of the United States in Asia. Maybe the United States doesn't care too much about such predictions, as it doesn't make much of these warnings.

According to virtually all Korean Government officials, businessmen, and academics, and some U.S. experts interviewed, an FTA approach could be a risky political strategy for the United States at the present time because of domestic political changes taking place in Korea. However, two U.S. Government officials concurred with former Secretary of State Shultz's

view that our trade interests with Korea are too important to ignore or concede simply because of anti-American sentiment.

*Could perpetuate or increase anti-American sentiment*

Many government and academic officials warned that the United States could run a major risk of setting off more anti-American sentiment and protests in Korea if FTA negotiations were proposed. Trade issues are given high visibility in the Korean press and the population is constantly informed of bilateral trade frictions. One private sector U.S. expert said, "With further trade pressure from the United States we can expect anti-Americanism and political radicalization to grow." The majority of those interviewed believed that growing anti-Americanism sentiment combined with the high-profile treatment by the press could be a recipe for misinterpretation followed by political opposition, if FTA negotiations were proposed.

According to a number of Korean and U.S. participants in Seoul, during the past 3 or 4 years there has been a marked shift in attitude among the Korean people towards an anti-American bias as the country has become increasingly independent in its political outlook, more resentful of its past dependence on the United States, and anxious to join the "mainstream of the global community." The comments of one Korean Government economist reflected the feelings of numerous participants in Korea:

There is a sense of being reborn as an independent country in Korea these days. Korea so helplessly depended on the United States for so many years, it came to resent this and to resent itself. The USA reminds us of this past. This helps explain anti-Americanism in Korea. We feel as if we've been excluded from half the world for a long time. Now we have Bolshoi Ballet and Ping Pong players come to visit. We'd like to enjoy the sense of being welcome in the global community on our own for a while.

One high-level U.S. official said, ". . . given the cultural differences and the current political situation in Korea, beginning FTA negotiations would cause a revolution in Korea. Koreans feel they are finally controlling their destiny and no one should interfere."

However, a few participants suggested that the wave of anti-United States sentiment depicted in the Korean press is not as broad-based as it is made to appear. One U.S. official even suggested that "final exams" for the students would help calm down the situation. A few participants who believed that demonstrations have been sparked by unilateral trade actions of the United States indicated that an FTA involving mutual

concessions might be easier to sell domestically in Korea.

Regardless of U.S. intentions in entering into FTA negotiations, the majority of Korean participants indicated that an FTA initiative would be viewed by the Korean Government, and Korean people, as "just one more [example of] the United States telling Korea what to do." Even if the United States attempted to portray an FTA initiative as a positive and mutual approach to bilateral trade problems, they said, the overture would still be interpreted in Korea as another instance in which Korea is treated "like an adolescent or child." A U.S. Government official shared this view in noting that the United States has spent the last 5 years trying to overcome the "big brother-little brother" perception of its relationship with Korea and that pushing for an FTA could negate any progress that has been made to improve the United States' image. According to several Korean Government officials and some U.S. businessmen, Korea is at an important juncture in defining its political identity at home and abroad. One element of this process is a desire amongst the government and people to become more independent of the United States in both its political and economic policies. One Korean businessman said, "An FTA would be seen from an absolutely negative viewpoint by the Korean government if it were seen as a U.S. initiative." A Korean academic said:

Korea always is suspicious with the mention of any FTA, especially when it is mentioned by foreigners. . . . The executive branch concedes too much of too many things to the United States. People are tired of hearing anything from the United States.

A few Koreans conceded that if FTA talks were approached delicately and Korea were "treated as an equal," it might be possible to achieve the necessary domestic political support.

#### *Would not improve the negotiating atmosphere*

A few participants noted that although the current negotiating strategy towards Korea has worked, it may not be as successful in the future given the increasing resistance to U.S. pressures. One U.S. academic said:

. . . U.S. pressure has at times helped in the past, but progressively less so over time. . . . Because of Korea's cultural and emotional makeup, the United States can only push so far before Korea reaches its breaking point and seeks to distance itself from the United States.

However, most participants said that an FTA would not be the end of trade disputes between the two countries even with a dispute settlement

mechanism. Some participants pointed out that under the United States-Canada agreement, the United States can still take restrictive actions and that Korea could expect similar treatment under a United States-Korea agreement.

Many participants in both the United States and Korea indicated that an FTA is not a "magic wand" that will "wave away trade tensions." Even under an FTA, it was expected that trade issues would still be given a great deal of attention both in the Korean press and within the U.S. Government. A number of persons who suggested that an FTA could even result in a higher profile for such sensitive areas as agriculture, textiles, steel, or footwear, pointed to the high level of attention and heightened tensions associated with the United States-Canada FTA. They predicted that such problems would be magnified during FTA discussions with Korea.

Some U.S. businessmen and Korean participants noted that the fragmented nature of the U.S. political system and trade-policy making process almost guarantees that small issues can be brought to the attention of negotiators at any time. They believed that this system would not change under an FTA and there would not be an improvement in prioritization of trade issues.

#### *Could delay liberalization in Korea*

Several U.S. businessmen suggested that Korea might enter into prolonged FTA negotiations in order to delay liberalization in certain areas. One businessman said that the Koreans "would like nothing better than a liberalization schedule that stretched to eternity." However, a U.S. Government official said that indeed the "Koreans could string us along saying we need more time, but the same thing applies to the United States in textiles also." Another U.S. Government official felt that Korea could use FTA negotiations to avoid taking liberalization actions in specific sectors: "The Koreans would love to sit down and talk about trade liberalization in general terms and put off making the [specific] changes being sought."

#### *Would not necessarily improve U.S. trade*

Most participants said that unless an FTA addressed barriers other than formal tariffs and quotas, there would be little increase in market access for the United States and little impact on the trade deficit. Yet many doubted that Korea would be willing to make concessions in areas the United States would be most interested in, such as agriculture, services, and intellectual property rights protection.

Many U.S. Government officials and businessmen indicated that export gains would only be made if an FTA covered such items as Korean import licensing restrictions, local content rules, and distribution channels. One U.S. businessman in Korea said that Korean barriers are "endemic"

and that there is a "systemic mindset" among Koreans that discriminates against imports. However, according to a number of participants this attitude among both government and businesses is changing slowly.

Many participants suggested that even if an FTA with Korea included subsidies, intellectual property rights protection, investment, services, etc., other countries, such as Japan, would be more likely to benefit. These participants noted that U.S. firms would not be able to increase their market shares in Korea even under an FTA because of their lack of competitiveness. One academic said:

The United States is seen as the least efficient of the industrial economies. Even if the U.S. trade deficit with the world falls, the bilateral deficit with Korea will still be there. The United States is inefficient in competing with Japan. If Korea buys more imports from anyone, they will buy them from Japan. . . . If Korea must have an FTA it should do it with Japan; the trade diversion effects will be less than if it would do one with the United States.

#### *Would not lead to free trade in all sectors*

Several participants suggested that an FTA would not necessarily lead to free trade in all sectors because both partners would request exceptions. "As we negotiated FTAs, we'd find our objectives whittled away by special interests," said one U.S. official. Some participants pointed out that the barriers remaining in areas such as agriculture are such politically sensitive issues that they would be hard to address under any kind of negotiation, either multilateral or bilateral. As one participant said:

Further liberalizing is going to be real hard, no matter what the forum. . . . It will be equally tough to deal with these barriers in any forum. We are down to the hardcore trade issues everywhere. There will be no advantage to deal with them either in a multilateral or bilateral setting.

Moreover, a majority of U.S. participants speculated that Korea would want to see U.S. restrictions on textiles, footwear, and steel removed but doubted that the United States would be willing to give them up under FTA negotiations.

In addition, several Korean government officials pointed out that Korea is the third largest market for U.S. agricultural products and there isn't much room to expand U.S. agricultural exports even under an FTA. A U.S. agriculture official said that the United States would be at a disadvantage under an FTA with regard to certain

agriculture issues such as labeling and health requirements. It was also noted that the small size of the Korean market would not make it more economical for U.S. firms to adjust their production to fit the standards for the Korean market regardless of whether or not there is an FTA.

#### *Would be difficult to implement*

Many Korean and U.S. officials questioned the feasibility of an FTA with Korea because the two economies are so different. Many participants in both the United States and Korea pointed out that the United States-Canada FTA situation is unique because the two countries are in close geographic proximity and have similar economic structures, legal systems, and cultures. These factors were viewed by many as a prerequisite for a successful FTA. Thus, a number of participants, in noting that the United States and Korea do not share such common economic and political characteristics, believed a United States-Korea FTA would not be feasible. One Korean businessman pointed out that an FTA with the United States would require considerable structural adjustment on Korea's part.

A few participants suggested that the Korean market is simply too small for FTA consideration. One Korean businessman commented, "We are the size of Virginia with a GNP the size of suburban Los Angeles." Accordingly, some Korean Government officials and businesses worried that the Korean economy would be subordinated to the United States under an FTA. Said one, "Korea is still a small potato compared with the United States' economic power." However, some Koreans suggested that an FTA might be possible if it were phased in over a period of time in order to give certain sectors of the economy time to adjust to market-opening measures.

#### *Is not politically feasible at the present time*

The majority of U.S. and Korean government officials did not believe that a political consensus could be achieved in Korea in favor of an FTA. Participants said the politically powerful agricultural constituency in Korea would oppose any FTA agreement. As one Korean noted:

In agriculture, the U.S. would be seen as victimizing an already injured area. There is sympathy with the farmers, who are seen as victims of past policies. This would be even more of a source of anti-Americanism than at present, even if people realize U.S. actions are correct and legal.

According to one Korean official, "A closer economic relationship with the United States is not salable in Korea." Said another, "It would be political suicide for the Korean Government"

and viewed as a "grand sellout of the government to the United States." However, these same government officials added that if an agreement were "forced on them by the United States," they would "swallow it." Some Korean officials tempered their opposition to FTA talks by saying that the Government's reaction to a proposal from the United States would depend on how it was presented. If an FTA is presented as an option rather than a demand to Korea, the response from the Korean government might be more positive.

A submission from a U.S. research institute stated:

While from an economic standpoint the Republic of Korea is a good candidate for an FTA, economic misunderstanding by opposition political parties make an FTA difficult at this time. The United States should let the government in Seoul know of American interest in an FTA but should not push the government at this point.

Even if an agreement were signed, one U.S. businessman in Korea said that he wouldn't trust the Korean officials to implement it and predicted that if it [adjustment under an FTA] starts to pinch or hurt, the Koreans would "take unilateral action or renegotiate the agreement to fix the problem."

#### *Alternative approaches to a United States-Korea FTA*

Some participants (including both those who opposed and those who favored the current approach) offered alternative suggestions for handling United States-Korean trade relations. One United States businessman suggested that the U.S. just needs to "fine tune" its current approach to trade with Korea and attempt to improve the ability of U.S. companies to compete with foreign firms by focusing on more than just Korea's import barriers. He said that Government and business should "sit down and think strategically about the next 2 to 4 years" and put more effort into "a strategic response to

competitive pressures" by focusing on export financing, investment flows, and the use of government financing.

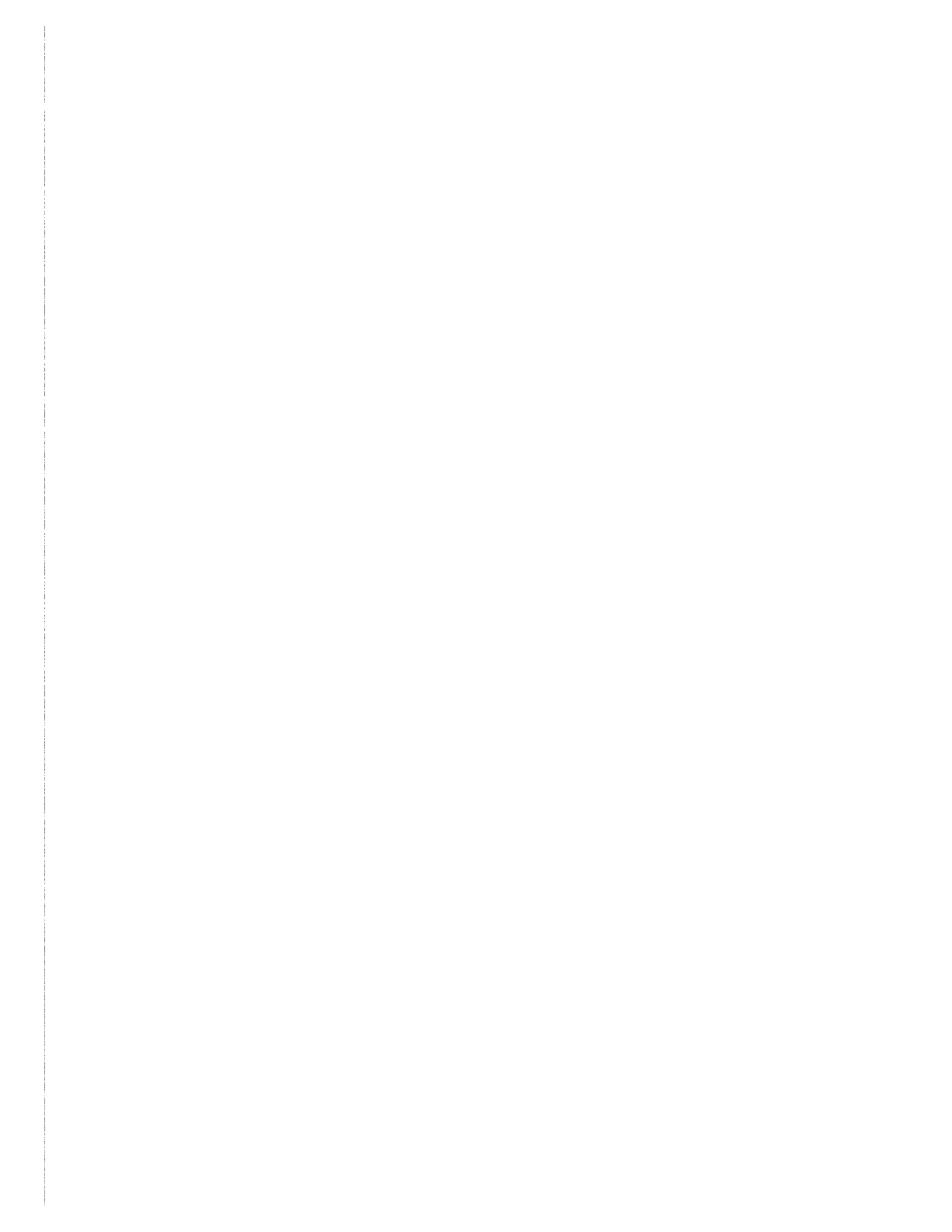
Some Korean businessmen and officials felt that a dispute settlement mechanism, even without an FTA, might be helpful in improving trade relations. They indicated that a binational forum would be attractive to Korea because it would remove the perception that the United States unilaterally makes decisions in certain trade disputes.

A Korean businessman suggested that "MOSS-like talks" with Korea might be more useful than FTA negotiations. This would involve selecting specific sectors for bilateral negotiations based on potential export sales and in consultation with U.S. industry. In the view of a few participants, the U.S.-Japanese MOSS talks were successful in gaining market access in several sectors of interest to the United States and the same approach might work with Korea.

Several participants, particularly U.S. Government officials, said that they have been attempting to change the focus of their discussions with Korea and move away from specific issues to a broader structural dialogue. These officials spoke optimistically about the prospects for widening the role of these talks to include a wider range of trade issues and suggested that this approach is preferable to FTA discussions. However, one Korean government official noted that the Korean government is concerned that the true U.S. intentions are to use the talks as a means of forcing Korea to explain its long-term industrial structure and political direction and said that:

Korea is not ready to have structural dialogue talks with the United States on sensitive issues of economic sovereignty with Korea having to explain the political direction.

Moreover, a few Korean participants suggested that it is premature for Korea to consider an FTA with the United States at this time because, in their view, the current direction of U.S. trade policy is uncertain.



## Chapter 3

### Summary of Views on a United States-ASEAN FTA

This chapter summarizes the views of persons interviewed by Commission staff, making formal submissions to the Commission, or participating in the Commission's hearing, on the possible advantages and disadvantages of entering into FTA negotiations with the Association of Southeast Asian Nations (ASEAN).

#### Background

##### *The ASEAN institutional framework*

In 1967, a time of political turmoil in Asia, ASEAN was established by Indonesia, Malaysia, the Philippines, Singapore, and Thailand. Brunei Darussalam, formerly a British protectorate, joined the organization in 1984, shortly after receiving its independence. The explicit objective of ASEAN was to foster economic, social, and cultural cooperation, but a desire to reduce regional tensions during that period and a sense of vulnerability to aggressive Communist forces in the 1970's pushed diplomacy to the forefront of the organization's agenda. The diversity in economic interests and in levels of development has limited the growth of cooperative economic activities. In the more than 20 years of ASEAN's existence, economic cooperation among its members has made little headway; ASEAN's most prominent successes have been as a political bloc, with regional security against Communism as its main priority.

In terms of institutional structure, the preference within ASEAN has been for a loose framework characterized by negotiations at all levels.<sup>1</sup> As Alagappa notes in his text, ASEAN's loose institutional framework, although perhaps ambiguous and inefficient, "provides opportunities for 'face-saving,' which is considered vital for ASEAN solidarity and cohesion." Thus, two important principles that govern ASEAN operations are the principle of consensus-building and the principle of rotation. Consensus-building is a lengthy and tedious process but is viewed as important to ensure that the national interests of all member states are taken into consideration, thereby ensuring ASEAN cohesion. However, the notion of "six minus x" has replaced strict consensus as the working principle in ASEAN's economic cooperation schemes. This means that although x number of members may disagree on a plan, the consenting countries can proceed

<sup>1</sup> The source for most of the material on ASEAN institutions is Muthiah Alagappa, "Asean institutional framework and modus operandi: recommendations for change," in *ASEAN at the Crossroads*, the Institute of Strategic and International Studies, Malaysia, 1987, pp. 183-226.

with the new program or arrangement. It would therefore be possible for the United States to enter into FTA negotiations with one or more of the ASEAN members.

The ASEAN members have consciously avoided creation of a strong Secretariat and favor a decentralized ASEAN machinery (see fig. 1). Under the principle of rotation, the chairmanship, location, and secretariat staff for nearly all key ASEAN institutions are rotated among the member states. The purpose is to ensure active participation by a broad segment of the government and people of all member states and to ensure that power, authority, and benefits are shared equally among the member countries. The rotation system, by relying heavily on the national government machinery, has hampered the development of a strong and efficient central ASEAN Secretariat.

The highest decision making body for economic cooperation in ASEAN is the ASEAN Economic Ministers Meeting (AEMM). This group meets biannually and is responsible for formulating recommendations for strengthening ASEAN economic cooperation; reviewing the implementation of agreed-upon ASEAN programs and projects on economic cooperation; exchanging views and consultation on national development plans and policies as a step toward harmonizing regional development; and performing such other relevant functions as agreed upon by the member governments.

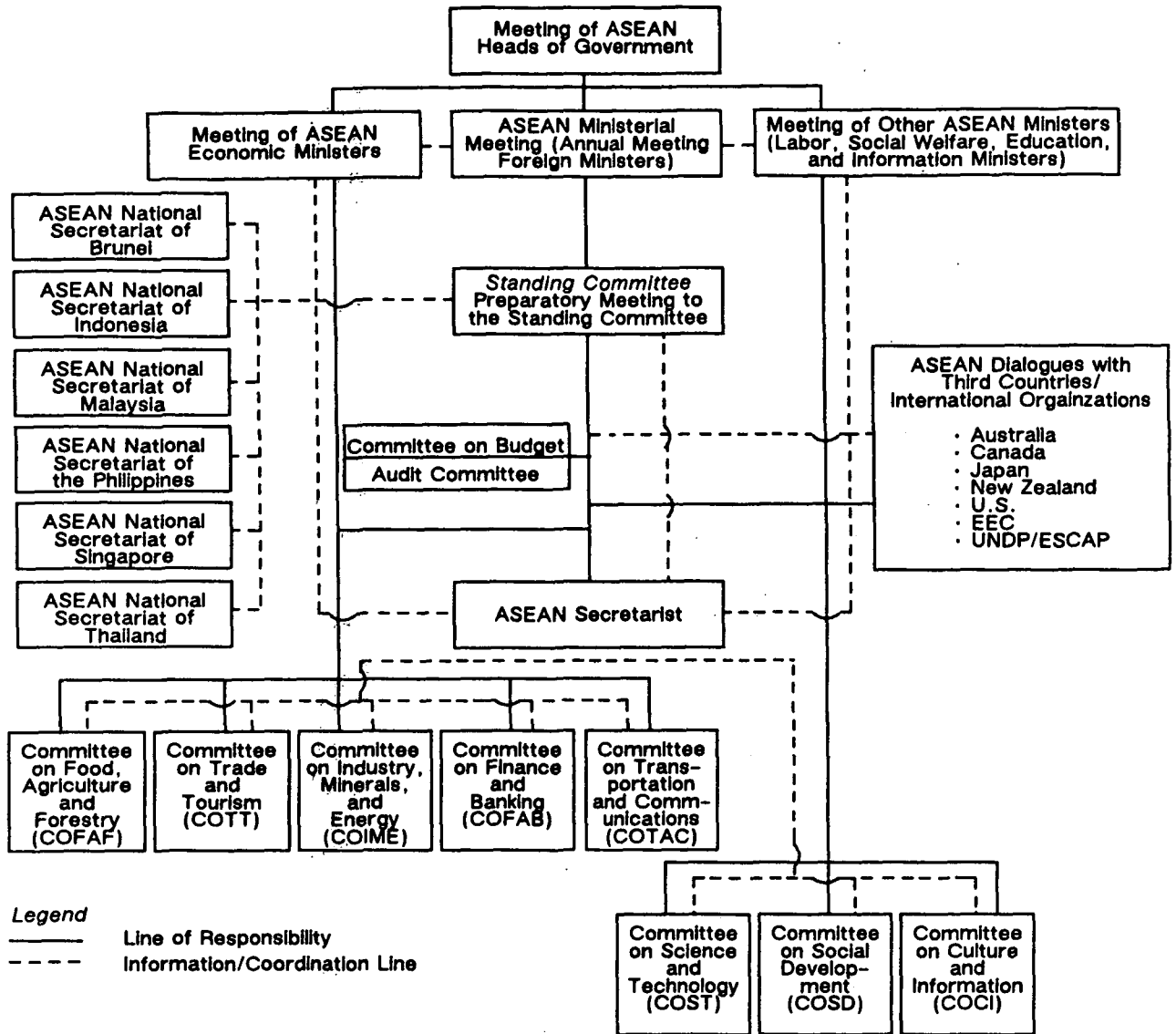
ASEAN does not have collective representation in any international economic or political forums but, when necessary, coordination on international issues is achieved through the relevant ASEAN committee. Decisionmaking, negotiations, and the general conduct of diplomacy for ASEAN are based on the principle of consensus.

##### *Economic and Trade Data*

In 1987, the ASEAN countries collectively were the United States' seventh largest trading partner. During that year, total trade turnover between the United States and ASEAN was \$26.5 billion. Principal U.S. exports to ASEAN are capital goods, transportation equipment, chemicals, and agricultural products. The United States imports 90 percent of its natural rubber, 28 percent of its tin, as well as petroleum, sugar, coconut oil, palm oil, textiles, and electronics products and components from the region. (See appendix D for leading items of trade).

Singapore is the only ASEAN member that has a predominantly industrial and commercial economy. The cultivation and processing of primary agricultural products are important industries in the other countries. The socio-economic indicators displayed in table 1

**Figure 1**  
**Organizational Structure of ASEAN**



Source: State Department Background Notes.

show the diversity among the ASEAN members. For example, annual per capita GNP in 1985 ranged from less than \$500 in Indonesia to over \$6,000 in Singapore. Oil-rich Brunei had a per capita GNP of over \$16,000.

**ASEAN-U.S. Initiative**

ASEAN and the United States have pursued an economic dialogue for over a decade. A recent outgrowth of that dialogue is the ASEAN-U.S. Initiative (AUI), a comprehensive joint economic study on ways to enhance United States-ASEAN trade, investment, and other economic relations. The study, initiated in July 1988, is being conducted by nongovernment consultants and is scheduled for completion in

early 1989. According to both U.S. and ASEAN officials, the AUI is a useful exploratory process that will help determine the direction of future U.S. policy with ASEAN, and could possibly lead to a framework for closer economic relations. The study will examine a number of alternatives for improving United States-ASEAN trade, including an FTA agreement. Although the United States and ASEAN countries support the study group's efforts, no party is under obligation to accept the report's recommendations.

In a separate development, on August 8, 1988, the United States and ASEAN signed Memorandum of Understanding for the creation of an automated data exchange (ADE) system linking the two parties. Accordingly, the United



Table 1

ASEAN socioeconomic indicators: Area, population, per capita GNP, GNP, real GDP growth, inflation, by countries, 1985

Country	Area	Popu- lation <sup>1</sup>	Per Capita GNP, 1985	GNP, 1985	Real GDP growth <sup>2</sup>	Inflation <sup>3</sup>
	1,000 sq km	Millions	U.S. currency	Billion U.S. dollars	Percent	Percent
Brunei .....	5.8	0.237	\$16,065	3.8	1.2 <sup>(4)</sup>	5.8 <sup>(5)</sup>
Indonesia .....	1,919	164.4 <sup>(6)</sup>	482	79.0	6.8	4.4
Malaysia .....	330	15.7	1,901	29.8	7.4	0.5
Philippines .....	300	54.6	598	32.6	4.1	5.7
Singapore .....	.6	2.6	6,223	15.9	8.1	0.2
Thailand .....	514	51.3	725	37.2	6.5	2.4

<sup>1</sup> Mid-1985.

<sup>2</sup> Average annual rate, 1971-85.

<sup>3</sup> CPI, 1985.

<sup>4</sup> 1983-85 data.

<sup>5</sup> 1984 data.

<sup>6</sup> Estimate.

Source: State Department Background Notes, "ASEAN," April 1986.

States will provide ASEAN members with the necessary technical assistance so that each can have access to the ADE. The ADE is to consist of a merged database containing information on foreign trade and tariffs.

### Overview

The majority of U.S. and foreign participants discussing the advisability of a United States-ASEAN FTA did not think such an agreement was workable. Many thought the idea was premature and that "jumping into an FTA" could well be too drastic and sudden a step; they urged that the United States proceed cautiously and pursue its liberalization efforts through the GATT. As one participant said, "Weighing the advisability of an FTA on purely economic grounds does not make much sense. Too many important exogenous factors need to be considered; political, cultural, and security." Other U.S. participants, in particular certain industry association representatives and businessmen, were not receptive to the concept of an FTA with ASEAN because they were not convinced the United States would benefit economically or politically from an FTA with the group. A submission from a manufacturing workers' union that typifies these responses made the following observation:

The record of the United States in negotiating contentious trade issues with [the subject countries], and the failure of many of these countries to live up to their bilateral commitments with the United States to end export subsidy practices do not bode well for the negotiation of an FTA in any meaningful sense of the term. These countries maintain excessively high tariff and innumerable non-tariff barriers to trade that heavily protect their domestic industries. Furthermore, work-

ers in these countries are very often subject to substandard conditions. In the case of Malaysia there have been serious allegations of workers' and human rights violations. None of these factors would indicate that Pacific Rim countries are particularly good candidates for FTAs. Evidence suggests otherwise. These countries are not even close to changing their way of doing business or making the kinds of commitments necessary to enter into an FTA. U.S. government officials should abandon this foolish notion, and address real trade problems: the mammoth trade deficit and deteriorating conditions in basic U.S. industries.

Several other participants said that a United States-ASEAN FTA could become an irritant; something the United States would continually struggle over and change to accommodate the diversity of the ASEAN members.

Others said that as with all negotiated agreements, objectives would be whittled away by special interests and the remaining accord would not be a true FTA.

Most of the participants who supported the notion of a United States-ASEAN FTA did so provisionally. They felt that the United States should continue its liberalization efforts through bilateral negotiations currently underway, multilateral efforts in the context of the Uruguay Round, and through use of the new "super" 301 authority before taking serious steps toward the FTA option. A few participants thought that it would not be productive to pursue an FTA until outstanding trade issues have been resolved.

Others saw a number of advantages and benefits to be derived from an agreement. Viewing the current approach as ad hoc and unprioritized, some businessmen felt that an FTA would establish a forum to address a broad range

of issues and would eliminate the need for the often contentious issue-by-issue approach. Others felt that the educational process from building the framework for an FTA—whether or not the agreement is implemented—could be invaluable. A number of persons said that if the Uruguay Round is not successful in increasing trade liberalization, then the FTA approach is ideal to pursue free-trade objectives. A few participants said that the United States might not gain much economically from an FTA with ASEAN but would gain a lot politically in terms of improved relations, particularly now that the Soviet Union is becoming skillful and adaptive in Asia, whereas the image of the United States is declining.

### Perceptions About the Diversity of ASEAN Members

Several participants noted that because the United States has such a long negotiating history with these countries, cultural differences are not significant considerations when discussing the advisability of a United States-ASEAN FTA. However, a number of people believed that the diversity in the levels of economic development between the United States and ASEAN could present problems for an FTA. Some pointed out that the economic development of the ASEAN countries is not suited to such an arrangement. Said one participant, "An FTA does not make sense for countries such as Indonesia and Thailand. They need to protect infant industries from the very competition that would result from an FTA." According to another participant, "There can be no FTA. ASEAN will require preferences for some time. They are very underdeveloped in many aspects of their operations." Several participants stated that similar levels of development and similar legal systems between potential FTA partners are necessary before an FTA will work and that this does not currently apply to the United States and the ASEAN region. As noted by one participant:

An FTA is unlikely because the philosophical and economic differences between the United States and many of [these] countries are vast. Even with Canada many agricultural issues could not be resolved, and we are light-years closer to Canada than the Pacific Rim.

To most participants, more significant than United States-ASEAN differences are the differences among the ASEAN members themselves. In most interviews regarding an FTA with ASEAN, the observation was made that the countries ASEAN comprises are so diverse in terms of size, cultures, levels of development, economic structures, and regulatory and political

systems (e.g., Brunei Darussalam is a sultanate), that it would be very difficult for the United States to negotiate an FTA with ASEAN as a bloc. Said one participant, "The AUI is a way to get basic data and then lay the groundwork for future possibilities. But there is no real basis with which to negotiate with the group." In a submission to the Commission it was noted that:

Asia is much too vast and diverse an area of the world to be dealt with as a homogeneous trading unit. Even regional groupings such as ASEAN have so many competing and peculiar interests that it would not be practical to consider the short- or medium-term conclusion of meaningful negotiations on the regional elimination of mutual trade barriers and frictions.

ASEAN attitudes about trade are also perceived as very diverse. Most participants felt that the ASEAN members are not united in their views on the concept of a free-trade area with the United States. Singapore, the most outward-looking and developed ASEAN member, was viewed as the most enthusiastic about an FTA, and Indonesia, more domestically oriented, the least developed, and least flexible ASEAN economy, was represented as the most disinclined. Comments made in interviews both in the United States and abroad suggested that the positions of the other members lie between the extreme Singapore and Indonesia viewpoints. As one U.S. Government official said:

Singapore and Indonesia are the extremes; Malaysia is a step ahead of Indonesia in terms of favoring more negotiated trade arrangements. Thailand is perhaps three or four steps ahead of Malaysia. Brunei doesn't have a position, and the Philippines always prefers to deal with the United States bilaterally.

If there is to be a United States-ASEAN agreement, participants generally visualized an "umbrella" agreement signed by all, with individual country negotiations taking place later on the specifics of each bilateral agreement.<sup>1</sup> The "umbrella" would provide the framework of the agreement, including rules of origin, dispute settlement, a consultative mechanism, etc. In recognition of the varying levels of development among the members, each ASEAN member would negotiate a bilateral agreement as it reached the appropriate level of readiness. Most persons expounding this view emphasized, however, that free trade with the United States would probably not result in free trade among the ASEAN members themselves.

<sup>1</sup> Former United States Trade Representative William Brock first suggested the idea of an "umbrella" agreement in 1983.

## Perceptions About Intra-ASEAN Trade

ASEAN is not a free-trade area or a common market like the European Community. Several participants noted that ASEAN is trying to improve intra-ASEAN trade but is not moving towards an internal FTA or customs union. In the past, ASEAN's economic ministers have indicated that they consider creation of a common market arrangement similar to that of the EC or formation of an intra-ASEAN free trade area an unrealistic goal. Increased economic cooperation, rather than integration, is the means that these nations favor towards internal trade liberalization.

The exchange of tariff preferences through preferential trading arrangements (PTAs) is the major instrument for liberalizing intra-ASEAN trade. To date, the impact of PTAs has been minimal because most of the items eligible for the preferences have not been important items of trade. This fact partly accounts for the relatively low level of intra-ASEAN trade, which has varied between 18 and 23 percent of total trade.<sup>1</sup> ASEAN is working toward reducing internal trade barriers and establishing joint industrial projects.

Many participants, though affirming that ASEAN has been successful as a political entity, emphasized that it has achieved little in terms of economic cooperation. These participants pointed out that it is difficult to imagine an FTA with ASEAN since its members are not even ready to open their markets to each other. One U.S. businessman typified this view:

It's premature for a U.S.-ASEAN FTA. The feasibility of an FTA with these countries would depend on what type of sliding scale was set up. If there were a 15-year phase-in, for example, it might be possible. The ASEAN countries don't have their act together as far as their own integration goes. They would have to accomplish that before a U.S.-ASEAN FTA could occur. Until you have an integrated market in this area it would not make sense to have an FTA with ASEAN.

Several participants noted that a basic obstacle to increased intra-ASEAN trade is the differences in economic structures and levels of development and the similarities in resource endowments and production. With the exception of Singapore and Brunei, the ASEAN members produce and export mainly primary commodities such as food, raw materials, and minerals, that

<sup>1</sup> ASEAN-U.S. Business Council, *The ASEAN-U.S. Economic Relationship: Overcoming Barriers to Business Cooperation*, Wash. DC, p. 9.

tend to compete with, rather than complement, the products of their ASEAN partners. As noted by a U.S. industry association, "Until ASEAN can reach agreement with themselves [on intra-ASEAN cooperation], they do not seem to be in a position to negotiate as a unit with the United States."

Other participants noted that there is little preoccupation with intra-regional trade because the growth prospects of extra-regional markets are better and the major markets for ASEAN's products are advanced industrial countries. A few participants said that an FTA with the United States is not unrealistic because, although the ASEAN countries are not willing to open up their borders to each other, they would be much more willing to engage in free trade with the United States:

## Perceptions About Special and Differential Treatment

The issue of "special and differential" treatment (S&D) arose frequently in interviews, particularly in those interviews conducted overseas. Within the context of this investigation, S&D means that the least developed partners in an FTA relationship would want and expect more time or a "slower track" than the more developed partner for implementing trade liberalizations. The general opinion among participants was that ASEAN would want a phased-in agreement that allowed them to make certain exceptions and that provided for responsibilities to fall faster to the United States than to them. As one participant said, "Even a 10-year phase-in period would be too [fast] for this region." Most participants felt that ASEAN would not press for unilateral Caribbean Basin Initiative-type one-way preferences but would like individual members to have the option to join in bilateral agreements with concessions for liberalization when ready. A few participants said that individual bilateral agreements under a broad framework agreement could work as a spur to economic integration among individual members. They felt that even with differences in economic development, a United States-ASEAN FTA is possible as long as allowances are made for a timetable that permits varying times for the countries to come on line—and allows that some may opt out for awhile. Others felt that the United States would have to allow the ASEAN members a very long time for significant liberalization to take place. However, a few participants believed the United States would never see the benefits of ASEAN liberalizations. As noted in a submission from a workers' union:

A negotiation with [a single or regional grouping of Pacific Rim countries] would be a negotiation of unequal partners on different scales of development, whose very concepts of what constitutes free trade are worlds apart. The logical outcome of such a negotiation or series of negotiations would *de facto* become one-way free trade.

### **Perceptions About Negotiating Resources and the Current Negotiating Approach**

A recurring concern among the participants was that many of the ASEAN countries lack sufficient negotiating resources to pursue an FTA at this time because their top negotiators are currently engaged in the Uruguay Round and any further negotiations would severely strain their resources. A few Government officials said that the United States might also be strained in terms of resources but they agreed that, as one negotiator put it, "we work as many hours as it takes to get the job done."

Participants were also asked about their views on the current U.S. negotiating approach with ASEAN as a preamble to the discussion on the advisability of entering into FTA negotiations. Persons expressing opinions were divided among three schools of thought on how the United States has handled its trade relations with the ASEAN nations—those who thought that trade relations with the ASEAN countries have been handled fairly well using the current issue-by-issue approach; those who thought that the current issue-by-issue approach has worked but is often contentious in nature and has led to increased trade frictions and confusion about U.S. priorities; and those who answered the question about U.S. negotiating strategy with a question of their own: "What strategy?"

#### *The current approach is successful*

A number of government officials and businessmen expressed the view that through the current issue-by-issue negotiating approach, significant progress has been made in high-priority areas and that the United States has won numerous concessions for removal of barriers "without giving anything away." Several persons holding this view pointed to countries' improvements in the area of intellectual property rights protection as a major result of U.S. diligence. One U.S. businessman said:

We don't need to do things differently; U.S. exports to ASEAN are up 30 percent. They are moving in the right direction anyway. We should continue pushing them the way we are. Even Indonesia is moving in the right direction.

#### *The current approach works, but is not ideal*

Some participants said that the current approach of unilaterally demanding changes from our trading partners has been largely responsible for the rising tide of anti-Americanism in Asia. Said one U.S. participant from the private sector:

Overall, foreign policy relations are what are at stake here, not the deficit numbers on the charts. Although we are skillful at communicating our problems and what we think is wrong, our methods are clumsy. In this region we don't need to strong-arm people; we have an immense stature there—this carries a lot of weight by itself. The effects of not realizing this can be seen in the resentment in Korea. The stakes aren't high enough to make trade problems worth the overall deterioration in overall relations. We could have been just as effective with persistent, quiet pressure.

A number of participants said that the United States has made progress using the issue-by-issue approach, not so much because of the method but because these countries saw the changes as to their own advantage and reflected that in new domestic policy.

#### *The current approach is undefined*

Many U.S. businessmen, particularly those based in ASEAN countries, said that U.S. trade policy in the ASEAN region is "ad hoc," and without discernible priorities. They believed that the U.S. approach to trade problems in the region is conducted on a piecemeal basis and that trade frictions in the region would be lessened if the United States were to make a clear statement of what it wants in terms of intellectual property rights, subsidies, licensing, etc.

### **Advantages of a United States-ASEAN FTA**

The following section summarizes the major advantages to a United States-ASEAN FTA as described by participants in the study. In addition to information obtained during interviews, the Commission received a number of written submissions. These views are also included in the following sections.

#### *Would provide emphasis to Uruguay Round*

Many participants thought that exploring the idea of FTAs in general, or a United States-ASEAN FTA in particular, could encourage GATT negotiators to reach a successful conclusion to the Uruguay Round. Some participants believed that an agreement with ASEAN would alert other U.S. trading partners that if they are not prepared to negotiate seriously in the GATT, the United States is ready

and willing to pursue other tracks. Nevertheless, participants were generally adamant that, unless there is some overriding reason to do so, the United States should not negotiate now. As one senior U.S. negotiator said:

We should wait out the Uruguay Round and also do our homework to see on what basis FTAs with any of these countries could be in the U.S. interest. We could let it be known that if the Uruguay Round failed, FTAs are an option that the United States will consider seriously.

Concerned about the integration of Europe in 1992, a few participants thought that a United States-ASEAN FTA could be a good counterweight since Europe is an important trading partner of ASEAN. Others held the view that the pursuit of FTAs now might have the opposite effect and would encourage Europe to become more protectionist.

#### *Would provide a forum for discussing trade issues*

A number of persons said that the United States has a number of trade priorities in the region that could be addressed effectively through the consultation forum FTA negotiations would provide. These issues include intellectual property rights protection in Malaysia, Thailand, and Indonesia, and expanding agricultural and services trade within ASEAN in general. An FTA would also provide a forum to address tariffs, export performance requirements, subsidies, etc., comprehensively. Many persons said that talking about bilateral trade issues in a broader context is always useful, regardless of the context (e.g., FTA, MOSS). Accordingly, these participants felt that the process of building the framework for an FTA could be an important ingredient in prioritizing U.S. objectives in the region. Negotiators could plan, study the issue, and determine what the United States wants from such an agreement. This would be beneficial whether or not an FTA is achieved.

#### *Would improve trade*

Most persons commented on the fact that there is great growth potential in ASEAN markets and, as one U.S. businessman said, "The more change we can bring to the region, the better off our industries will be." Many agreed that a United States-ASEAN FTA would help tap a large and important market for the United States.

Many persons who acknowledged that concluding an FTA with ASEAN would be very difficult because of the economic diversity of the members said, however, that an FTA might encourage ASEAN countries to open up to each other and would most likely encourage the least developed members to develop faster. An FTA

could also help ASEAN liberalize at a faster pace. Several businessmen, although skeptical about improving intra-ASEAN trade, remarked that if a United States-ASEAN FTA could compel intra-ASEAN free trade, the size of the internal market would be substantial. As one U.S. businessman based in Singapore said, "I am 100 percent in favor of any arrangement that improves trade, but I don't think it's achievable. But any arrangement that reduces barriers is to the advantage of ASEAN and should be supported."

Concern about competition from Japan in the region led several participants to advocate that the United States examine the possibilities of an FTA. A senior U.S. negotiator said:

I am concerned about Japan elbowing us aside to a certain extent in the region. We need to stay in the ball game. FTA explorations may be one way to explore future relationships with countries in the region and eventually we will have a more equitable and reciprocal relationship.

Said another participant:

We are competing against Japan for an economic hold in the region and an FTA will help us, although Japan will always dominate financially. An FTA would give a substantial share of ASEAN markets to the United States; without an FTA, Japan will be more successful than the United States.

### **Disadvantages of a United States-ASEAN FTA**

The following section summarizes the major disadvantages of a United States-ASEAN FTA as described by study participants. In addition to information obtained during interviews, the Commission received a number of written submissions. These views are expressed in the following sections.

#### *Would be impossible to monitor*

A number of persons thought an FTA with ASEAN is not feasible because it would be too difficult to administer. As one participant noted, "The mechanism doesn't exist to monitor such a structure." Several U.S. Government officials said that a United States-ASEAN FTA would create major technical problems that would make policing the agreement difficult. In particular, they were concerned that rules-of-origin could be easily circumvented. As one official said, "You would have to change the rules of origin. The levels of domestic content would have to protect us from Japan."

#### *Would not improve negotiating atmosphere*

Several persons said that an FTA would not make trade negotiations easier or eliminate the

need for an issue-by-issue approach because the most difficult barriers to eliminate are not tariffs, but politically sensitive nontariff measures. Even with an FTA agreement, they argued, the United States would still need to address certain contentious bilateral issues on an issue-by-issue basis. There would be no advantage in terms of improved negotiating. As one person said, "Usually the more trade there is, the more squabbles there are." Other participants felt that although it is true that an FTA might alleviate some tensions, that is not a valid reason for pursuing an FTA. One person remarked that after the United States-Canada FTA dispute settlement mechanism gets tested we may find that an FTA does not alleviate trade tensions at all.

#### *Would not necessarily benefit U.S. trade*

A number of participants suggested that a regional agreement, in which ASEAN members could opt to join or not join, might be practical but would not be as valuable as an agreement that included all the members. Such an agreement, they said, would be likely to include so many caveats and exceptions that it would be less than a true FTA.

Several participants were concerned that an agreement with ASEAN would confer only limited economic benefits to the United States. As a senior U.S. Government official said:

My first reaction is that their level of development is different—at a lower level than Taiwan and Korea. That would make it more difficult to gain complete access to their markets; they could not economically stand it. There would not be a lot to gain for the United States to conclude an FTA with ASEAN or with Singapore alone. If you are thinking of the future market of ASEAN then there is something to gain. But economic development is the most important element in greater sales to these countries. If they can get the money, we can sell them some things. Development will do more for our market share in these countries than an FTA.

A number of participants also noted that since an FTA would probably not stimulate intra-ASEAN trade, the United States could become even more of a target for ASEAN's export promotion efforts, and that could lead to increasingly unbalanced trade. Participants were pessimistic about the prospect of significantly increased U.S. sales because of concern about the limited ability of ASEAN countries to absorb the consequences of free trade. Although Singapore is a free-trade country, the others are highly protected and would have to move slowly. The less developed countries among ASEAN

would require substantial time to restructure their economies before the United States could expect to see any significant benefits. As one official said, "The only one ready is Singapore. All the others operate import substitution regimes and fear being flooded with imports because their industries are inefficient."

Several other U.S. officials were pessimistic about the agricultural benefits derived from an FTA. As one official said, "We might not have to give up much in an FTA, but we would not gain a lot either." A submission by a group of growers said:

[We are] generally skeptical of free trade agreements, which historically have not been good vehicles for producing liberalization in agricultural trade. Recent attempts at free trade agreements have taught us that agricultural issues, because of their complexity and political sensitivity, are either ignored, such as in the U.S.-Canada Free Trade Agreement, or skewed against U.S. interests, as in the U.S.-Israel Free Trade Agreement.

The question was also raised as to how an FTA would get at the health and labeling requirements that are currently a problem for agriculture items. Said one official, "The United States is at a disadvantage because our market is so big it is economically worthwhile for them to adjust their production to our standards, but for us to adjust to their [standards] is not economical."

Another group of persons noted that an FTA would probably not improve U.S. trade significantly because it would not address the basic issue of U.S. competitiveness and that it is unrealistic to think that it would. A U.S. diplomat overseas said, "A level playing field doesn't mean all the teams are equal."

#### **Alternatives to the United States-ASEAN FTA Approach**

Several U.S. and foreign government officials suggested that if a United States-ASEAN FTA is not feasible, an FTA agreement with Singapore would be workable, and (since Singapore is a free-trade nation) might be the appropriate place for the United States to begin if it is considering a series of bilateral with a number of countries. Additionally, these participants suggested that the United States should not favor the worst trade offenders with an FTA, but instead should reward those who pursue free trade policies, such as Singapore and Hong Kong. A few participants believed that although Singapore is ready for such an agreement, it would be divisive within ASEAN for the United States to pursue a bilateral agreement with Singapore alone, and that is not in the best interest of the United States. Moreover, these participants believed that the

United States already has relatively free access to Singapore, so there is not much to gain from an FTA. Other participants felt that a United States-Singapore FTA might cause the other ASEAN nations to raise additional trade barriers in self-defense.

Several other bilateral alternatives to the United States-ASEAN FTA approach were broached as means for improving trade relations with the ASEAN countries. Several persons suggested creating a consultative mechanism to

discuss trade issues. They felt such a structure would enable the United States to handle trade problems on an incremental basis and forestall the trade problems that disrupt relations.

A number of persons suggested that, instead of attempting an FTA, the United States and ASEAN could pursue a series of liberalization accords on specific issues, such as gradual access to markets, transparency of regulations, intellectual property rights protection, etc.





## Chapter 4

### Summary of Views on a United States-Pacific Rim Regional FTA

In its request letter, the Senate Finance Committee also asked the Commission to summarize reactions to the concept of "a broader free trade arrangement for the Pacific Rim countries in general, which interested market economy members could join."<sup>1</sup> This chapter addresses that aspect of the study request and presents the collected opinions regarding the advisability of entering into negotiations for a regional FTA, the feasibility, advantages and disadvantages, and possible ways of achieving such an agreement. Finally, the chapter presents third country considerations and participants' suggestions for alternative regional approaches.

#### Background

As requested by the Senate Finance Committee, the scope of this chapter, in addition to including Taiwan, Korea, and the ASEAN countries covered elsewhere in this report, also considers other "interested market economy countries" in the region. Determining which countries would be candidates for a Pacific Rim regional arrangement was not an easy task. No standard definition of the Pacific Rim is universally employed. Instead, it is generally defined in terms useful for the aims of particular research or analysis, both broad and narrow. For example, as noted in an OECD report:

The broadest sense [of the Pacific Rim] is geographical: it is that collection of nations washed by the Pacific Ocean, including North and South America, the Asian continent and the island states east and north of Indonesia. The more widely used but restrictive sense of the term 'Pacific' is used in the Asia-Pacific concept. This groups together the market economy nations on the Pacific slope of the Asian continent, and the island states on the Asian side of the Pacific.<sup>2</sup>

Starting with the assumption that at least Taiwan, Korea, the six ASEAN nations, Australia, New Zealand, Hong Kong, and certain Pacific islands<sup>3</sup> are likely candidates for a regional United States-Pacific Rim arrangement, the Commission sought the opinions of participants on the inclusion of these and other countries. Participants frequently offered views on whether or not Japan, Canada, Mexico, and

China should be included. Ultimately, the composition of a regional FTA, if it were formed, would be determined by the interest of governments in the region in joining such an arrangement.

Institutional vehicles to promote Pacific regional cooperation and economic coordination have been proposed and discussed on and off for at least two decades. Japan has expressed interest since the late 1960s in greater Pacific economic cooperation, as has the United States since the 1970s.<sup>4</sup> Most recently, in a speech delivered in Jakarta in July, U.S. Secretary of State Shultz urged looking to "both sides of the Pacific Basin . . . to consider measures for cooperation among the market-oriented economies of this vast area."<sup>5</sup> As the economic and political importance of the Pacific Rim countries has grown in the post-war era, so has interest in establishing stronger regional ties. In the words of one high-level official of an ASEAN government, "[the region] is important because it can be a stabilizing influence in the world. The region is looking for faster development . . . and stability comes from economic growth."

#### *Status of trade and market access*

U.S. trade relations with the Pacific Rim countries were generally described as "good" though with a few outstanding problems. One participant acknowledged that political tensions are not as high between the United States and these countries as between the United States and Japan. Although many U.S. participants consider protectionism a problem in exporting to most of the region's countries (citing high tariffs and frustrating nontariff barriers), they acknowledged progress on the part of Korea, Taiwan, the ASEAN countries, and others to liberalize their trading regimes. On the other hand, most participants from these countries expressed dissatisfaction about particular U.S. trade barriers, such as textile quotas, and concern about the direction of current protectionist pressures they see in the United States. U.S. businessmen with manufacturing operations in the Pacific also noted that their own products, at times, face U.S. trade barriers.

U.S. trade with a selected grouping of Pacific countries accounted for 14.0 percent of total U.S. exports to the world in 1987 and 18.1 percent of total U.S. imports, which is 16.5 percent of total

<sup>1</sup> Senate request letter is reproduced in appendix A.

<sup>2</sup> Michael W. Osborne and Nicolas Fourt, *Pacific Basin Economic Cooperation*, OECD, 1983, p. 4.

<sup>3</sup> Macao, Papua New Guinea, Fiji, Tonga, and Nauru.

<sup>4</sup> For example, "An Asian-Pacific Regional Economic Organization: An Exploratory Concept Paper" was prepared by the Congressional Research Service for the Senate Committee on Foreign Relations in July 1979.

<sup>5</sup> Secretary Shultz' speech in Jakarta, Jul. 11, 1988 entitled "Facing the Future: America, Asia, and the Global Economy."

U.S. trade turnover.<sup>1</sup> By rank within the region, Taiwan, Korea, Hong Kong, Singapore, and Australia were the largest U. S. trading partners. In trade with the Pacific Rim countries, the United States recorded a \$38.7 billion trade deficit in 1987, accounting for almost 25 percent of the total U.S. trade deficit. The deficit reflected \$34.1 billion in U.S. exports and \$72.7 billion in U.S. imports. The United States ran a trade surplus in 1987 with only three of the countries included in this data—Australia, Brunei, and Papua New Guinea.

In general, leading U.S. exports to the region are concentrated in various component parts, aircraft, agricultural products, and some other machinery and equipment. U.S. imports are dominated by consumer items. By far, the top U.S. export to the region was certain types of electronic tubes, valued at almost \$3.9 billion in 1987 and almost \$3.4 billion in January–September 1988. The second-ranking U.S. export was parts of office machinery in 1987 and gold and silver bullion in interim 1988 (mostly attributable to Taiwan). Some of the other leading exports in 1987 and 1988 were aircraft and aircraft parts. The highest ranking U.S. import from the region was monolithic integrated circuits, valued at over \$3.5 billion in 1987 and over \$3.6 billion in January–September 1988. The second ranking U.S. import in 1987 and 1988 was parts of automated data processing machines, followed by motor vehicles. Other items totaling more than \$1 billion in imports in 1987 were crude petroleum, certain footwear, women's manmade knit blouses, machines, beef and veal, and television receivers. (See appendix D for further details of United States-Pacific Rim trade.)

The merchandise trade figures do not, however, provide a complete picture of flows between the United States and the Pacific Rim countries. The abundance of U.S.-owned firms producing in the region was pointed out by many study participants. The Asia-Pacific Council of American Chambers of Commerce estimates that its members represent investments of \$40 billion in the region.<sup>2</sup> Estimates of the percentage of goods manufactured by American firms and

<sup>1</sup> The data presented in this section is intended to provide a reference point of the composition and importance of U.S. trade with Pacific countries. Included in the data are South Korea, Taiwan, Hong Kong, Australia, New Zealand, Thailand, the Philippines, Brunei, Malaysia, Singapore, Indonesia, Macao, Papua New Guinea, and certain Pacific island nations (Nauru, Fiji, and Tonga). Data does not include other countries that were at times suggested by participants for inclusion in a Pacific Rim arrangement, such as Canada, Mexico, and China. Data on Japan were excluded because Japan is covered in-depth in the September 1989 Commission study on a U.S.-Japan FTA.

<sup>2</sup> Harvey Goldstein, Chairman of the Asia-Pacific Council of American Chambers of Commerce in "Letter of America", No. 2, Nov. 1988.

exported to the United States from some of these countries was estimated to be as high as 50 percent for certain products. An example is electronic products exported from Singapore.

### Perceptions on Feasibility and Negotiating Modalities

A majority of participants, both favorable and unfavorable to the idea of a regional FTA, questioned the feasibility of negotiating, designing, or implementing a regional agreement. A comment frequently made by participants was that such an agreement would "be great for the United States and for the region, but is an unattainable ideal." "The idea is ridiculous and besides, it could not be done," said one U.S. official. A Taiwan academic surmised that "an FTA with the region might make sense for some reasons, but would be more difficult to achieve." Moreover, one submission noted that:

Current trade policy considerations would also render an FTA with some countries under consideration less feasible. Provisions in the Trade Act of 1988 require negotiations with identified priority countries under "super 301," "special 301" intellectual property rights protections, and telecommunications reciprocity. These negotiations could overlap with or block FTA negotiations with at least one of the Pacific Rim countries.

#### *A regional FTA is not feasible*

The majority of participants saw a regional approach to an FTA as unfeasible. Many thought the differences in levels of development among Pacific Rim countries made the idea a nonstarter. Some also thought diversities in social and political systems were not amenable to an FTA approach. Still others felt that dealing with so many countries in a regional FTA approach would make it unfeasible for negotiations to succeed, for a meaningful document to be drawn up, or for implementation to be assured. Given a choice between bilateral or regional approaches, many thought bilaterals were more feasible.

The diversity of the region was one of the most frequently cited reasons for opposing the regional approach. Speaking at a meeting of a group of businessmen operating in the Pacific, one said, "It's too big—a dream. You are never going to make an agreement with a collection of countries as diverse as Asian countries." A U.S. Government official called the idea "Pie in the Sky," adding that "it would never work because of the disparity among nations." Another U.S. businessman said, "The region is so diverse and ethnically different—it's not Europe—you really need bilateral agreements."

The opinion that disparity in levels of economic development presented a serious obstacle to achieving a regional FTA was frequently voiced by participants. Within the region, some countries are considered developed (e.g. Australia, and New Zealand), some are considered advanced developing economies (e.g. Taiwan and Korea), and most are considered developing countries. A number of participants supported a general premise that an FTA was not the appropriate vehicle for managing trade relations between developed and developing countries and, furthermore, that a developing country needs to reach a more secure level of development before it is actually willing or able to dispense with its high levels of protectionism. One U.S. Government official said that a regional FTA would be "unrealistic primarily because of the level of development disparities among the countries." Another U.S. official asserted that "similar levels of development and similar legal systems are required before an FTA will work. This is not the case with the Asian region at this time." A noted U.S. academic on Asian Pacific affairs called the idea of an FTA in the region "premature, while they are at different levels of development." "Even the more developed [NIEs]," complained a couple of participants, "still have an LDC mentality of protecting infant industries." A foreign government official predicted that the "varying levels of development would bring in the same problems as with a U.S.-ASEAN FTA but on a larger scale."

Supporting the idea that actually negotiating a Pacific Rim FTA was unfeasible for the United States, one businessman said, "It would be a dumb idea to negotiate with many countries simultaneously." "The negotiating problems would be enormous," said a U.S. Government official, adding that "It is not practical to begin negotiations with all countries in the region at once." A U.S. diplomat remarked, "A regional FTA? No way! How would you like to negotiate that for the rest of your life?" Another U.S. official argued, "The more countries, the more difficult to negotiate—the problems would multiply with each country added."

One trade policy analyst cautioned that any attempt at a regional arrangement "would essentially entail a series of bilaterals with concomitant resource problems." One former Commerce Department administrator also cited limitations in negotiating resources. "We can't negotiate a bunch of FTAs at once due to resource limitations," he warned, "We could start with one." An ASEAN private sector representative voiced a related concern that ASEAN alone is big enough for an FTA—"there would be practical problems with making it broader." Most participants agreed that attempting a regional FTA—no matter how defined—would be a long-term process. A former

U.S. trade negotiator admitted that for "some countries it would take longer than others to negotiate" and cited Korea as an example.

On the feasibility of negotiations from the point of view of U.S. trading partners in the region, one Taiwan academic observed that there is "not much trade between certain Asian countries . . . where would they find common interest to negotiate?" Another participant speculated that their incentive to negotiate would be reduced because the NIEs are all direct competitors.

A business representative raised concerns voiced by several participants that negotiators would have a difficult time accomplishing their aims because of the high levels of trade barriers and protectionism in the region. "It would be impossible to put together a paper on barriers in the Pacific region because it would be very long," he said. A regional FTA "won't work—Asia is not ready." He saw an additional problem that "No one will take down barriers while they are negotiating" so any liberalization that is taking place would be stalled.

Many participants thought that drafting an agreement that could apply to the whole Pacific region would not be possible. "This can't be translated into an official agreement" said one U.S. businessman operating there. "Although you might have more to work with," said another U.S. businessman, "[the agreement] also becomes more vague and therefore less significant." A member of a U.S. trade association with members based in ASEAN countries said, "I don't know anyone in Washington that could design such a thing."

Finally, a few participants thought such an agreement would be difficult or impossible to implement. "How would such an agreement be administered and balanced?" wondered one Washington academic. He also feared that the Asian countries "would recognize the unsustainability of such an arrangement."

#### *A regional FTA is feasible*

Some participants thought a regional agreement would be achievable, and in some ways more feasible than bilateral FTAs. A private sector participant speculated that it "would not be impossible if countries begin to see that free trade works." Said one foreign government official, "It is more likely to be accepted by many countries in the region than [separate] bilaterals with the United States. For example, there would be a more positive reaction from Korea." Other participants thought the end result of starting out on the bilateral path might in any event result in a regional arrangement.

How would a regional FTA be accomplished? Several participants speculated on ways to reach this end. Some suggested that with whichever country or countries an FTA might be first

initiated, the goal of freer Pacific-wide trade could be achieved by leaving the initial agreement open ended and encouraging other countries to join the agreement at a later date. Many participants holding this view also predicted that if an agreement were concluded with one country in the region, the interest of others would not lag far behind. As one businessman observed, "If you start with one, others will not want to be left out. They would be at a disadvantage otherwise. The choice is whether to form a regional FTA or do a series of bilaterals." "Perhaps bilateral agreements could precede a Pacific community relationship," said one academic. Another academic agreed that bilateral agreements could be steps along the way to reaching a regional agreement.

At the Commission hearing, one participant recommended that the United States draft a model agreement that could be used in negotiations with a number of countries. Although this implies a series of bilateral agreements, some thought that the ultimate effect of several bilaterals might be similar to a regional arrangement. A few participants suggested that the FTA between the United States and Canada might be extended to encompass some Pacific nations. Another suggestion was to involve the Pacific Economic Coordination Conference (PECC) and the Pacific Basin Economic Council (PBECC) in active study of the possibilities for a regional FTA.<sup>1</sup> "Issues must be clearly delineated and extensively studied," said one source.

### **Advantages of a Regional FTA Approach**

Few participants expressed unqualified support for the idea of a United States-Pacific Rim regional FTA. Those who found the idea attractive in principle noted potential advantages but tempered their views with warnings on the disadvantages. One remark typical of this mixed reaction was that a regional FTA is "a daunting prospect but intriguing." Thus, many of the advantages listed below should be read in close conjunction with the disadvantages that follow. Even among those participants who saw benefits to be gained, few thought the benefits of a regional accord could outweigh those of a successful Uruguay Round and stronger GATT.

Reactions favorable to a Pacific regional FTA included such comments as "This is a good idea, particularly as a long-term goal. It would be a step in the right direction." One association executive summed up the advantages as expand-

ed markets for the United States, a way of dealing with and countering Japan's dominance in the region, and enhanced national security through moderating the economic disputes that erode overall relations. A few thought it might be a better alternative than bilateral FTAs because it would offer a much wider market for U.S. exports than an FTA with any individual country.

#### *Would confer political benefits and promote regional cooperation*

Some participants believed that a political benefit of a regional FTA would be to foster improved regional cooperation. One U.S. official argued that it also avoids the political fallout of "doing it with one or two and leaving the rest out." In a somewhat cynical endorsement, one U.S. official said that Pacific regionalism is attractive to politicians who can see that although "they won't gain a lot, they won't lose anything either."

Many persons who cited increased regional cooperation as an advantage asserted that U.S. interests in the region go beyond trade issues to include military, strategic, and other economic concerns, such as debt and monetary matters. An FTA that is broad in scope, some thought, would be beneficial to U.S. interests by improving regional cooperation not only on the trade level, but on the economic, political, and strategic levels as well. An American academic suggested that a regional agreement could also coordinate monetary and fiscal policies. U.S. businessmen in the Pacific saw advantages accruing from including investment and services provisions in an agreement. A foreign official suggested that another function of a regional arrangement might be to coordinate aid policies.

#### *Would confer economic benefits and opportunities*

Some participants saw significant potential for economic gain through a regional FTA because, in the words of one businessman, "the region will be one of the largest markets in the next 10 years." Moreover, one submission suggested that U.S. industries that offer virtually unrestricted access to the U.S. market while confronting significant trade barriers would benefit the most from a regional FTA approach. Services, telecommunications, and aerospace would likely fall into this group. In addition, the submission noted that:

Substantial reductions in tariffs, coupled with liberalized import regimes and improved intellectual property protections, would produce tangible opportunities for many U.S. industries, among them computers, sporting goods, furniture, musical instruments, processed foods, machinery, air-conditioning and

<sup>1</sup> PECC is a nongovernmental association of academics, business representatives, and government officials that sponsors discussion of Pacific economic issues. It is described in greater detail later in this chapter. PBECC is a forum of senior business leaders from over 850 firms located throughout the Pacific Basin, dedicated to the expansion of trade and investment.

refrigeration equipment, and oil field equipment.

Economic dynamism of the region was not the only reason seen to contribute to the economic benefits of a regional FTA. An additional argument was based on the benefits of including a greater number of countries in any FTA arrangement. Said one U.S. Government official, "If you believe in comparative advantage, the larger the block the better; but . . . it would be very difficult to negotiate." An American academic agreed that "the bigger the arrangement, the better" was an important consideration from the U.S. standpoint. "The advantage is opening up all of the countries," said a U.S. Agriculture official. A U.S. trade official noted that "An FTA with this region would free half the world's trade." An additional advantage is that certain U.S. industries would benefit not only from expanded access but also from preferential access to Pacific Rim markets. A submission reflecting the opinion of a broad group of industry analysts stated:

In general, there are some inherent benefits to seeking a broad arrangement rather than a series of separate agreements. For one thing, a broad arrangement would reduce problems of transshipment. This occurs when countries—not FTA partners or eligible for GSP or other duty-free treatment—try to ship their products through countries qualified for lower U.S. import tariffs. A broader arrangement also offers the advantage of economics of scale. In addition to expanding the size of the potential market, border arrangements could help in overcoming some cultural barriers, such as limited experience in computer programming in Asian languages. The difficulty, of course, is finding a mix of countries that is attractive to the broadest possible spectrum of U.S. industry. This is not easy in the Pacific Rim. Many industries, such as aerospace and telecommunications, would be most attracted by the large markets of Korea and Taiwan, while these same countries pose the most formidable competitive challenge for import-impacted U.S. industries.

#### *Would complement and augment the GATT*

Another advantage of a regional arrangement was described by one academic as the ability to achieve greater specific gains than can be achieved in the GATT. "In GATT you get the lowest common denominator," he said, "it could be raised in a regional FTA." One U.S. Government official said that a regional approach could have the advantage of serving to "augment

the GATT [although] the negotiating problems would be enormous."

### **Disadvantages of a Regional FTA Approach**

The idea of a regional agreement brought on negative reactions such as "unworkable," "impossible," "ridiculous," "too big," "a pipe dream," "an ideal," "impractical," "pie in the sky," "hard to imagine," and just plain "dumb." The overall perspectives of those opposed to a regional FTA varied. Some preferred bilateral agreements rather than a regional grouping. Some opposed both regional and bilateral agreements, attributing similar disadvantages to both. Some opposed a regional approach as an idea that was premature, but did not dismiss its usefulness at some time in the future.

#### *Would have political risks*

A few participants observed that the political dynamics of the region's countries, and the dynamics of negotiating with several countries at once, could result in a regional agreement that would not accomplish its objectives. This result might have the added political risk of yielding disappointment and poor acceptance both in the United States and other Pacific Rim countries. A U.S. businessman surmised that the "increase in the number of players you have decreases the chances that the package will really mean something." One trade analyst noted that the political reality is that a Pacific Rim regional FTA would be "chock full of exceptions, resulting in a patchwork quilt of good intentions." A few participants suggested that the six ASEAN countries would also be politically resistant to a broad regional grouping. One diplomat said that "ASEAN countries would be reluctant to get involved [in a broader regional group] because they are very proud of what they have accomplished as an independent institution."

#### *Would have a negative economic impact*

Other disadvantages cited were economic costs—on a global scale and on a national scale. In global terms, one trade policy analyst said that a regional FTA would not avoid trade diversion, "which is normally regarded as a major cost of FTAs." At a gathering of trade policy analysts, one academic noted that FTAs "do not necessarily cause an improvement in international efficiency, and it is possible that they reduce efficiency and real incomes instead."

As for potential costs to U.S. industry, a number of trade associations feared the worst. One industry association representative predicted that an FTA with "any or all" of the Pacific Rim countries "would have a devastating impact on the import-sensitive, labor-intensive domestic rubber footwear industry." The mushroom industry went on record opposed to "bilateral or

any broader free trade arrangements" on the basis of "documented serious injury to the domestic mushroom industry by Pacific mushroom imports in the past, and the anticipated additional economic harm to U.S. producers and canners entailed by a free trade agreement with Pacific nations." Another submission noted that industries, such as footwear, household appliances, power hand tools, bearings, valves and pipe fittings would have difficulty adjusting to increased competition. Another major concern was voiced about the effects on U.S. industry if third-country competitors, particularly Japan, were to gain unanticipated and unreciprocated access to the U.S. market by acquiring "national" status in the Pacific Rim countries through subsidiary arrangements.

Some participants noted that the disparity in levels of economic development between Pacific Rim countries and the United States would provide only limited prospects for balancing trade concessions within industry sectors. Also, one submission noted that any FTA proposal would be hardest for those U.S. industry sectors that already have special trade arrangements with the Pacific Rim countries. This would include steel, machine tools, and textiles. The submission suggested that liberalization in these sectors would best be addressed in a global context.

Similar dire concerns were voiced by representatives of the textile industry and of the leather and plastic goods industries. However, comments from U.S. businesses with interests in the Pacific Rim generally saw potential economic payoffs, and U.S. domestic industries less sensitive to imports from low-wage, Pacific Rim countries felt considerably less threatened.

#### *Would further fragment the world into trade blocs*

Another disadvantage attributed to a regional arrangement was that it would further promote the formation of competing and protectionist trade blocs. One foreign businessman expressed concern about development of regional blocs and their impact on free and fair trade in the world. Another participant said that either a Pacific Rim FTA or a series of bilateral FTAs in the region would tend to "fragment the world trading system into blocs which could well acquire protectionist characteristics." The ill effect of this, he said, was that "a world of trading blocs would leave out Latin America and Africa." Further, he argued that a regional FTA would not completely address the trading concerns of the Pacific Rim countries because, "They have global interests as well." He added that movement toward trading blocs is not a "message we want to send the EC at a time when we are concerned about the policies the EC may adopt in 1992."

### **Third Country Considerations**

A number of participants noted that countries outside of any FTA arrangement may have legitimate concerns about the trade diversion effects of the FTA on important export markets. Many thought that the greater the pressures, (i.e., the more bilateral arrangements, formation of protectionist trade blocs, or pessimism about the GATT round), the more likely a greater number of countries would be interested in including themselves in a Pacific regional arrangement, rather than getting "left out in the cold."

However, with regard to those areas of the world not within the Pacific region, some participants expressed concern about the implications for overall U.S. economic and political relations of negotiating a major agreement that ignores them. As one participant warned, it "... would implicitly and significantly downplay our relationships in other parts of the world." Another agreed, saying that "leaving out countries in other parts of the world creates trade policy problems as well as overall foreign policy problems."

Some participants viewed support for a Pacific regional FTA proposal as a reaction by the region to protect its interests as "third countries" left out of the Canada-United States pact and European integration. EC 1992 is "pushing the Pacific Rim countries into acting and reacting more like a bloc," said a U.S. private sector representative working in the Pacific. Although some participants thought a Pacific FTA might provide leverage in encouraging the EC to avoid protectionism in its 1992 program, others feared that it might fuel the arguments of those in the EC already pushing for a "fortress Europe" and incite further EC protectionism.

Many participants offered views regarding the ramifications of excluding Japan, Australia, and New Zealand from a regional agreement. Although geographically falling within the Pacific Rim, if, as some participants suggested, these countries were excluded they would have substantial interests as "third" countries. Therefore, some special considerations regarding these countries are presented in this section. Participants' reactions were mixed regarding whether or not the inclusion of Japan would be in the region's interest. Some argued that an agreement excluding Japan might provide leverage with that country in other trade negotiations. Regarding Australia and New Zealand, many participants saw no greatly enhanced economic benefits to include them in a regional agreement, but no compelling reasons to leave them out.

#### *Further considerations regarding Japan*

Study participants foresaw both advantages and disadvantages to excluding Japan from a regional FTA.<sup>1</sup> Although the response was

mixed, many asserted that Japan might be included by virtue of its importance as an export market for the region's countries. However, a drawback to including Japan, in the view of one U.S. official, was that many countries in the region "have no desire to open up further to the Japanese." Also, a few participants noted that some Pacific countries would find a group including both Japan and the United States preferable to a regional trading group formed only with Japan. Another association executive noted that a "dominant concern of the Pacific countries is how to deal with the two giants—the United States and Japan." An Asian government official argued that "China and Japan are the key economies in this region," but he added that "there are psychological and political implications with including them."

Some participants believe, however, that leaving Japan out of a regional FTA might not be possible or practical. One trade policy analyst speculated:

If the United States started running around doing bilateral trade deals with Asian countries other than Japan, the Japanese would be in the door as fast as the United States is out because those are major trading partners of theirs.

A foreign academic predicted that, if excluded, Japan would be "unhappy with trade diversion effects" and implied that Japan might attempt to form its own arrangements. A former U.S. trade negotiator said a regional agreement should begin by excluding Japan and negotiating with other countries first to gain "huge negotiating leverage with Japan." A few U.S. and foreign participants thought a regional FTA might help the United States balance Japan's large and growing influence in the region, whether or not Japan is included in the agreement.

One foreign Government official expressed a frequently encountered opinion that Japan "wants to lead a regional group and is economically strong enough to do so." One trade policy analyst dismissed this as a reason for the United States to pursue an FTA with the region. "I happen to think that's nonsense," he said, "because I don't think any Asian countries are very anxious to join a trading bloc with Japan." Also, a U.S. Government official recalled that "Japan has proposed a Pacific Rim community, but this idea was received coolly by other Asian countries. They saw it as beneficial to Japan but not to them."

As a last resort, however, some participants speculated that countries in the region might join

<sup>1</sup> Although some of the most salient issues regarding inclusion of Japan in a regional FTA are summarized in this chapter, Japan is not the main focus of this report. The reader may find an in-depth treatment of considerations regarding Japan in the Commission's previous study regarding Japan.

with Japan (if the United States is not interested) rather than be left out in a world of regional trading blocs. One Korean businessman echoed the thoughts of others saying:

A regional FTA led by Japan? We are interested. We don't like it. We have a long history of differences. If given no choice we would have to join a trade bloc, but it would be built on sand, not on concrete.

#### *Further considerations regarding Australia and New Zealand*

Participants from Australia and New Zealand indicated that both countries see the Uruguay Round and the multilateral system as by far their first priority, with regional or other FTAs a distant alternative. However, neither country would want to be excluded from a regional FTA if it were negotiated and formed. Also, participants from other Pacific countries did not object to including Australia and New Zealand in such an agreement.

An Australian academic argued that "the risks of damage to the multilateral system are somewhat greater" for Australia than for the United States. "Australia has a big stake in U.S. (and European and Japanese) markets being open not just to direct exports from Australia, but also . . . for imports from Asian exporters who in turn import Australian raw materials," he observed. In view of these interests, the participant said Australia and New Zealand "might go along with the idea of joining a regional FTA but would do so reluctantly." "Our argument is that we are an integral part of the Pacific" said an Australia official, "Australia does not want an FTA, but if the process gets farther, we don't want to be left out." Other participants agreed, adding that New Zealand would also be "resistant to any agreements by the U.S. that would exclude New Zealand from competing fairly."

According to some participants, the economic consequences of including Australia and New Zealand in a regional arrangement might not be great, whether negative or positive. However, some thought adverse political consequences would result if the two countries were excluded. Several businessmen operating in Asia argued that although Australia and New Zealand are very protectionist, they "are not now important in terms of markets." One U.S. official noted areas of competition in U.S. exports and those of Australia and New Zealand and said that including them "might not help maximize U.S. sales." A foreign official agreed that it "would be difficult for the United States to have an FTA with them because of the high agricultural content of their exports." Nevertheless, a number of participants cautioned that Australia and New



Zealand "would be against an arrangement that excluded them."

The doubts of Australia and New Zealand about a regional FTA did not extend to the idea of improving Pacific Rim cooperation in general. Officials from both countries, and others familiar with their interests, reported that they are interested in greater regional cooperation. As some government officials described it, "Australia is very interested in Pacific cooperation with two major interests in mind. First, to build a stronger regional commitment to multilateral negotiations, and second, to see that Pacific trade and regional interests are not harmed by the growth of FTAs."

The conclusion of the United States-Canada FTA and the work toward completing the integration of the European Community in 1992 appear to have intensified Australian concerns about the growth of regional economic blocs. As a result, Australia and Japan have formed a bilateral group to discuss the possible effects on third countries of the United States-Canada agreement. The group intends to meet regularly through 1992. According to an Australian participant, while the success of the Uruguay Round is the highest priority for both Australia and Japan, in his opinion, this group could also explore avenues for greater Pacific cooperation.

According to Australian officials, the Closer Economic Relationship (CER) concluded with New Zealand does not represent an interest in the formation of trading blocs.<sup>1</sup> They argued that the CER is a "legal expression for a relationship that has been growing more complementary for many years because of culture, proximity, and mutual interests." Like the United States-Canada FTA, the CER is viewed by many participants as a "special case" because of geographical proximity and other reasons stated above. Participants from other Pacific countries noted that the Australia-New Zealand pact is understandable given the history of economic cooperation and other ties between the two countries.<sup>2</sup>

<sup>1</sup> Since the 1960s a limited trade agreement had been in operation between Australia and New Zealand. Since this agreement gradually degenerated, a new agreement the CER, was negotiated and first put into effect in 1983. Originally calling for phasing in of free trade in goods by 1995, the deadline has now been moved 5 years forward to 1990, and coverage of services was added. The CER also calls for review stages. At the most recent review, in autumn 1988, the two countries agreed to add a protocol covering the elimination of service barriers, antidumping duties, and other nontariff barriers. Waiving the use of antidumping laws between each other is a feature not found in other trade agreements. The agreement is structured as an ongoing process of negotiations lasting beyond 1990 with

Asked whether the CER might serve as a model for other arrangements in the region or be extended to other countries, one participant speculated that as a practical matter it could not: "The provisions were too specifically designed and detailed for application between two countries that are historically linked with similar economic and legal systems and cultural traditions." The official also pointed out that the CER required a number of decades and recurring negotiations to reach even a yet unfinished stage. The official saw this effort as no small indicator of the difficulty the United States would encounter in trying to conclude an FTA to cover an entire region of countries that are economically and politically diverse.

### Alternative Regional Approaches

Many participants acknowledged the need for some kind of forum or mechanism for enhanced consultation, coordination, and/or cooperation among Pacific Rim countries. These ideas were manifested in several kinds of proposals. Some suggested loosely knit consultative mechanisms such as the "Shultz initiative," and Senator Bradley's "PAC-8" proposal, which have been publicly aired in the past year. A few proposed making better use of already existing avenues, such as PECC. Some thought more formal institutionalization, either OECD-like or GATT-like in nature, was called for. One participant proposed that the United States should limit itself to an FTA with the "four tigers" of the region. Such proposals, and reactions to them by study participants, are outlined in the following sections.

#### <sup>1</sup>—Continued

continued negotiation of further protocols to progressively eliminate all barriers and harmonize standards and business practices. The agreement, however, is not without its exempted lists for certain products and service sectors, although, at times, exempted areas have been brought in at later phases (e.g., services).

The CER is said to have some advantages for the global trading environment by setting an example in some areas. Australia's Minister of Foreign Affairs and Trade has said, "Our own experience with [CER] has demonstrated the benefits which can be derived from freeing trade barriers between neighbors. (From an address by Australian Senator Gareth Evans, Asia Society, Washington, D.C., Oct. 7, 1988.) In addition, an ASEAN government official gave the CER credit for "pushing GATT along on services."

<sup>2</sup> Nevertheless, some Government officials expressed mild concern about the potential effect the agreement might have on their trade. "It should affect us because they have high barriers," said one ASEAN country official, "but it has had only a limited effect." Singapore's Prime Minister Lee Kuan Yew has voiced this concern to New Zealand's Prime Minister David Lange, saying that it will put countries other than Australia at a disadvantage in exporting to New Zealand markets. ("PM: Trade pact will affect S'pore," *The Straights Times*, Singapore daily newspaper, Nov. 8, 1988, p. 1.)



Participants offered several caveats that could apply to broad regional arrangements of any kind. An Asian businessman advised that "To be effective a forum needs high-level contacts. But since sensitivities develop when issues are considered at a high level, there needs to be a way found to have a forum without such sensitivities." A Korean academic was somewhat pessimistic on this score: "The idea of regional cooperation has been around for decades. There has been some institutionalization, but few results."

One American academic suggested a "framework agreement, rather than an FTA, as a process for discussing trade." He thought such an agreement could help avoid trade disputes, handle tensions, and raise ideas about mutually beneficial activities that might be undertaken in the region. A U.S. Government official suggested starting with something less than an FTA by creating a "consultative mechanism for discussing trade issues." "Negotiating something less than an FTA might be desirable," he said, "to clear the path leading to a more comprehensive arrangement."

#### *Pacific Economic Cooperation Conference*

Several study participants suggested that an already existing regional forum such as PECC, could be used as a basis to explore the possibility of broader regional economic cooperation, including but not limited to the idea of an FTA.<sup>1</sup> One former Commerce Department administrator thought talking about doing FTAs "doesn't mean we shouldn't look at PECC." He saw utility in gaining a forum for Taiwan with PECC. "Maybe PECC will grow into a concrete forum to help promote free trade in the region," said one foreign trade association official. The U.S. National Committee for PECC suggested that "PECC itself would be a logical place in which to conduct a preliminary study of a Pacific FTA" or other alternatives. "It should be used more," said a foreign academic, "it needs to set a common outlook for the region every year. It could also help with coordination of investment in each country."

#### *Shultz initiative*

In July 1988 in Jakarta, Secretary of State George Shultz floated ideas for closer regional economic cooperation. In a speech, he said:

<sup>1</sup> PECC is a nongovernmental group that serves as a regional forum in which government officials, academics, and business leaders meet to discuss policy responses to Pacific Basin economic concerns, particularly regarding trade. PECC was formed in 1980 and the U.S. National Committee to coordinate U.S. participation in PECC was formed in September 1984. Its membership is broad based, including not only the United States, Taiwan, Korea, and ASEAN countries, but also China, Australia, Japan, Canada, New Zealand, and the Pacific Islands. The Pacific Basin Economic Council and the Pacific Trade and Development Conference are institutional members.

... we should consider measures for cooperation among the market-oriented economies of this vast area of the world. Any initiative, to be successful, must be outward-looking and inclusive. We do not seek to create a closed trading block in the Pacific. That would be to no one's benefit. Rather, we should start intergovernmental exchanges on the structural policies needed to promote more integrated processes of production and distribution.<sup>2</sup>

He then elaborated on several sectors, naming transportation, telecommunications, education, natural resources, and the environment, in which cooperation would be valuable. He also urged adjustment in domestic policies to address structural rigidities, exchange rates, and trade barriers. Shultz proposed cooperation among "market-oriented economies" but did not specify which countries he intended to cover with this phrase. He also stopped short of proposing the formation of any institution, however, and the actual methods intended for managing this cooperation were not clear to either U.S. or foreign trade specialists interviewed for this study.

A U.S. Government official who favored this approach over an FTA approach with the region said the Shultz initiative "envisions meetings between government officials on an annual basis and perhaps eventually some type of institution." The official also did not speculate on exactly which countries should be included, except to say that the China would probably eventually be included. He also acknowledged that the initiative would be "compatible with FTAs" but said he wouldn't want to turn the Shultz initiative into an FTA.

#### *"PAC-8" proposal*

In a December 1988 speech, Senator Bill Bradley proposed the formation of a Pacific Coalition.<sup>2</sup> He proposed that the group begin with eight countries (hence its acronym "PAC-8") including an equal number of developed and developing countries. The countries he suggested were the United States, Japan, Canada, Australia, Mexico, South Korea, Indonesia, and Thailand. He describes the mission of this coalition as reinforcing the Uruguay Round by building consensus, fostering greater economic policy coordination, and removing obstacles to developing country growth. Bradley elaborates on the three main tasks he assigns to this group: to strengthen the multilateral system; to move toward greater Pacific economic integration; and to create a closer partnership between developing and industrialized countries. He cautions that if such a coalition does not seek to address the

<sup>1</sup> Speech by Senator Bill Bradley to the New York Economic Club, Dec. 9, 1988.

<sup>2</sup> Secretary Shultz' speech in Jakarta, Jul. 11, 1988 entitled "Facing the Future: America, Asia, and the Global Economy."

problems of the world economy then "terrible crises could impoverish hundreds of millions of people, destroy democracy, and lead to massive social unrest."

### *Pacific OECD*

The formation of an OECD-like arrangement has been suggested over the years under various guises. The idea seems often to be associated with proposals that have been raised from time to time by Japan since the 1960s. Hence, some participants' reactions to the idea are linked to their concerns about Japan's role in the region. "A Pacific OECD with Japan in it?—not likely to happen," said an academic from an ASEAN nation. "This would not be likely because of feelings toward Japan," said an ASEAN businessman.

"Perhaps an OECD-like organization might be an appropriate place to discuss trade concerns," said one U.S. Government official. "We need something," he added, "but not an FTA." In a recent speech, Australia's Prime Minister acknowledged the Shultz and Bradley proposals and noted his country's interest in exploring "a more formal intergovernmental vehicle of regional cooperation" for analysis and consultation on economic and social issues. "I see merit," he added, "in the model provided, in a different context, by the OECD."<sup>1</sup> Citing the economic disparities among countries, an official of an ASEAN government said "Perhaps it is possible in the far future, but it is not likely to happen in the near future." A Korean official said that such an arrangement could only work if all member countries were treated as equals, "otherwise a structural dialogue could be interpreted as one-sided."

Trade officials both in the United States and in ASEAN countries feared a Pacific OECD might not be useful. "There are no significant benefits for an OECD-like organization in the near future," said the official from an ASEAN government. A former U.S. official thought an OECD-like organization irrelevant because of its lack of enforcement mechanisms. A U.S. official speculated that it "won't do much in the trade area."

### *A greater role for the NIEs*

A few study participants suggested the United States should give particular focus to the NIEs (Taiwan, Korea, Hong Kong, and Singapore) in the region. In the words of one U.S. official, "getting the developed countries in the region to cooperate and to take on more responsibility for trade in the region should be encouraged." A

<sup>1</sup> Speech by Prime Minister Robert Hawke, entitled "Regional Cooperation: Challenges for Korea and Australia," before a luncheon of Korean Business Associations in Korea, Jan. 31, 1989.

foreign academic suggested that "an FTA with the four NIEs might be more reasonable" for the United States than FTA's with other Pacific Rim countries. However, a few participants suggested that greater involvement of the NIEs in global economic policymaking could be best achieved through membership in the OECD.

### *Mini-GATT proposals*

Proposals supporting the formation of a GATT-like organization (sometimes referred to as "mini-GATT" or "super-GATT") have been given thought in the academic and "think tank" community in the United States. The idea's proponents argue that it might be more useful or beneficial than FTAs or other alternatives and avoid some of the disadvantages. Some feel such an organization could serve the region, and some see it as expanding to include countries beyond the region. A few participants offered the proposal as a strategy to fill the void if the Uruguay Round fails, whereas some see it as a supplement to the GATT. Maintaining GATT-like or GATT-consistent principles is the cornerstone of these kinds of proposals.

If Uruguay Round efforts falter, one trade policy analyst said, "the preferred fallback would be a "mini-GATT" of as many like-minded countries as should choose to participate, rather than a regionally oriented series of deals along bilateral or plurilateral lines." Such a "fallback" is not aimed at exclusively including the Pacific Rim. A foreign businessman expressed concern, however, that a mini-GATT "would be a more significant departure from the GATT than bilaterals would be."

Another participant noted problems with modernizing the GATT, including the inability of the GATT to "graduate" developing countries into assuming greater obligations and responsibility. As an alternative, she suggested that "like-minded" countries that want to modernize the GATT might "band together and agree to a new set of rules which wouldn't differentiate between developed and developing countries." She recommended that the arrangement be opened, welcoming other countries that are interested." As for the existing GATT, she said, "A super-GATT agreement need not replace the current GATT. Members would obey GATT rules plus the additional rules." Asked if Pacific Rim countries fit her conception of "like-minded," she responded that they would if current trends toward liberalization continue. "Such Pacific countries that could be included are," she said, "Japan first, then Taiwan, Korea, Singapore, Canada, and Australia and New Zealand." She cautioned, however, that if GATT "could be modernized and made to work, that would be a preferred solution."

A similar approach was supported by another participant, who said:

A free-trade negotiation with these countries should be within the framework of a multilateral free-trade strategy: a strategy through which the United States invites the economically advanced countries of the free world to join with us in forming a multilateral free-trade area.

Alternatively, he suggested that "Any bilateral negotiation should be open ended to welcome any other countries that may care to participate."



## Chapter 5

### Implications For The Multilateral Trading System

Almost all participants expressed support for the multilateral trading system, and the majority agreed that the Uruguay Round is the best current vehicle for trade liberalization. A large number of persons, representing a broad spectrum of interests, believed that now is not the time to begin negotiating additional FTAs; that the United States should concentrate its energy and resources to bring about the successful conclusion to the Uruguay Round. Only after evaluating the results of the Round, they said, should the United States explore alternative methods for achieving its liberalization objectives, including FTAs. In noting that the Round is scheduled to conclude in 1990, one participant said, "We should wait until 1990 and then evaluate what is possible and what isn't." However, many participants also noted that alternative approaches (including FTAs) should be judged on whether they improve trade prospects on a multilateral level.

A number of participants suggested that it is appropriate and desirable to study the idea of FTAs while the Round is ongoing, as this could provide an incentive to GATT negotiators to reach a successful conclusion. Others suggested that while the threat of an FTA may stimulate others to participate more seriously in the Uruguay Round, the threat could also be interpreted as another signal that the United States is abandoning multilateralism for bilateralism.

Several persons said that even if the Uruguay Round is successful, specific country goals not reached in the multilateral forum might then be accomplished through bilateral FTAs. Several participants commented that the United States should pursue bilateral FTAs because "world trade is moving toward bilateralism anyway."

A number of participants said that FTAs and the GATT are compatible and can be pursued simultaneously. Others thought that pursuing FTAs could hurt the multilateral trading system and the United States should forgo FTAs altogether and use only the GATT to pursue trade liberalization objectives. A small group of participants thought that even building the framework for FTA negotiations—particularly on the scale necessary for a Pacific Rim regional FTA—could harm the multilateral system and possibly derail the current Uruguay Round negotiations.

#### *Rely on the GATT, but use FTAs as fallback*

A recurrent theme in a majority of the interviews was that the United States must begin

to devote more attention to its trade options with the Pacific Rim countries because "they have growth, dynamism, and the technological innovation." However, the opinion was frequently expressed that FTAs are, at most, a second-best alternative to multilateralism. One participant echoed the views of many in saying, "maximum global trade. . . can best be achieved through an integrated, liberalized multilateral setting, rather than through a disintegrated series of bilateral or regional arrangements."

Many participants prefaced their remarks by saying they fully support the GATT and prefer the global approach to trade policy because the United States will have a better opportunity to achieve its liberalization objectives there. These participants felt that as long as the Round makes reasonable headway there is no reason to engage in bilateralism, but they also emphasized the point that if the Round is not successful, bilateral FTAs could be an effective alternative to achieve liberalization goals. In a submission, although noting that the issue of future FTAs will have to be addressed by the incoming administration, United States Trade Representative Clayton Yeutter wrote:

As we evaluate progress in achieving our objectives in the Uruguay Round, we may want to explore ways in which bilateral agreements can complement or enhance these efforts. When additional results can be achieved bilaterally, we should not hesitate to move in that direction—including, if appropriate, the negotiation of free trade agreements.<sup>1</sup>

A number of participants did not rule out the possibility of conducting FTA negotiations after the Uruguay Round with a view toward resolving outstanding trade issues. If properly constructed, they suggested, an FTA among like-minded countries could establish a precedent and influence others to move toward freer trade. Importantly, many individuals holding the view that FTAs are premature at this time and that the United States should first allow the Uruguay Round to play out before initiating FTA discussions, emphasized that the timing is crucial; FTA discussions now could derail the Uruguay Round.

#### *Pursue FTAs and GATT simultaneously*

A number of persons said that bilateral and multilateral approaches to trade liberalization are not necessarily incompatible and that FTAs could be pursued on a parallel track with the Uruguay Round without upsetting the multilateral negotiations. Persons who held this view generally believed that either regional or indivi-

<sup>1</sup> See Appendix E for a copy of Ambassador Yeutter's submission.

dual FTAs with the Pacific Rim countries would not be a substitute for liberalization under GATT but could provide the United States with leverage in dealing with other countries and thus could stimulate recalcitrant trade partners. As noted by a former U.S. negotiator:

FTAs are not designed to, nor do they have the effect of replacing the GATT system. They can, however, act to spur needed changes in the multilateral trading system. Multi-country negotiations have become increasingly complex, time-consuming, and slow to achieve the kind of far-reaching results the U.S. Government desires and the U.S. economy requires.

Several participants noted that negotiating FTAs would provide the opportunity for the United States to reassert its "leadership role" in the world trading system. One submission reads:

The United States used to be the unquestioned leader in the world trading system and the GATT. As such it could essentially dictate GATT policy and ensure the implementation of trade liberalizing measures. Today that situation has changed markedly. The EC, Japan and the [NIEs] are other powerful influences whose ideas regarding international trade rules often differ considerably from those of the United States. Developing countries generally have acted as a block to push their own trade agenda. . . . The United States needs to re-exert its leadership role in the world trading system.

In addition, a number of participants felt that FTAs could serve as "a demonstration of what free trade can do" and provide a model for new trade concepts and approaches that could be used as precedents for later implementation in the multilateral arena, for example in licensing or services.

A number of persons thought that movement now on bilateral FTAs would push GATT negotiations along; that the idea need not lie dormant, but should be allowed "to simmer to keep things going." One participant said, "if FTAs are used judiciously, they could have a positive effect on the [multilateral] system."

*Pursue the GATT only; FTAs will hurt the multilateral system*

A number of participants said they were generally amenable to any arrangement that opens markets, but they believed that talk about FTAs sends mixed signals and is thus detrimental to the multilateral trade negotiations process. These participants were concerned that U.S. interest in bilateral links through FTAs is already sending the message that the United States is

pessimistic about the outcome of the Uruguay Round. Moreover, regarding individual or regional FTAs with the Pacific Rim countries, numerous persons expressed a sentiment similar to a comment made by a senior U.S. official: "Dumb idea...not doable. The best shot is the GATT." Commented a trade policy analyst, "Bilateralism could lead to a mind-boggling proliferation of overlapping and retaliatory deals." Speaking before a gathering of trade experts, a former high-level U.S. negotiator said, "I am not convinced anymore that bilateral and multilateral approaches can prosper together. FTA has become an inside-the-beltway buzzword." Said a foreign government official, "Bilateralism has an invidious effect on the world trading system." Furthermore, it was noted by many participants that whereas the world trade community saw no threat from the United States' FTA agreements with Canada and Israel, it would most likely be different with the Pacific Rim countries. FTAs, they believed, would further politicize trade issues.

Yet, there was also an undercurrent of dissatisfaction with the GATT and multilateral trading system that pervaded many of the participant interviews and written submissions. One official made the observation that, "There is frustration in the United States that something needs to happen soon. GATT has not dealt with major issues." Said another, "Dissatisfaction with GATT is growing because it has not kept up with the times." In a written submission it was noted:

Almost all close observers of trade policy, whether advocating freer trade or more overt management of trade flows, are dissatisfied with the status quo. There is widespread pressure for new initiatives, and the only issue is the nature of those initiatives.

However, even the pessimists said that a stronger GATT system is still the best option for achieving trade liberalization objectives.

Quite a few participants were concerned about the bilateralization of world trade relations. As one businessman noted, "The multilateral system has worked fairly well up to this point. Negotiating FTAs would be a step backward. FTAs could result in trading blocks, which would complicate the trading system." Many persons said that the United States should continue to focus its efforts on the GATT rather than to "compartmentalize trade relationships" and pointed out that negotiations in a multilateral setting are no tougher or easier than those in a bilateral setting. As one participant noted, "In fact, multilateral talks are really just a series of bilateral deals."

A number of persons said that the argument that FTAs do not depart from the GATT is plausible, but on a wider scale, when many FTAs

are being done they do depart from the GATT and the multilateral trading system will break down. Some disagreed that the multilateral system works slowly, and said, "it works as fast as countries let it work." One foreign government official said, "The more we look at FTAs, the more logic comes back to the MTN approach." Moreover, a number of persons who said that they did not object to FTAs if they are GATT-consistent, also warned that they did not believe a GATT-consistent agreement could be negotiated with the Pacific Rim countries.

Another concern expressed by several participants was that the commitment to GATT by other countries could diminish if the United States were to push for bilateral agreements, especially since the United States was a leading advocate for the new Round. In a submission it was noted:

The United States has a major stake in the success of the Uruguay Round negotiations and in the integrity of the multilateral approach to the solution of international trade problems. We need to shore up the multilateral trading system, to strengthen and reinforce its disciplines, and to extend it to new areas. . . It would be a grave error to disperse our time and attention into bilateral agreements which would risk fragmenting the multilateral system.

For some of the Pacific Rim countries, an FTA was seen as detracting from the effects of the Round and presenting problems for these countries. It was believed that since the purpose of the Round and an FTA is trade liberalization, a combination of the two approaches might be more than some Pacific countries could handle politically. In addition, it was noted that many of these countries have a limited number of negotiators, and they will be working on the Round.

#### *The special case of Taiwan*

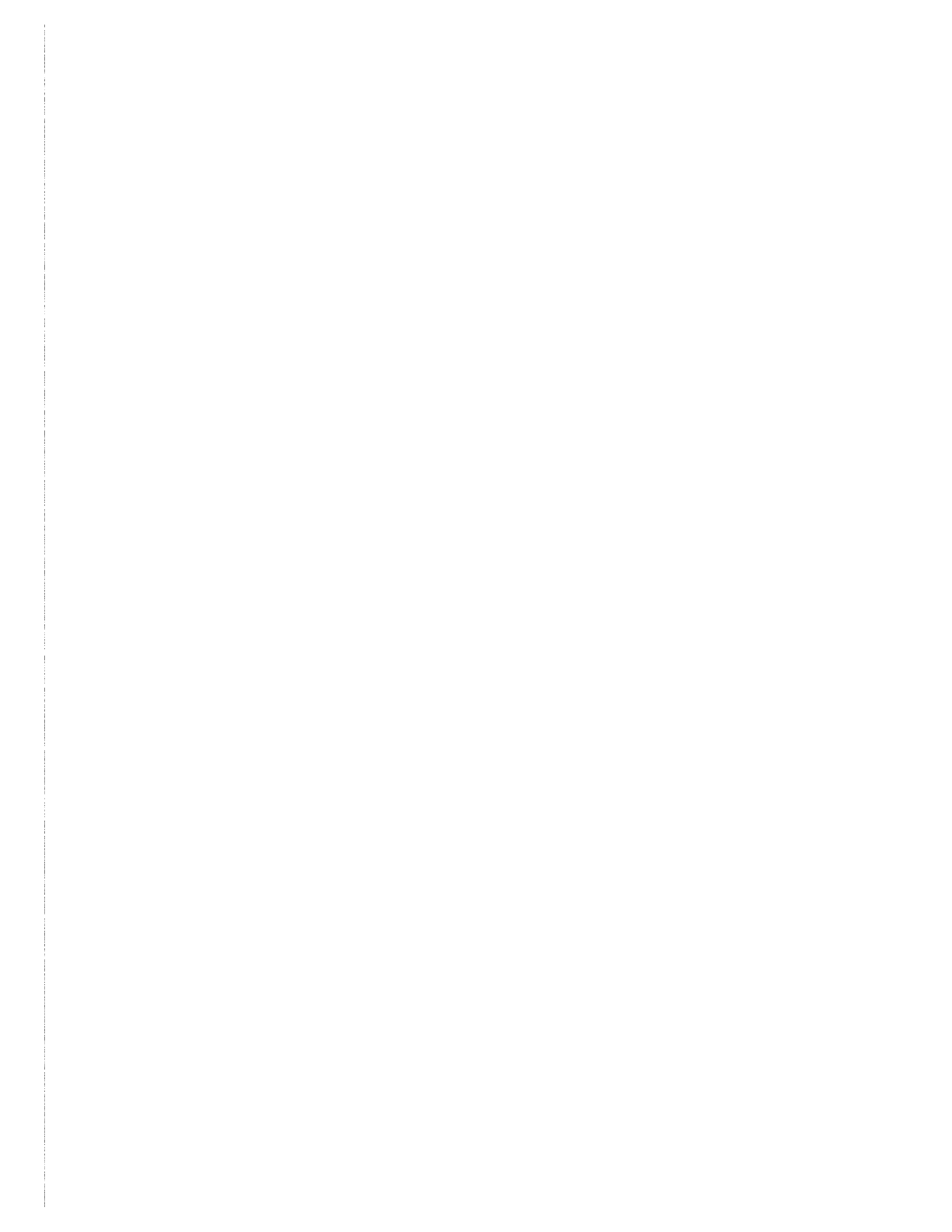
Since Taiwan is not a member of the GATT, many participants who commented on the possible effect of United States-Taiwan talks on the multilateral system did not feel there would be a strongly negative effect of such talks on the GATT system. Others suggested that because Taiwan is not a member of the GATT, bilateral FTA talks could be a useful "parallel track" to, and not a substitute for, multilateral trade negotiations, and as such, would not harm the GATT system. The United States will still need to negotiate a special accord with Taiwan after the Uruguay Round (as it did after the Tokyo Round) to apply the outcome of the round bilaterally. It was suggested that the United States could use that opportunity to expand the bilateral trade relationship further through negotiation of an FTA.





**APPENDIX A**  
**LETTER OF REQUEST FROM SENATE COMMITTEE ON FINANCE**

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LLOYD BENISEN TEXAS CHAIRMAN

SPARE M. MATSUDA HAWAII	BOB PACKWOOD OREGON
DANIEL PATRICK MOYNIHAN NEW YORK	BOB DOLE KANSAS
MAR BAUCUS MONTANA	WILLIAM V. ROY JR. DELAWARE
DAVID L. BORAH OREGON	JOHN C. DANFORTH MISSOURI
BILL BRADLEY NEW JERSEY	JOHN H. CHAFFEE RHODE ISLAND
GEORGE J. MITCHELL MAINE	JOHN HENNE PENNSYLVANIA
DAVID PRYOR ARKANSAS	MALCOLM WALLACE WYOMING
DONALD W. RIEGLE JR. MICHIGAN	DAVID DURKENBERGER MINNESOTA
JOHN S. ROCKEFELLER IV WEST VIRGINIA	WILLIAM L. ARMSTRONG COLORADO
TOM GASCHLE SOUTH CAROLINA	

# United States Senate

COMMITTEE ON FINANCE  
WASHINGTON, DC 20510-6200

August 3, 1988

JAMES C. GOULD STAFF DIRECTOR AND CHIEF COUNSEL  
ED MWALSKI MINORITY CHIEF OF STAFF

The Honorable  
Anne Brunsdale  
Acting Chairman  
United States International  
Trade Commission  
500 "E" Street, S.W.  
Washington, D.C. 20436

Docket NUMBER  <span style="font-size: 2em;">1461</span> <hr/> Office of the Secretary U.S. Trade Commission
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OFFICE OF THE CHAIRMAN

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RECORDED

Dear Madam Chairman:

I recently made a request to you on behalf of Senator Byrd and the Members of the Committee on Finance for the Commission to provide the Committee with a summary of the views of recognized authorities on U.S.-Japan relations concerning the pros and cons of entering into negotiations with Japan to explore the possibility of establishing a U.S.-Japan Free Trade Area. Many Members of the Committee have indicated an interest in a similar investigation to examine the feasibility and desirability of using the free trade area concept to develop a more comprehensive and fruitful approach to trading with other countries in the Pacific Rim.

As a result of this interest, the Commission is requested, pursuant to section 332(g) of the Tariff Act of 1930, to institute an investigation for the purpose of providing the Committee with a summary of the views of recognized authorities on U.S. trade relations with Pacific Rim countries concerning the pros and cons of entering into negotiations for a U.S.-Taiwan Free Trade Agreement, a U.S.-Korean Free Trade Agreement, a U.S.-ASEAN Free Trade Agreement, or a broader free trade arrangement for the Pacific countries in general, which interested market economy members could join.

OFFICE OF THE SECRETARY  
DOCKET/USITC

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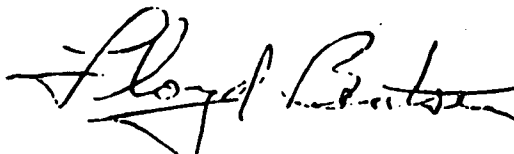
The Honorable  
Anne Brunsdale  
August 3, 1988  
Page Two

Such free trade agreements could include, in addition to the eventual complete elimination of all tariffs and other restrictive regulations of commerce on substantially all trade between the United States and these countries, the removal of barriers to investment and trade in services and the guarantee of adequate protection of intellectual property rights. If the experts believe that there are specific characteristics of the trade relationship between the United States and the subject countries which would make a free trade relationship more attractive or feasible between one or more of these countries than others or that would make a broader arrangement with Pacific Rim countries more appropriate, the report should include this information. Furthermore, where the experts identify problem areas that would render the completion of free trade agreements less than ideally effective, your report should clearly identify those problem areas and present their suggestions for alternative policy approaches for the United States.

It is expected that the Commission's report concerning these investigations will reflect the views of knowledgeable Government officials who have worked in the area of U.S.-Pacific Rim country relations, including those in the Office of the United States Trade Representative, scholars, private business officials, and others that could contribute to our assessment of this proposal.

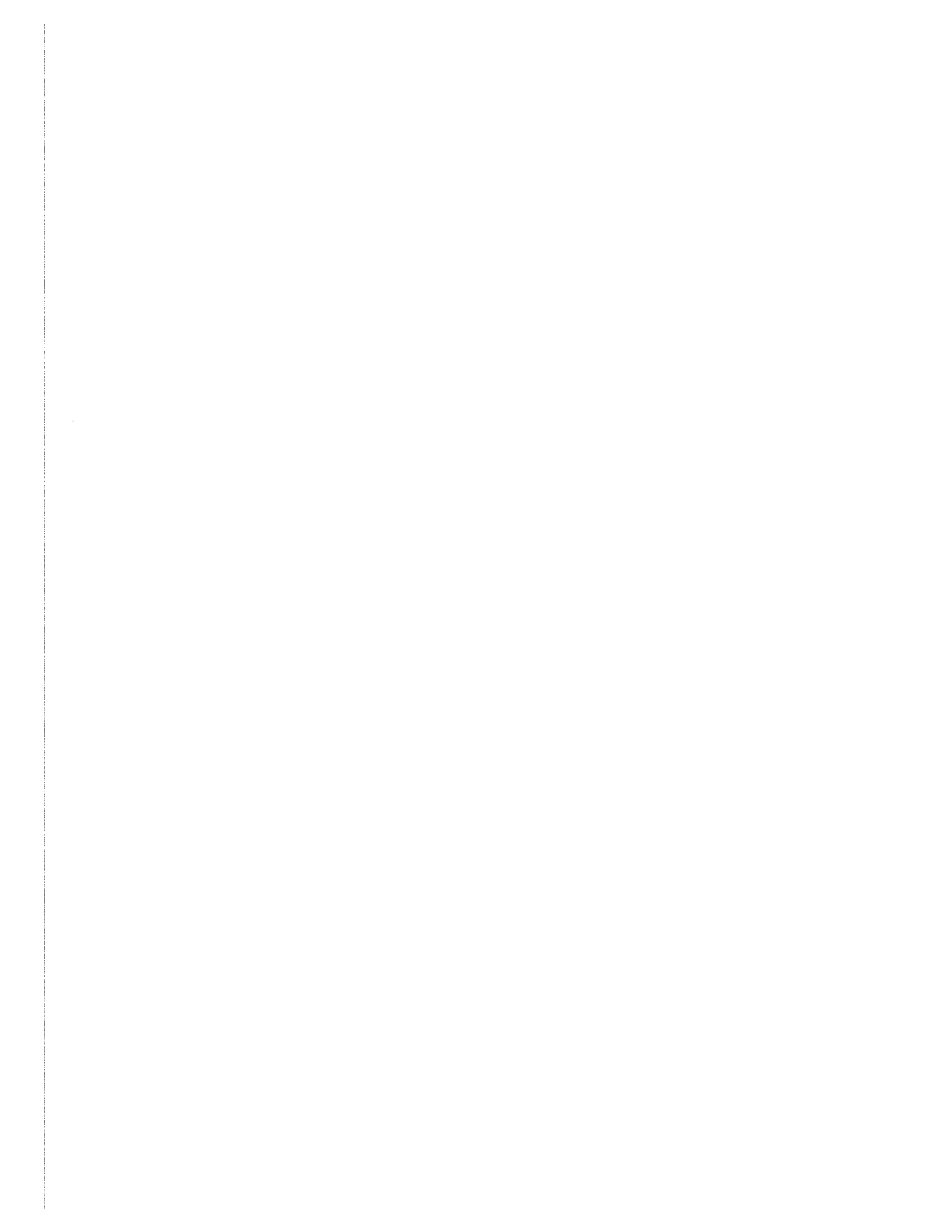
The Commission's report on these investigations should be submitted as soon as possible, but not later than six months after initiation of the investigation.

Sincerely,



Lloyd Bentsen  
Chairman

**APPENDIX B**  
*FEDERAL REGISTER NOTICE*



UNITED STATES INTERNATIONAL TRADE COMMISSION  
Washington, D.C. 20436

Investigation No. 332-259

Report on the Pros and Cons of entering into Negotiations  
on Free Trade Area Agreements with Taiwan,  
The Republic of Korea, and ASEAN, or the  
Pacific Rim region in general

AGENCY: United States International Trade Commission

ACTION: Institution of investigation, scheduling of hearing, and  
request for comments.

EFFECTIVE DATE: September 9, 1988

FOR FURTHER INFORMATION CONTACT: Constance A. Hamilton (202-252-1263),  
Trade Reports Division, Office of Economics, U.S. International Trade  
Commission, Washington, D.C. 20436

BACKGROUND: The Commission instituted investigation No. 332-259 following receipt of a letter dated August 4, 1988 from the Senate Committee on Finance requesting the Commission to conduct an investigation under section 332(g) of the Tariff Act of 1930 (19 U.S.C. 1332(g)) to provide a summary of the views of recognized authorities on U.S.-Pacific Rim trade relations on the pros and cons of entering into negotiations for a U.S.-Taiwan Free Trade Agreement, a U.S.-Korean Free Trade Agreement, a U.S.-ASEAN Free Trade Agreement, or a broader free trade arrangement for the Pacific countries in general, which interested market economy members could join. The Committee requested that the report be submitted no later than six months after initiation of the investigation.

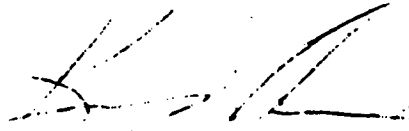
The Committee letter stated that such agreements could include, in addition to the eventual complete elimination of all tariffs and other restrictive regulations of commerce on substantially all trade between the United States and these countries, the removal of barriers to investment and trade in services and the guarantee of adequate protection of intellectual property rights.

The Committee also requested that if the experts believe there are specific characteristics of the trade relationship between the United States and the subject countries which would make a free trade relationship more attractive or feasible between one or more of these countries than others or that would make a broader arrangement with Pacific Rim countries more appropriate, the report should include this information. The Committee also requested that, where the experts identify problem areas that would render the completion of free trade agreements less than ideally effective, the report should clearly identify those problem areas and present the experts' suggestions for alternative policy approaches for the United States.

**PUBLIC HEARING:** A public hearing in connection with this investigation will be held in the Commission Hearing Room, 500 E Street, SW, Washington, D.C. 20436, beginning at 9:30 a.m. on November 29, 1988. All persons shall have the right to appear by counsel or in person, to present information, and to be heard. Requests to appear at the public hearing should be filed with the Secretary, United States International Trade Commission, 500 E Street, SW, Washington, D.C. 20436, no later than noon, November 21, 1988. The deadline for filing prehearing briefs (original and 14 copies) is November 21, 1988.

**WRITTEN SUBMISSIONS:** Interested persons are invited to submit written statements concerning the matters to be addressed in the report. Commercial or financial information that a party desires the Commission to treat as confidential must be submitted on separate sheets of paper, each clearly marked "Confidential Business Information" at the top. All submissions requesting confidential treatment must conform with the requirements of section 201.6 of the Commission's Rules of Practice and Procedure (19 CFR 201.6). All written submissions, except for confidential business information, will be made available for inspection by interested persons in the Office of the Secretary to the Commission. To be assured of consideration by the Commission, written statements relating to the Commission's report should be submitted at the earliest practical date and should be received no later than January 9, 1989. All submissions should be addressed to the Secretary to the Commission at the Commission's office in Washington, D.C.

By order of the Commission.



Kenneth R. Mason  
Secretary

Issued: September 9, 1988



**APPENDIX C**  
**LIST OF SUBMISSIONS AND HEARING PARTICIPANTS**



## SUBMISSIONS FOR THE RECORD

332-259

- Gerald Andersen,  
Executive Director, Neckwear Association of America Inc.
- Fritz E. Attaway,  
Vice President and Counsel, Motion Picture Export Association of America
- W. Baer,  
Executive Vice President, International Hardwood Products Association
- C. Fred Bergsten,  
Director, Institute for International Economics
- C. Edwin Brino,  
Vice President, Finance & Treasurer, Cornell-Dubilier
- Olivia Chiou,  
Chiao Tung Industrial Co., Ltd
- Wen-Yeong Chou,  
Chairman, Taipei Chamber of Commerce
- Joseph Cook,  
Executive Director, Work Glove Manufacturers Association
- Doral Cooper,  
President, C&M International, Ltd.
- Mitchell J. Cooper,  
Counsel on behalf of The Rubber and Plastic Footwear Manufacturers Association
- Domenic DiPaola,  
International President, International Leather Goods, Plastics and Novelty Workers Union
- Robert Ermatinger,  
Executive Vice President, The Luggage and Leather Goods Manufacturers of America
- Fawn K. Evenson,  
President, Footwear Industries of America
- Richard M. Fairbanks III,  
President, U.S. National Committee for Pacific Economic Cooperation
- Mathilde Genovese,  
Vice Chairman, Asia-Pacific Council of American Chambers of Commerce
- Carolyn B. Gleason,  
Heron, Burchette, Ruckert, and Rothwell, on behalf of Blue Diamond Growers
- Carolyn B. Gleason,  
Heron, Burchette, Ruckert, and Rothwell, on behalf of California-Arizona Citrus League
- Carolyn B. Gleason,  
Heron, Burchette, Ruckert, and Rothwell, on behalf of Welch Foods, Inc.
- Maurice Greenberg,  
President, American International Group, Inc.

Arthur Gundersheim,  
Assistant to the President, Amalgamated Clothing and Textile Workers Union

Cheng-Tsang Hsu,  
Chairman, Taiwan Regional Hand Tools Association

Joseph Hsu,  
General Manager, ABC Taiwan Electronics Corporation

T.W. Hu,  
President, United Friends, Inc.

Edward Hudgins,  
Director, Center for International Economic Growth, The Heritage Foundation

Douglas T. Hung,  
Director, Liaison Center of The General Chamber of Commerce of the Republic of China

Ann Ottoson King,  
Leighton and Regnery, on behalf of The American Cordage and Netting Manufacturers

Lewis, Eckert, Robb, & Co.,  
Government Relations Consultant, American Mushroom Institute

Julian C. Morris,  
President, Automotive Parts & Accessories Association

Harry Reinsch,  
Bechtel Energy Cooperation

George Seignious II,  
President, The Atlantic Council of The United States

Ke-Sheng Sheu,  
Director, Coordination Council for North American Affairs

David J. Steinberg,  
President, U.S. Council for an Open World Economy

Lawrence S. Ting,  
Chairman, The Taiwan Plastics Industry Association

C. William Verity,  
Secretary of Commerce

Ron Walker,  
Executive Director, The National Potato Council

C.Y. Wang,  
Vice President, China Steel Corporation, on behalf of Taiwan Steel and Iron Industries Association

Mark Y.Y. Wang,  
Executive Secretary, Taiwan Toy Manufacturers Association

Jonathan C.Y. Woo,  
Importers and Exporters Association of Taipei

Han Xu,  
Ambassador, The Embassy of The People's Republic of China

Clayton Yeutter,  
United States Trade Representative

## TENTATIVE CALENDAR OF PUBLIC HEARING

Those listed below are scheduled to appear as witnesses at the United States International Trade Commission's hearing:

Subject : REPORT ON THE PROS AND CONS OF ENTERING INTO NEGOTIATIONS ON FREE TRADE AREA AGREEMENTS WITH TAIWAN, THE REPUBLIC OF KOREA, AND ASEAN, OR THE PACIFIC RIM REGION IN GENERAL

Inv. No. : 332-259

Date and Time : November 29, 1988 - 9:30 a.m.

Sessions will be held in connection with the investigation in the Main Hearing Room 101 of the United States International Trade Commission, 500 E Street, S.W., in Washington, D.C.

<u>WITNESS AND ORGANIZATION</u>	<u>TIME CONSTRAINTS</u>
U. S. Council for an Open World Economy, Inc. Alexandria, Virginia  David J. Steinberg, President	10 Minutes
C & M International Ltd. Washington, D.C.  Doral S. Cooper, President	10 Minutes
Institute for International Economics Washington, D.C.  C. Fred Bergsten, Director	10 Minutes
The Heritage Foundation Washington, D.C.  Dr. Edward Hudgins, Director of the Center for International Economic Growth	10 Minutes

- more -

WITNESS AND ORGANIZATION

TIME  
CONSTRAINTS

Importers and Exporters Association of Taipei  
Taiwan, Republic of China  
Monterey Park, CA

10 Minutes

Johnathan C. Y. Woo,  
Representative in the U.S.

Coordination Council for North American Affairs  
Economic Division  
Washington, D.C.  
on behalf of

10 Minutes

The Board of Foreign Trade in Taipei  
Ke-sheng Sheu, Director

Welch's  
Concord, MA

10 Minutes

William C. Hewins, Vice President,  
International Division;  
and  
Carolyn B. Gleason, Counselor at Law,  
Heron, Burchette, Ruckert & Rothwell

Mitchell J. Cooper Law Offices  
Washington, D.C.  
on behalf of

10 Minutes

Rubber and Plastic Footwear Manufacturers Association

Mitchell J. Cooper )--OF COUNSEL

Davis Wright & Jones  
Washington, D.C.  
on behalf of

20 Minutes

Taiwan Steel and Iron Industries Association

Taiwan Industrial Fasteners Institute

David Simon )--OF COUNSEL

General Chamber of Commerce of  
Republic of China, San Francisco, CA

10 Minutes

Douglas T. Hung, Director

- end -

**APPENDIX D  
TRADE DATA**





Table D-1

Imports for consumption at customs value from Taiwan, 1985-87, January-September 1987, and January-September 1988

(Thousands of dollars)

TSUSA commodity	1985	1986	1987	January-September—	
				1987	1988
70056 Footware, 90% rubber or plastic .....	963,621	1,173,108	1,331,681	1,039,717	933,899
67630 Office machines, n.s.p.f .....	295,755	498,530	708,946	504,997	552,763
67654 Parts of A.D.P. machines .....	( <sup>1</sup> )	300,390	557,052	370,355	505,064
72735 Furniture, of wood, not chairs .....	253,125	395,617	500,621	380,159	320,678
38480 Women's man-made fiber knit blouse .....	<sup>2</sup> 339,665	439,342	476,663	387,576	250,320
67850 Machines, n.s.p.f., and parts .....	293,493	312,740	443,586	334,535	287,810
70045 Footware, leather, not for men, .....	229,801	347,769	428,357	338,111	305,944
68492 Television receivers, complete .....	308,365	420,828	421,269	319,616	203,626
70035 Footwear, leather, other, for men .....	341,849	373,767	415,392	302,448	394,728
66106 Fans and blowers, and parts, n.s.p.f .....	326,765	344,515	384,477	344,983	337,708
67615 Accounting, computing, and other .....	190,331	229,587	359,022	231,491	403,682
72770 Furniture, n.s.p.f., other .....	198,944	273,660	346,192	255,412	246,798
68774 Monolithic integrated circuits .....	207,464	230,539	334,425	241,123	340,806
73520 Puzzles, games, etc .....	172,768	279,304	306,797	227,184	194,463
38195 Men's man-made fiber apparel .....	<sup>3</sup> 251,851	283,188	287,368	217,265	192,500
77235 Curtains, drapes, like furnishing .....	126,234	183,563	281,633	199,522	192,708
68590 Electrical switches .....	135,375	181,987	277,710	200,739	261,823
68508 Television apparatus, other .....	215,180	157,270	255,805	186,801	213,016
68470 Microphones .....	163,172	177,642	254,667	189,857	197,719
70641 Luggage and handbags of textiles .....	189,801	203,478	233,262	181,559	151,154
Total of items shown .....	5,203,558	6,806,827	8,604,925	6,453,451	6,487,209
Total other .....	11,150,795	12,963,785	15,970,757	11,920,554	12,141,813
Total, U.S. Imports from Taiwan .....	16,354,353	19,770,612	24,575,682	18,374,005	18,629,022

<sup>1</sup> Prior to Feb. 1, 1986, trade for T.S.U.S. item 676.54 was reported under 676.52 (part). Since those portions of T.S.U.S.A. items 676.5230 (Jan. 1984-Dec. 1985) and 676.5215 (Jan. 1986) assigned to 676.54 are not known, these items were excluded from the data above.

<sup>2</sup> Prior to Sept. 1, 1985, trade for T.S.U.S. item 384.80 was reported under 383.80 (part).

<sup>3</sup> Prior to Sept. 1, 1985, trade for T.S.U.S. item 381.95 was reported under 379.95 (part).

Note: Compiled from official statistics of the U.S. Department of Commerce. Top 20 commodities sorted by imports for consumption, customs value in 1987.

Table D-2

U.S. domestic exports at F.A.S. value to Taiwan, 1985-87, January-September 1987, and January-September 1988

(Thousands of dollars)

Schedule B commodity	1985	1986	1987	January-September—	
				1987	1988
60520 Gold or silver bullion, dore, .....	891	1,700	564,099	1,660	2,456,930
68760 Electronic tubes, not T.V. ....	183,275	283,893	489,469	335,917	437,329
17541 Soybeans, other .....	321,720	358,750	379,935	286,289	347,840
13034 Corn, seed for planting purposes .....	374,299	271,002	250,825	177,425	351,436
52131 Coal .....	134,044	157,377	192,156	142,642	147,261
67655 Parts of office mach, other .....	107,664	134,465	191,155	135,792	176,590
12014 Whole cattle hides .....	112,247	155,687	172,259	135,286	131,782
30010 Cotton, staple <=1 1/8 inch .....	112,386	36,721	135,011	111,977	68,757
40422 Polycarboxylic acids .....	92,527	132,216	133,890	98,310	127,856
17065 Cigarettes .....	4,890	4,355	118,767	94,491	91,783
67628 Digital C.P.U.'s .....	85,293	87,686	116,294	78,479	101,252
40405 Hydrocarbons, exc derivatives .....	4,047	38,688	111,574	67,760	124,574
69210 Passenger cars .....	6,314	10,645	111,348	56,422	319,580
13065 Wheat .....	99,082	101,505	103,578	74,471	93,451
68462 Telephonic aparatus .....	47,666	39,549	101,845	57,380	75,748
25004 Waste paper .....	61,697	74,233	89,692	67,229	82,523
68590 Electrical switches .....	50,327	71,648	83,117	59,381	79,327
47507 Crude petroleum .....	20,676	85,321	82,435	51,849	130,677
25002 Wood pulp of fibrous materials .....	34,197	57,778	81,741	55,688	73,561
69465 Aircraft, parts .....	253,570	129,366	77,082	58,332	53,396
Total of items shown .....	2,106,811	2,232,587	3,586,272	2,146,780	5,471,654
Total other .....	2,230,688	2,824,538	3,432,967	2,425,005	3,699,607
Total, U.S. exports to Taiwan .....	4,337,499	5,057,124	7,019,239	4,571,785	9,171,261

Note: Compiled from official statistics of the U.S. Department of Commerce. Top 20 commodities sorted by domestic exports, F.A.S. value in 1987.

Table D-3

Imports for consumption at customs value from South Korea, 1985-87, January-September 1987, and January-September 1988

(Thousands of dollars)

TSUSA commodity	1985	1986	1987	January-September—	
				1987	1988
69210 Motor vehicles, other .....	5,846	798,685	2,062,209	1,482,272	1,870,317
70035 Footwear, leather, n.s.p.f., men .....	528,171	663,083	756,941	531,228	810,021
68774 Monolithic integrated circuits .....	409,307	436,375	656,015	467,393	820,411
73730 Stuffed toy figures, >\$.10/inch .....	227,056	357,467	442,859	341,587	216,523
70045 Footware, leather, not for men .....	289,741	462,631	442,817	316,143	490,376
79176 Wearing apparel, leather, n.s.p.f. ....	225,407	241,068	390,325	271,844	413,253
68425 Microwave ovens .....	219,648	292,411	366,201	271,779	255,634
38195 Men's man-made fiber apparel .....	<sup>1</sup> 330,000	<sup>1</sup> 333,256	359,516	275,909	272,149
67850 Machines, n.s.p.f., and parts .....	202,544	221,415	340,792	250,368	310,698
68540 Tape recorders & dictation machines .....	172,753	307,099	337,687	256,858	300,338
68492 Television receivers, complete .....	247,363	357,109	336,870	252,425	167,587
67630 Office machines, n.s.p.f. ....	160,696	158,551	299,619	202,375	321,383
67615 Accounting, computing machines .....	59,550	205,745	261,993	148,423	264,341
38480 Women's man-made fiber knit blouse .....	<sup>2</sup> 193,199	246,511	248,217	222,013	142,270
70056 Footware, 90% rubber or plastic .....	49,184	128,763	186,220	148,126	84,853
38453 Women's apparel, except cotton .....	<sup>3</sup> 145,553	253,736	172,437	147,015	61,126
77251 Pneumatic tires, other .....	181,608	162,926	163,554	126,276	125,934
33859 Woven fabrics, man-made fibers .....	<sup>4</sup> 125,923	<sup>4</sup> 158,213	<sup>4</sup> 158,449	<sup>4</sup> 120,891	145,679
68458 Telephone sets and parts .....	75,958	106,968	146,240	104,096	96,018
72445 Magnetic recording media, no material .....	98,615	168,977	142,802	106,737	126,178
<b>Total of items shown .....</b>	<b>3,948,122</b>	<b>6,060,988</b>	<b>8,271,764</b>	<b>6,043,759</b>	<b>7,295,089</b>
<b>Total other .....</b>	<b>6,038,241</b>	<b>6,621,831</b>	<b>8,616,389</b>	<b>6,423,701</b>	<b>7,472,964</b>
<b>Total, U.S imports from South Korea .....</b>	<b>9,986,363</b>	<b>12,682,819</b>	<b>16,888,153</b>	<b>12,467,460</b>	<b>14,768,053</b>

<sup>1</sup> Prior to Sept. 1, 1985, trade for T.S.U.S. item 381.95 was reported under 379.95 (part).<sup>2</sup> Prior to Sept. 1, 1985, trade for T.S.U.S. item 384.80 was reported under 383.80 (part).<sup>3</sup> Prior to Sept. 1, 1985, trade for T.S.U.S. item 384.53 was reported under 383.52 (part).<sup>4</sup> Statistical reporting numbers under T.S.U.S. 338.50 were reissued with different commodity coverage on Apr. 1, 1985. T.S.U.S. item 338.59 was established to provide reporting numbers distinct from those used prior to this date. Trade carryovers of \$33,998, \$24,955, and \$23,355 were reported in 1986, 1987, and Jan.-Sept. 1987 respectively for item 338.50, and included above.

Note: Compiled from official statistics of the U.S. Department of Commerce. Top 20 commodities sorted by imports for consumption, customs value in 1987.

Table D-4

U.S. domestic exports at F.A.S. value to South Korea, 1985-87, January-September 1987, and January-September 1988

(Thousands of dollars)

Schedule B commodity	1985	1986	1987	January-September—	
				1987	1988
12014 Whole cattle hides .....	267,353	445,780	577,469	432,736	507,522
68760 Electronic tubes, not T.V. ....	436,960	467,859	566,972	411,977	526,290
13034 Corn, seed for planting purposes .....	209,868	129,956	356,490	256,510	328,431
30010 Cotton, staple <=1 1/8 inch .....	332,691	142,066	289,213	193,005	326,099
17541 Soybeans, other .....	185,476	206,091	232,188	158,216	183,850
69465 Aircraft, parts .....	274,543	209,951	215,075	157,194	217,660
13065 Wheat .....	270,158	240,388	213,349	167,113	217,335
60708 Carbon steel and iron .....	155,631	239,278	212,007	164,869	193,462
25002 Wood pulp of fibrous materials .....	77,099	117,540	181,501	133,156	181,699
67655 Parts of office mach, other .....	103,204	119,443	176,179	116,777	202,137
52131 Coal .....	157,087	158,162	171,735	119,136	125,867
20035 Logs .....	98,141	105,718	158,375	107,950	186,075
67850 Machines, n.s.p.f., and parts .....	160,740	126,892	149,513	100,500	207,900
47507 Crude petroleum .....	214,160	53,539	123,403	82,596	38,058
25004 Waste paper .....	72,318	103,539	122,164	87,491	115,304
69229 Chassis, parts .....	14,856	29,326	96,029	81,363	56,179
67628 Digital C.P.U.'s .....	69,116	76,157	92,641	70,158	89,037
68560 Radio navigation aids .....	19,987	23,057	88,461	67,043	27,714
40422 Polycarboxylic acids .....	63,038	72,282	88,399	65,631	87,068
69440 Aircraft .....	211,432	54,432	85,302	81,653	189,410
<b>Total of items shown .....</b>	<b>3,393,859</b>	<b>3,121,456</b>	<b>4,196,465</b>	<b>3,055,075</b>	<b>4,007,097</b>
<b>Total other .....</b>	<b>2,272,644</b>	<b>2,674,248</b>	<b>3,289,599</b>	<b>2,470,798</b>	<b>3,594,294</b>
<b>Total, U.S. exports to South Korea .....</b>	<b>5,666,503</b>	<b>5,795,704</b>	<b>7,486,064</b>	<b>5,525,874</b>	<b>7,601,391</b>

Note: Compiled from official statistics of the U.S. Department of Commerce. Top 20 commodities sorted by domestic exports, F.A.S. value in 1987.

Table D-5

Imports for consumption at customs value from ASEAN countries,<sup>1</sup> 1985-87, January-September 1987, and January-September 1988

(Thousands of dollars)

TSUSA commodity	1985	1986	1987	January-September—	
				1987	1988
68774 Monolithic integrated circuits .....	2,023,904	2,067,349	2,467,723	1,813,780	2,340,720
67654 Parts of A.D.P. machines .....	( <sup>2</sup> )	1,140,067	1,782,517	1,256,141	2,014,048
47510 Crude petroleum, >=25 degs a.p.l. ....	3,135,156	1,805,394	1,525,556	1,192,813	824,591
44605 Natural rubber not containing .....	590,879	544,612	675,055	493,331	658,937
24017 Plywood, with a face ply of wood .....	211,362	251,931	323,185	241,526	227,011
47505 Crude petroleum, <25 degs a.p.l. ....	235,883	231,373	239,367	166,624	103,110
67615 Accounting, computing, and other .....	59,663	147,309	229,853	159,331	218,752
68777 Other integrated circuits .....	42,036	120,182	225,769	155,760	156,678
67850 Machines, n.s.p.f. ....	72,756	80,228	210,461	143,639	228,253
80000 U.S. goods returned .....	179,816	159,634	204,973	142,650	204,549
68492 Television receivers, complete .....	119,863	137,175	203,103	147,635	141,034
17617 Coconut oil .....	245,072	161,424	177,524	114,580	160,967
67630 Office machines, n.s.p.f. ....	74,069	105,324	176,745	134,438	160,429
38480 Women's man-made fiber knit blouse .....	<sup>3</sup> 123,034	143,194	165,993	137,562	115,231
16010 Coffee, crude, roasted or ground .....	234,531	366,949	160,487	124,161	132,808
47565 Natural gas condensate, other .....	189,280	161,227	158,232	113,324	135,439
11445 Shellfish other than clams, crabs .....	119,831	130,963	154,799	122,684	136,543
38141 Men's other cotton knit shirts .....	<sup>4</sup> 80,589	97,701	144,559	104,133	108,149
14898 Pineapples, prepared or preserved .....	135,524	144,103	141,459	112,732	110,472
38491 Women's other (not knit) apparel .....	46,402	137,974	132,778	98,057	103,306
<b>Total of items shown .....</b>	<b>7,919,650</b>	<b>8,134,114</b>	<b>9,500,138</b>	<b>6,974,902</b>	<b>8,281,027</b>
<b>Total other .....</b>	<b>6,741,296</b>	<b>6,068,126</b>	<b>7,389,158</b>	<b>5,375,254</b>	<b>6,865,319</b>
<b>Total, U.S. Imports from ASEAN countries .....</b>	<b>14,660,946</b>	<b>14,202,239</b>	<b>16,889,296</b>	<b>12,350,156</b>	<b>15,146,346</b>

<sup>1</sup> Includes Brunei, Indonesia, Malaysia, Philippines, Singapore, Thailand.<sup>2</sup> Prior to Feb. 1, 1986, trade for T.S.U.S. items 676.54 was reported under 676.52 (part). Since those portions of T.S.U.S.A. items 676.5230 (Jan. 1984-Dec. 1985) and 676.5215 (Jan. 1986) assigned to 676.54 are not known, these items were excluded from the data above.<sup>3</sup> Prior to Sept. 1, 1985, trade for T.S.U.S. item 384.80 was reported under 383.80 (part).<sup>4</sup> Prior to Sept. 1, 1985, trade for T.S.U.S. item 381.41 was reported under 379.40 (part).

Note: Compiled from official statistics of the U.S. Department of Commerce. Top 20 commodities sorted by imports for consumption, customs value in 1987.

Table D-6

U.S. domestic exports at F.A.S. value to ASEAN countries,<sup>1</sup> 1985-87, January-September 1987, and January-September 1988

(Thousands of dollars)

Schedule B commodity	1985	1986	1987	January-September—	
				1987	1988
68760 Electronic tubes, not T.V . . . . .	1,771,993	2,119,824	2,597,535	1,901,676	2,146,131
67655 Parts of office mach, other . . . . .	383,081	465,508	704,871	482,797	792,978
69440 Aircraft . . . . .	437,970	477,981	506,220	163,160	160,113
69465 Aircraft, parts . . . . .	254,796	391,075	342,043	251,944	282,287
66054 Parts of comp-ignition engines . . . . .	149,247	156,727	215,882	149,447	157,996
30010 Cotton, staple <=1 1/8 inch . . . . .	118,084	66,489	162,843	119,401	158,165
67850 Machines, n.s.p.f., and parts . . . . .	152,875	144,480	156,968	109,569	140,600
13065 Wheat . . . . .	199,170	193,939	156,335	117,602	123,970
66405 Mechanical shovels, n.s.p.f . . . . .	294,675	238,588	156,145	112,148	184,524
43310 Chemical mixtures & preparation . . . . .	109,326	125,478	145,402	112,464	119,445
68590 Electrical switches . . . . .	95,248	109,139	140,856	103,293	126,443
81890 General merchandise . . . . .	260,415	271,506	128,383	95,191	121,222
67628 Digital C.P.U.'s . . . . .	132,552	107,305	122,299	83,852	144,386
44417 Polypropylene resins . . . . .	36,314	91,170	115,409	91,535	88,940
71250 Instr for measuring electrical . . . . .	63,191	86,843	113,921	80,828	109,039
68527 Radiotelegraphics, other . . . . .	52,673	68,431	89,089	65,487	77,561
17065 Cigarettes . . . . .	62,782	63,715	79,096	56,628	70,785
25278 Unbleached kraft packaging paper . . . . .	33,853	56,755	76,912	58,222	51,699
17033 Cigarette leaf . . . . .	120,645	93,285	73,576	56,527	67,279
72445 Magnetic recording media, blank . . . . .	12,897	18,947	65,238	42,519	150,565
<b>Total of items shown . . . . .</b>	<b>4,541,788</b>	<b>5,147,187</b>	<b>6,149,023</b>	<b>4,254,291</b>	<b>5,274,128</b>
<b>Total other . . . . .</b>	<b>3,145,591</b>	<b>3,072,066</b>	<b>3,463,014</b>	<b>2,444,892</b>	<b>3,600,480</b>
<b>Total, U.S. exports to ASEAN countries . . . . .</b>	<b>7,687,378</b>	<b>8,219,252</b>	<b>9,612,037</b>	<b>6,699,182</b>	<b>8,874,608</b>

<sup>1</sup> Includes Brunei, Indonesia, Malaysia, Philippines, Singapore, Thailand.<sup>2</sup> Prior to Jan. 1, 1987, Schedule B item 818.90 included only general merchandise valued \$1,000 or less.

Note: Compiled from official statistics of the U.S. Department of Commerce. Top 20 commodities sorted by domestic exports, F.A.S. value in 1987.

Table D-7

Imports for consumption at customs value from Pacific Rim countries,<sup>1</sup> 1985-87, January-September 1987, and January-September 1988

(Thousands of dollars)

TSUSA commodity	1985	1986	1987	January-September—	
				1987	1988
68774 Monolithic integrated circuits .....	2,720,046	2,779,677	3,530,586	2,571,313	3,616,707
67654 Parts of A.D.P. machines .....	( <sup>2</sup> )	1,850,536	2,830,427	1,979,355	2,979,667
69210 Motor vehicles, other .....	9,776	801,621	2,072,215	1,490,816	1,882,857
47510 Crude petroleum, >=25 degs a.p.l .....	3,581,780	2,025,309	1,830,035	1,426,766	1,044,376
70056 Footwear, 90% rubber or plastic .....	1,040,680	1,328,975	1,550,026	1,210,485	1,054,931
67630 Office machines; n.s.p.f .....	592,346	849,621	1,286,771	913,121	1,116,431
70035 Footwear, leather, other, for men .....	883,679	1,057,978	1,188,526	843,459	1,246,585
38480 Women's man-made fiber knit blouse .....	<sup>3</sup> 811,170	1,040,122	1,111,370	918,433	625,888
67850 Machines, n.s.p.f .....	643,943	679,383	1,091,594	798,755	889,376
10610 Beef and veal, fresh, chilled, .....	792,179	828,396	1,060,630	897,681	1,038,005
68492 Television receivers, complete .....	704,139	985,417	1,008,749	761,384	524,196
70045 Footwear, leather, not for men .....	584,776	901,803	983,205	734,625	914,618
67615 Accounting, computing, and other .....	325,970	611,290	914,398	573,398	995,484
38195 Men's man-made fiber apparel .....	<sup>4</sup> 747,445	734,840	754,164	569,974	557,308
44605 Natural rubber not containing .....	594,186	545,101	676,957	494,533	659,308
73730 Stuffed toy figures, >\$.10/inch .....	357,811	553,899	647,589	505,959	288,042
80000 U.S. goods returned .....	541,703	668,404	636,995	480,595	531,296
72735 Furniture, of wood, not chairs .....	331,915	500,035	632,044	472,869	439,681
68590 Electrical switches .....	313,975	397,393	581,556	418,416	562,082
68458 Telephone sets and parts .....	291,047	532,869	581,086	426,080	414,754
Total of items shown .....	15,868,565	19,672,667	24,968,923	18,488,131	21,381,593
Total other .....	37,519,595	39,902,821	47,765,141	35,502,004	38,587,302
Total, U.S. Imports from Pacific Rim .....	53,388,160	59,575,489	72,734,064	53,990,136	59,968,895

<sup>1</sup> Includes South Korea, Taiwan, Brunei, Indonesia, Malaysia, Philippines, Singapore, Thailand, Hong Kong, Macao, Papua New Guinea, Australia, New Zealand, and other Pacific Islands group (Nauru, Fiji, and Tonga). Island territories of Australia and New Zealand are also included.

<sup>2</sup> Prior to Feb. 1, 1986, trade for T.S.U.S. items 676.54 was reported under 676.52 (part). Since those portions of T.S.U.S.A. items 676.5230 (Jan. 1984-Dec. 1985) and 676.5215 (Jan. 1986) assigned to 676.54 are not known, these items were excluded from the data above.

<sup>3</sup> Prior to Sept. 1, 1985, trade for T.S.U.S. item 384.80 was reported under 383.80 (part).

<sup>4</sup> Prior to Sept. 1, 1985, trade for T.S.U.S. item 381.95 was reported under 379.95 (part).

Note: Compiled from official statistics of the U.S. Department of Commerce. Top 20 commodities sorted by imports for consumption, customs value in 1987.

Table D-8

U.S. domestic exports at F.A.S. value to Pacific Rim countries,<sup>1</sup> 1985-87, January-September 1987, and January-September 1988

(Thousands of dollars)

Schedule B commodity	1985	1986	1987	January-September—	
				1987	1988
68760 Electronic tubes, not T.V . . . . .	2,572,385	3,050,706	3,889,582	2,813,300	3,389,754
67655 Parts of office mach, other . . . . .	1,096,315	1,191,884	1,616,216	1,133,505	1,704,861
69465 Aircraft, parts . . . . .	1,294,210	1,335,011	1,317,777	953,100	995,830
69440 Aircraft . . . . .	1,266,117	1,709,844	1,223,635	781,327	680,498
12014 Whole cattle hides . . . . .	383,844	606,427	757,481	573,095	641,668
67628 Digital C.P.U.'s . . . . .	646,513	618,159	730,860	523,450	683,798
17541 Soybeans, other . . . . .	518,078	579,408	650,830	449,615	607,354
13034 Corn, seed for planting purpose . . . . .	588,985	401,856	642,756	435,314	704,368
30010 Cotton, staple <=1 1/8 inch . . . . .	580,812	246,928	605,703	435,523	568,625
60520 Gold or silver bullion, dore, . . . . .	21,680	2,042	579,964	11,961	2,781,227
13065 Wheat . . . . .	583,680	549,827	489,411	369,218	449,202
17065 Cigarettes . . . . .	246,168	271,904	474,519	336,900	465,706
66054 Parts of comp-ignition engines . . . . .	342,817	339,081	469,790	337,250	369,423
81890 General merchandise . . . . .	<sup>2</sup> 225,737	<sup>2</sup> 257,345	467,973	348,486	426,869
67850 Machines, n.s.p.f. and parts . . . . .	430,792	405,767	446,068	303,632	493,776
68590 Electrical switches . . . . .	260,158	321,393	406,076	292,713	398,242
67627 Digital machines . . . . .	228,676	290,675	364,310	265,930	317,613
52131 Coal . . . . .	294,355	329,410	364,083	261,944	278,051
66405 Mechical shovels, n.s.p.f . . . . .	497,648	455,376	342,285	246,472	361,772
43310 Chemical mixtures and preparation . . . . .	238,424	268,800	336,106	259,413	280,534
Total of items shown . . . . .	12,317,395	13,231,846	16,175,425	11,132,149	16,599,174
Total other . . . . .	13,803,341	14,780,751	17,880,399	12,960,456	18,340,737
Total, U.S. exports to Pacific Rim . . . . .	26,120,735	28,012,597	34,055,824	24,092,604	34,939,547

<sup>1</sup> Includes South Korea, Taiwan, Brunei, Indonesia, Malaysia, Philippines, Singapore, Thailand, Hong Kong, Macao, Papua New Guinea, Australia, New Zealand, and other Pacific Islands group (Nauru, Fiji, and Tonga). Island territories of Australia and New Zealand are also included.

<sup>2</sup> Prior to Jan. 1, 1987, Schedule B item 818.90 included only general merchandise valued \$1,000 or less.

Note: Compiled from official statistics of the U.S. Department of Commerce. Top 20 commodities sorted by domestic exports, F.A.S. value in 1987.



**APPENDIX E**  
**SUBMISSION FROM UNITED STATES TRADE REPRESENTATIVE**  
**CLAYTON YEUTTER**



THE UNITED STATES TRADE REPRESENTATIVE  
WASHINGTON  
20506

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Mr. Kenneth R. Mason  
Secretary  
United States International Trade Commission  
500 E Street, S.W.  
Washington, D.C. 20436

Dear Mr. Mason:

I am writing in response to your letter dated October 4 in which you request our views on the pros and cons of entering into negotiations for free trade agreements with Taiwan, Korea, and ASEAN, or a broader free trade arrangement for the Pacific Rim region in general, pursuant to the Commission's Notice of Investigation No. 332-259.

As I stated in my response to your earlier request for our views on the negotiation of a free trade agreement with Japan, this Administration is deeply committed to the ongoing multilateral GATT trade negotiations in the Uruguay Round. We strongly believe that this effort will result in liberalization of trade in goods and services, including agriculture, improved intellectual property protection, and strengthened disciplines over international investment measures. This commitment to the multilateral approach has been held by previous administrations as well, and all have placed high priority on multilateral trade negotiations conducted in the GATT.

We are now in the midst of moving the Uruguay Round negotiations forward to what we hope will be a productive mid-term ministerial review in Montreal in December. This meeting should establish the framework for completing the negotiations by 1990, as called for in the Punta del Este Declaration of 1986. The countries of the Pacific Rim--with the exception of Taiwan, which is not a GATT member--have been active participants in the negotiations. Their continued full and active participation is essential to the successful completion of the negotiations.

As we evaluate progress in achieving our objectives in the Uruguay Round, we may want to explore ways in which bilateral agreements can complement or enhance these efforts. When additional results can be achieved bilaterally, we should not hesitate to move in that direction--including, if appropriate, the negotiation of free trade agreements. I would note in this regard that the United

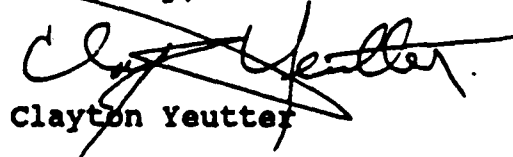
Mr. Kenneth Mason  
October 27, 1988  
Page Two

States and the ASEAN countries are currently undertaking a study of the economic costs and benefits of various options for strengthening the ASEAN-U.S. economic relationship. This study, which is known as the ASEAN-U.S. Initiative (AUI), will examine a whole range of liberalization options but will not be limited to examining free trade arrangements. Taiwan, on the other hand, is now seriously considering becoming a GATT member. This represents a significant step, the consequences of which will require careful study.

While we remain receptive, in principle, to bilateral initiatives with other trading partners similar to the U.S.-Canada FTA, the appropriateness of initiating negotiations with particular countries is an issue that future administrations will need to address. It would be inappropriate at this time to decide either to exclude the possibility of free trade agreements with the countries of the Pacific Rim or to begin negotiations on such arrangements when the implications of that decision will be the responsibility of the next Administration.

I hope this responds to your request regarding the desirability of pursuing negotiations with selected countries of the Pacific Rim on bilateral or regional free trade agreements. I look forward to seeing the results of your study.

Sincerely,

  
Clayton Yeutter

CY:ojh