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South Korea-U.S. Economic Relations: Cooperation, Friction, and Future Prospects

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South Korea-U.S. Economic Relations: Cooperation, Friction, and Future Prospects

Summary

Over the past decade, South Korea has emerged as a major economic partner for the United States. In 2000, Koreans purchased over \$26 billion in U.S. goods, making Korea the U.S.'s sixth largest export market. Korea has also become a significant investment site for American companies, which have poured nearly \$10 billion into the country over the past three years. The U.S. is Korea's number export market and number one supplier of imports.

Increased economic interaction has been accompanied by disagreements over trade policies. The level of bilateral friction is principally affected by three factors: the size of the U.S. trade deficit with South Korea; the state of the U.S. economy; and whether or not bilateral political or security issues override bilateral trade considerations.

During Korea's financial crisis in 1997 and 1998, the Clinton Administration tended to mute its criticism of Seoul's alleged barriers to foreign exports and investors. Since the spring of 2000, however, the United States has intensified its pressure on bilateral trade issues, protesting that Seoul has been unresponsive to a host of longstanding U.S. complaints. In its annual report on foreign trade barriers, issued in April 2001, the Office of the United States Trade Representative (USTR) devoted 22 pages to South Korea, more than it did to any other country except Japan and China. The shift in U.S. policy has been due in part to the swings in the U.S.-Korean trade balance; after enjoying three years of trade surpluses with South Korea, the U.S. has run increasingly large bilateral trade deficits since 1998. As the U.S. economy has slowed, Congress has become more vocal on bilateral trade issues, particularly semiconductors and automobiles. Additionally, the months-long stalemates in North-South Korean and North Korean-U.S. relations have dulled the acuteness of security issues in the U.S.-South Korean relationship; Washington does not have to be as concerned that its trade policy will jeopardize its own or Seoul's negotiations with Pyongyang.

This report summarizes the main issues in U.S.-South Korean economic relations. It will be updated periodically.

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South Korea-U.S. Economic Relations: Cooperation, Friction, and Future Prospects

U.S.-South Korea Bilateral Trade

Over the past decade, South Korea has emerged as a major economic partner for the United States. Between 1990 and 2000, U.S.-Korean trade more than doubled (see Table 1). In 2000, two-way trade (exports plus imports) was over \$66 billion, making South Korea the U.S.' seventh-largest trading partner. South Korea was the U.S.' sixth-largest export market (after Canada, Mexico, Japan, Germany and the United Kingdom) in 2000, with \$26.3 billion in U.S. goods shipped to Korea.

For decades, the United States has been Korea's largest export market. Exports to the U.S. accounted for approximately 20% of Korea's total exports in 1999 and 2000. In recent years, exports to the United States accounted for more than 6% of Korea's gross domestic product (GDP).¹ Moreover, since Korea's financial crisis in 1997, the United States has overtaken Japan as Korea's largest supplier of imports. Major U.S. exports to South Korea include semiconductors, machinery (particularly semiconductor production machinery), aircraft, agricultural products, and beef. South Korea is the U.S.' 4th largest market for agricultural products and 3rd largest market for beef. Major U.S. imports from South Korea include electrical machinery (with semiconductors accounting for nearly 20% of total South Korean shipments to the U.S.), cellular phones, general machinery, automobiles, textile products, and steel.

Mid-1990s: U.S. Bilateral Trade Surplus. As shown in Table 1, from 1994-1997 the U.S. ran a trade surplus with South Korea, after several years of trade deficits. The surplus peaked at nearly \$4 billion in 1996, the same year South Korea became the U.S.'s fifth largest export market. The primary reason for the surplus was a sharp rise in U.S. exports – which peaked at \$26.6 billion in 1996 – propelled by the boom in South Korea's economy in the mid-1990s, which increased demand for foreign products. The 60% rise in U.S. shipments from 1990 to 1997 more than offset the 25% increase in U.S. imports from South Korea over the same time period.

1998-2001: U.S. Bilateral Trade Deficit. In the fall of 1997, South Korea plunged into a serious economic crisis. In December of that year, Seoul and the International Monetary Fund (IMF) agreed to the terms of a \$58 billion financial support package. As a *quid pro quo* for receiving IMF emergency loans,

¹ Choi, Inbom, and Jeffrey J. Schott, *Free Trade between Korea and the United States?* Washington, DC: Institute for International Economics, 2001, p. 59.

Seoul agreed to tighten its fiscal and monetary policies and engage in far-reaching, market-oriented reforms of its financial and corporate sectors, and of its labor market policies. South Korea also agreed to open its economy further to foreign goods and investors.

Table 1. Annual U.S.-South Korea Merchandise Trade
(Billions of U.S. Dollars)

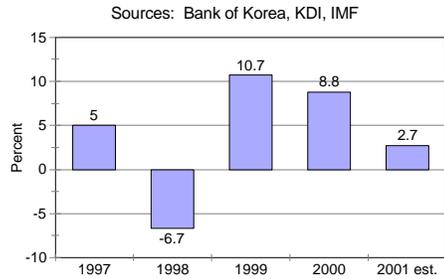
Year	U.S. Exports	U.S. Imports	Trade Balance	Total Trade (Exports + Imports)
1990	\$14.40	\$18.49	-\$4.09	\$32.89
1991	\$15.51	\$17.02	-\$1.51	\$32.53
1992	\$14.64	\$16.68	-\$2.04	\$31.32
1993	\$14.78	\$17.12	-\$2.34	\$31.90
1994	\$18.03	\$19.63	-\$1.60	\$37.66
1995	\$25.38	\$24.18	\$1.20	\$49.56
1996	\$26.62	\$22.66	\$3.97	\$49.28
1997	\$25.05	\$23.17	\$1.87	\$48.22
1998	\$16.49	\$23.94	-\$7.46	\$40.43
1999	\$22.04	\$31.15	-\$9.11	\$53.19
2000	\$26.30	\$39.83	-\$13.53	\$66.13
Jan - Oct 2000	\$ 22.16	\$32.74	-\$10.58	\$54.90
Jan - Oct 2001	\$ 17.49	\$29.18	-\$11.69	\$46.67

Sources: 1990-1998 data from Global Trade Information Services. 1999-2001 data from U.S. International Trade Commission.

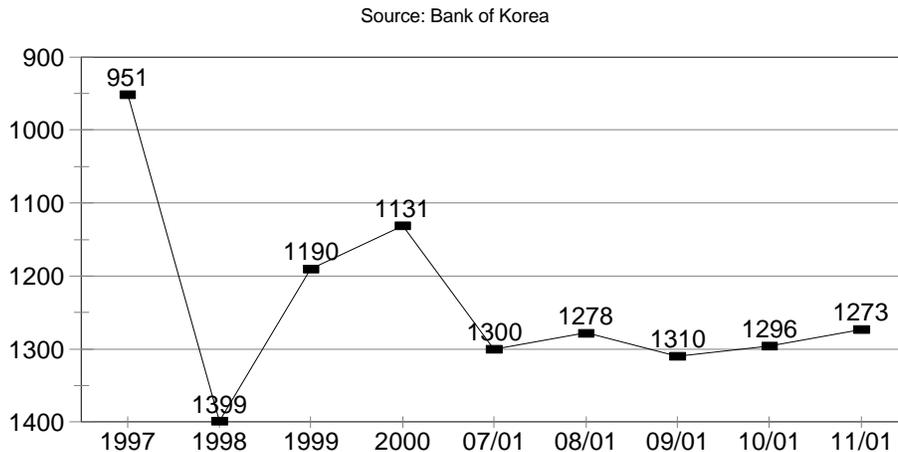
Since Korea's economic crisis, the U.S. has run an increasingly large bilateral trade deficit with that country. Korea's 1998 recession, during which time its gross domestic product (GDP) shrank by 6.7% (see **Figure 1**), led to a sharp decline in most countries' exports to South Korea, including those from the United States.² American imports from South Korea, however, rose slightly in 1998 and significantly in 1999 and 2000. These increases were propelled by the strong U.S. economy, which increased U.S. demand for foreign goods and services, and by the devaluation of the won, which made Korean products cheaper for Americans to buy. In 2001, the slowing U.S. economy in 2001 has led to a drop in Korean imports.

In 1999, with Korea's economy growing by 10.7%, U.S. exports to South Korea recovered somewhat. With Korea's economy growing by nearly 9% in 2000, U.S. shipments to Korea rose by more than 20% compared with 1999. Growth in imports from Korea (up by nearly 30% in 2000), however, continued to outstrip U.S. export

² See Raymond Ahearn, *South Korea's Economic Prospects*, CRS Report RS20041, February 1, 1999.

Figure 1. Korea's GDP Growth

growth, causing the trade deficit to widen. The deficit has grown further in the first ten months of 2001, as year-on-year U.S. exports to the ROK have fallen by more (down by more 20%) than have U.S. imports from Korea (down by 11%). U.S. exports have decreased in large measure because of Korea's sharp economic slowdown and the effects of the Korean *won's* devaluation (see Figure 2).

Figure 2. Won-Dollar Exchange Rate (Average), 1997-2001

Foreign Direct Investment Flows

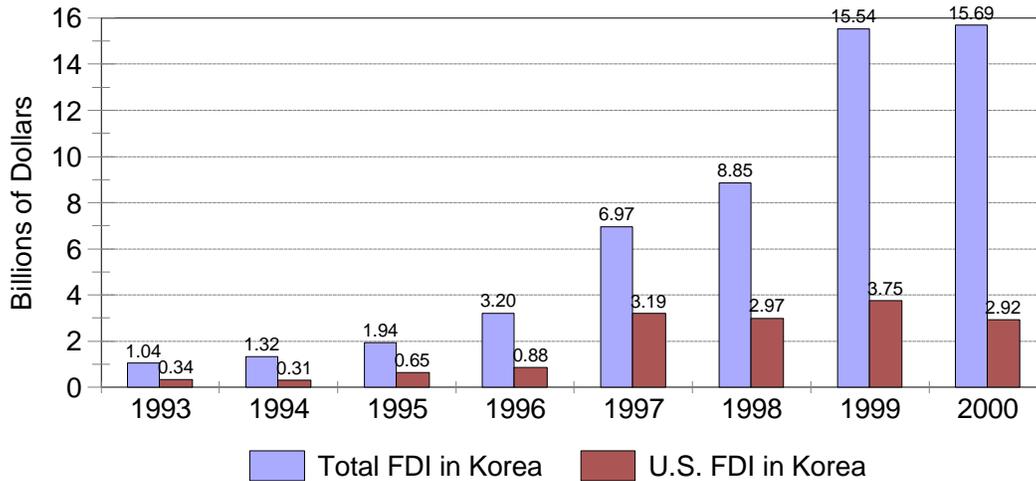
As part of its commitment to the IMF in December 1997, Seoul pledged to eliminate most restrictions on foreign direct investment (FDI). The government of President Kim Dae Jung, who was elected during the nadir of Korea's financial crisis, has moved aggressively to liberalize Korea's foreign investment regime. Partly as a response to Kim's reforms, and partly in response to the lower prices of Korean assets following the 1997 crisis, FDI flows have increased markedly, soaring from \$3.2 billion in 1996 to \$15.7 billion in 2000. American companies have invested nearly \$10 billion in South Korea over the past three years. U.S. FDI in 2000 alone – amounting to \$2.9 billion – was greater than total U.S. FDI in Korea from 1993 to 1996. For the first nine months of 2001, recorded U.S. FDI was \$1.8 billion, roughly the same as was recorded in the same period in 2000.³

³ Korean Ministry of Commerce, Industry, and Energy. See www.mocie.go.kr/eng/index.asp. Much of the new foreign direct investment has come from Western European firms, which in 1998 replaced their American counterparts as the largest source of FDI in Korea. In 2000, for example, European Union firms accounted for nearly 30% of FDI, followed by U.S. firms (18%), and Japanese firms (15%).

For the first half of the 1990s, annual South Korean FDI in the U.S. ranged from \$350 million to \$535 million. After soaring to \$1.57 billion in 1996, Korean FDI fell to \$729 million in 1997 and \$874 million in 1998.⁴

Figure 3. Foreign Direct Investment in Korea

Source: Ministry of Finance & Economy



Bilateral Investment Treaty Negotiations. For several years, the U.S. and South Korea have been discussing a bilateral investment treaty (BIT). BITs are designed to improve the climate for foreign investors – typically by committing the signatories to prohibit discrimination against foreign investors – by establishing dispute settlement procedures, and by protecting foreign investors from performance requirements, restrictions on transferring funds, and arbitrary expropriation. The U.S. has signed over 30 BITs, primarily with countries undergoing significant economic reforms. The U.S. and South Korea last held formal negotiations in 1999. Reportedly, the major stumbling block is Korea’s so-called “screen quotas,” which are limits on the dates and screen time given to foreign films. Foreign ownership in the Korean telecommunications industry and Korea’s copyright rules also remain outstanding issues.

A Possible Korea-U.S. Free Trade Area (FTA). In recent years, there have been some calls for the U.S. and Korea to negotiate a free trade area, which would lower trade barriers between the two countries. The idea enjoys the support of the American business community in Korea, and many Korean businesses in the U.S. In the Senate, Max Baucus introduced legislation in May 2001 (S. 944) authorizing FTA negotiations with Seoul, the second time he has presented this initiative. No legislative action was taken on his first attempt, S. 1869, introduced in the 106th Congress. To date, no formal government-to-government discussions have been held over an FTA. Speaking in December 2001, U.S. Ambassador to Korea

⁴ Organization for Economic Cooperation and Development, *International Direct Investment Statistical Yearbook 1999*.

Thomas Hubbard said that a Korea-U.S. FTA is not on the Bush Administration's short-term policy agenda.

In 2001, at the request of the Senate Finance Committee, the International Trade Commission conducted a fact-finding investigation on the likely economic impact of a South Korea-U.S. FTA. The ITC's final report estimated that within four years after implementation of an FTA, U.S. exports to Korea would increase by 54% while U.S. imports would rise by 21%. In the short run, the biggest beneficiaries would likely be those industries in both countries that face high initial trade barriers. On the U.S. side, the ITC found that bilateral agricultural exports would increase by more than 200%. For Korea, the ITC projected that textiles and apparel exporters would see their shipments to the U.S. rise by 125%.⁵ Thus, the report implied that the FTA's potential benefits would be greatly diluted if these politically sensitive sectors were excluded.⁶

Overall, the ITC estimated that within four years after implementation of an FTA, U.S. GDP would increase by approximately 0.2%, while Korean GDP would rise by 0.7% as a result of the FTA.⁷ An earlier study by the Institute for International Economics (IIE), found similar effects for the U.S. economy, but had a wider band for the increase on Korean GDP, which was projected in the 0.4%-2.0% range. As in the ITC study, the IIE report found that most of the benefits to U.S. firms would derive from increased access to Korea's market. In contrast, the IIE projected that most of Korea's gains from an FTA would stem not from preferential access to the U.S. market but from improvements in the allocative efficiency of the Korean economy brought about by the trade reforms required by an FTA.⁸

Major U.S. Trade Disputes with South Korea

During the Asian financial crisis in 1997 and 1998, the U.S. tended to mute its criticism of South Korea's alleged barriers to foreign companies. Since the spring of 2000, however, the U.S. has intensified its pressure on trade issues, protesting that Seoul has been unresponsive to a host of longstanding U.S. complaints. In its annual report on foreign trade barriers, issued in April 2001, the Office of the United States Trade Representative (USTR) devoted 22 pages to South Korea, more than it did to any other country except Japan and China. In early May 2000, the USTR cited Korea as a "priority watch country" under "Special 301" (Section 182 of the Trade Act of 1974) because it deems Seoul's enforcement of intellectual property rights to be unsatisfactory. Korea remains on this list. In the spring of 2001, in an attempt to exert more pressure on Seoul, the U.S. government began holding quarterly,

⁵ United States International Trade Commission (ITC), *U.S.-Korea FTA: The Economic Impact of Establishing a Free Trade Agreement (FTA) Between the United States and the Republic of Korea*, (Washington, DC, 2001), p. 5-1 - 5-2.

⁶ For a similar argument, see Choi and Schott, *Free Trade*, p.80.

⁷ ITC, *U.S.-Korea FTA*, p. x-xi.

⁸ See Choi and Schott, *Free Trade*, p. 79-82.

interagency “stocktaking” meetings to discuss progress on and strategies for settling major bilateral trade disputes.

Congressional interest in U.S.-Korean trade relations also has increased in recent months. After introducing no major Korea-related economic legislation in 2000, in 2001 Members of Congress have introduced a number of measures complaining about alleged Korean trade barriers and allegedly unfair subsidy policies.

Below are brief descriptions of several major sector-specific disputes between the U.S. and South Korea. In general, U.S. exporters and trade negotiators identify the lack of transparency of Korea’s trading and regulatory systems as the most significant barrier to trade with Korea, in almost every major product sector.

Automobiles. South Korea, the world’s fourth-biggest producer of automobiles, has long maintained a variety of barriers to the import of automobiles, including a ban on Japanese automobiles and the auditing of the income taxes of individuals who purchased foreign luxury cars. The ban on Japanese automobiles was eliminated in 1999. In its October 1997 Super 301 report to Congress, the Clinton Administration designated Korea as a “Priority Foreign Country” for its barriers to foreign motor vehicles.⁹ USTR subsequently initiated an investigation under Section 301 of the U.S. Trade Act of 1974, as amended, and issued a call for bilateral consultations to provide fair market access for foreign autos in Korea.¹⁰ In 1998, the U.S. and South Korea signed a Memorandum of Understanding (MOU) on foreign access to Korea’s auto market, which led the USTR to terminate the Section 301 investigation. Under the MOU, Seoul agreed to reduce its tariffs on motor vehicles from 80% to 8%,¹¹ proactively address instances of anti-import activity in Korea, lower or eliminate many automobile taxes, create a new financing system to make it easier to purchase automobiles, and streamline its standards and certification procedures. Many of these steps – including lowering tariffs – have been implemented.

In the spring of 2000, the USTR criticized South Korea’s compliance with some areas of the MOU, and called on Seoul to take additional steps – outside the MOU

⁹ Super 301 (Section 310 of the 1974 Trade Act) requires the USTR to report to congress on “priority foreign countries” that practice unfair trade and “priority practices” that have the greatest effect on restricting U.S. exports. If agreement is not reached on the priority practices, the USTR is required to initiate a Section 301 case (see the following footnote). For more information, see Wayne Morrison, *Section 301 of the Trade Act of 1974*, CRS Report 98-454. See also Gwenell Bass, *U.S.-South Korea Auto Talks*, CRS Report 97-1030, December 4, 1997.

¹⁰ Section 301 (sections 301-309 of the Trade Act of 1974) authorize the USTR to initiate investigations of foreign trade practices that allegedly discriminate against U.S. commerce. If a settlement with the foreign country is not reached following the initiation of the investigation, the USTR decides whether or not to retaliate, usually in the form of 100% tariffs on selected imports from the offending country. See Morrison, *Section 301 of the Trade Act of 1974*, CRS Report 98-454.

¹¹ By way of comparison, the U.S. tariff on passenger vehicles is 2.5%. The Japanese tariff rate is 0%.

– to open the auto market. In particular, foreign market share for autos remains extremely low at approximately 0.37%, compared with 5% in Japan, 25% in the European Union, and 30% in the United States.¹² U.S. officials and businesspeople attribute the poor sales to a “buy Korea” mentality among most Koreans, protectionist statements made by high level Korean government officials, high tariffs and auto taxes, onerous standards and certification rules, and a perception among Koreans that their income taxes will be audited if they purchase a foreign automobile. The U.S. government and auto executives have called on the Korean government to take more visible steps to encourage purchases of foreign cars and to rewrite Korean regulations to reduce the barriers to foreign autos. Korean officials contend that few foreign vehicles are sold because of the decreased purchasing power of Korean consumers since the crisis (foreign autos cost considerably more than Korean models), the lack of advertising by foreign auto manufacturers, and Korean consumers’ preference for smaller vehicles.

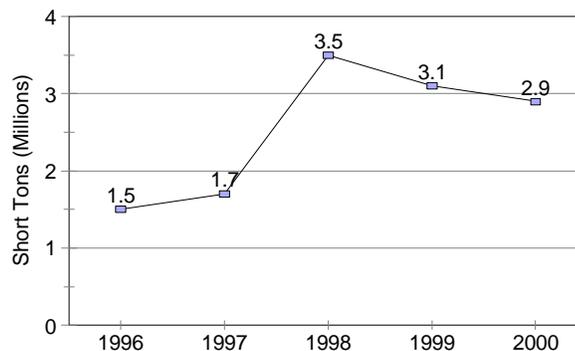
U.S.-Korean consultations on the MOU have been held regularly in recent months, but without any new progress reported. One obstacle appears to be paralysis in the Korean government; with President Kim Dae Jung’s popularity at an all-time low, governmental authorities appear unwilling to take the high-profile, politically unpopular, steps to encourage more automobile imports. It is unclear whether the completion of General Motors’ takeover of Daewoo Motors – a deal that is in the final stages of negotiation – will alter Korea’s auto imports.

H.Con.Res. 144 and S.Con.Res. 43, introduced in May 2001, call on South Korea to end the practices that impede foreign market access, and request various U.S. executive agencies to monitor Korea’s progress on this issue.

Steel. For years, South Korean steel exports to the United States have been one of the most politically charged items on the bilateral economic agenda, particularly since the 1997 Asian financial crisis. From 1997 to 1998, Korean shipments of steel to the U.S. surged by 109%, vaulting South Korea into the top five U.S. sources of steel imports. Although Korea’s steel exports to the U.S. have declined since 1998 (see Figure 4), they have not returned to pre-crisis levels. For the first six months of 2001, Korean exported just under 1.3 metric tons of steel to the United States, a 22.4% year-on-year decline, in line with a general decline in U.S. steel imports.

Figure 4. Steel Imports from Korea

Source: International Trade Commission



¹² According to the American Chamber of Commerce in Korea, of the more than 1 million automobiles sold in Korea in 2000, 4,414 were foreign-made. See American Chamber of Commerce in Korea, *Improving Korea’s Business Climate. Recommendations from American Business 2001*, p.50-52.

In response to the 1998 surge from Korea and other steel-producing countries, Congress joined major U.S. steel manufacturers in pressuring the Clinton Administration to take action. President Clinton granted safeguard relief (under Section 201 of the Trade Act of 1974) for U.S. producers of steel welded line pipe and wire rod, a move that raised tariffs on imports of those products.¹³ In September 2000, Korea challenged the Section 201 action in the WTO. In October 2001, the WTO panel ruled that the Korean claims were partly valid. The U.S. has appealed the ruling. A decision is due in February 2001.

The Clinton Administration also imposed anti-dumping duties on Korean exports of stainless steel plate in coils and stainless steel sheet and strip. Seoul protested these duties WTO, and a dispute settlement panel was formed in November 1999. In its final report of December 2000, the WTO panel ruled against the United States' methodology used to calculate the margin of dumping in the case, and the U.S. subsequently agreed to abide by the ruling.

Korea is likely to be affected by President Bush's decision in June 2001 to initiate a Section 201 investigation of the effects of imports of over 600 steel products on the U.S. steel industry. The U.S. International Trade Commission (ITC) has recommended that the President grant the U.S. industry relief through a variety of trade remedies – including increased tariffs – for imported steel products representing a majority of U.S. imports. President Bush now has until February 2002 to decide on the size and type of remedy he will apply, if any. In the WTO, Seoul has protested the Section 201 petition and the ITC's findings. Higher duties are expected to have a significant, but not devastating, impact on Korea's steel industry in part because many of Korea's major export items to the United States were excluded from the Section 201 investigation. Moreover, while industry petitioners sought tariff increases of 40-50%, the majority of the ITC recommended much lower rates.¹⁴

From time to time, Congress has called on the Korean government to end its ownership of some steel firms and subsidization of others. The October 1998 omnibus spending bill (P.L. 105-277), for example, directed (section 621) USTR to monitor and report upon the Korean government's support for Korean producer Hanbo Steel, the insolvency of which in 1997 helped precipitate the country's

¹³ Section 201 relief, often referred to as "safeguard" or "escape clause" relief, is defined in sections 201-204 of the Trade Act of 1974, as amended (19 U.S.C. 2251-2254). Safeguard relief provides for temporary duties, quotas, or other restrictions on imports that may be traded fairly, but that enter in such quantities as to cause or threaten to cause serious injury to a domestic industry. The relief is intended to give the domestic industry an opportunity to adjust to the new competition and remain competitive. Within six months after a Section 201 petition has been filed with the International Trade Commission, the ITC must conduct an investigation, determine if relief is warranted, and recommend appropriate remedial action from a specified range of options. The President then decides whether to implement the recommended measure, apply an alternative measure, or take no action at all.

¹⁴ *Korea Times*, December 11, 2001. For more on the Section 201 case, see Stephen Cooney, *Steel Industry and Trade Issues*, CRS Report RL31107.

financial crisis later that year.¹⁵ In 2000, a consortium of U.S. investors abandoned its attempt to purchase Hanbo for \$480 million, reportedly because a number of its demands had not been met by the government-controlled entity that is managing Hanbo. In December 2001, the Korean government announced it would sell Hanbo to AK Capital of the U.S. However, the sale has hit a snag due to the government's contention that AK Capital's \$550 million bid is insufficient.

For years, the U.S. has demanded that the South Korean government reduce its ownership of the Korean steel industry. Most prominently, the U.S. has called on Seoul to *fully* privatize Pohang Iron & Steel Co (**POSCO**), the world's second-largest steel producer, which has been accused of using government subsidies to dump steel in the U.S.¹⁶ In October 2000, the Korean government partially met U.S. demands by selling off the remaining 6.84% stake held by state-run Korea Development Bank (KDB), formerly the majority shareholder in POSCO. Shortly before the sale, the government also scrapped its rules limiting individual owners to a 3% stake in POSCO. Seoul now contends that the privatization of the steel-maker is complete. Korea, however, has not yet met the United States demand that the Korea Industrial Bank – which is 98% owned by the Korean government – divest its 3.01% stake in POSCO. Foreign interests now own a majority of POSCO's shares. POSCO dominates the Korean steel industry, accounting for over 60% of the nation's crude steel output in 1999.¹⁷

Assistance to Hynix Semiconductor. In 2001, a major trade dispute nearly erupted between the United States and South Korea over allegations that the Seoul government was propping up Hynix Semiconductor, presently the world's third-largest producer of dynamic random access memory (DRAM) semiconductor chips. Last year, Hynix's leading creditors – most of which are owned by the Korean government – orchestrated a series of rescue packages that have kept Hynix in business by enabling it to restructure its 8.6 trillion *won* (over \$6.5 billion) in debt. In the U.S., Micron Technology, the Idaho-based second largest producer of DRAMs, led a campaign against the support packages, arguing that they amounted to government-sponsored bailouts that allow Hynix to export at low prices and that they were a prime cause of the drastic plunge in global chip prices in 2001. Micron, the last U.S.-based DRAM producer, threatened to file countervailing duty and anti-dumping petitions. Prodded by Micron and some Members of Congress,¹⁸ the Bush

¹⁵ See Gwenell Bass, *The Steel Import Surge: Causes and Proposed Remedies*, CRS Report RL30073, March 19, 1999.

¹⁶ See Chapter 3 of the U.S. Department of Commerce's report, *Global Steel Trade*, available as of October 4, 2000 at [<http://www.ita.doc.gov/media/steelreport726.htm>].

¹⁷ ITC, *U.S.-Korea FTA*, p.3-23.

¹⁸ For instance, in September, an amendment sponsored by Senator Larry Craig protesting the "Republic of Korea's improper bailout of Hynix" was incorporated into the Senate's version of H.R. 2500, the appropriations bill for Commerce, Justice, and State. The legislation notes that in 1998, Congress inserted a provision into the Omnibus Fiscal 1999 Appropriations Act (H.R. 4328, P.L. 105-277) requiring that the 1997 IMF \$58 billion assistance package to Seoul not be used to support South Korean companies that compete

Administration raised the matter in bilateral and multilateral meetings with South Korea and considered requesting that the World Trade Organization establish a dispute settlement panel to investigate. The Korean government has presented evidence that the decisions on whether to aid Hynix have been in the hands of the company's creditors.

The economic stakes are high. U.S. and South Korea trade in DRAMs totaled almost \$3 billion in 2000, nearly twice the value of the two countries' trade in iron and steel products. Semiconductors as a whole are the number one U.S. import from and export to Korea. Furthermore, the Hynix packages call into question the Korean government's commitment to economic reforms, which are designed to make Korean conglomerates more responsive to market pressures and end the past practice of rescuing troubled conglomerates considered "too big to fail." Hynix accounts for an estimated 4% of South Korea's exports. Over 150,000 Koreans are employed by Hynix and its network of suppliers.

In early December 2001, the impetus for the dispute was suddenly removed – at least temporarily – by the announcement that Micron and Hynix had begun negotiating a possible strategic alliance. By early January 2002, no deal had been reached. The key business and governmental players involved in the dispute remain poised to pursue international trade remedies if the talks break down. In the meantime, amid reports that DRAM chip demand is beginning to recover, Hynix has announced three price increases within the past month.

Intellectual Property Rights Issues. Bilateral tensions often have arisen over U.S. allegations that Korea does not sufficiently protect intellectual property rights (IPRs). In 1999, the U.S. praised Korea for making significant efforts to strengthen its IPR laws, a result of Seoul becoming a signatory to the World Trade Organization Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs) in 1994. The USTR downgraded Seoul from Special 301 "priority watch list" in 1997 to "watch list" in 1998.¹⁹ In May 2000, however, Korea was elevated back to the "priority watch list," where it remains today, due to concerns about inadequate protection of rights in the pharmaceutical industry, continued piracy of computer software, and new (December 1999) revisions to Korea's copyright laws.

In 2000 and early 2001, the Korean government took many steps to improve the enforcement of its intellectual property rights regulations, particularly those pertaining

¹⁸ (...continued)

unfairly with U.S. companies. The Craig amendment was stripped from the bill in conference.

¹⁹ "Special 301" refers to Section 182 of the Trade Act of 1974. Since the start of the Special 301 provision in 1989, the USTR has issued annually a three-tier list of countries judged to have inadequate regimes for IPR protection, or to deny access: 1) *priority foreign countries* are deemed to be the worst violators, and are subject to Section 301 investigations and possible trade sanctions; 2) *priority watch list countries* are considered to have major deficiencies in their IPR regime, but do not currently warrant a Section 301 investigation; and 3) *watch list countries*, which maintain IPR practices that are of particular concern, but do not yet warrant higher level designations. See Morrison, *Section 301 of the Trade Act of 1974*, CRS Report 98-454.

to the computer software industry. While welcoming these moves, the Bush Administration has stated that it “is too soon to judge their effectiveness,” and has expressed concerns over whether the improved regime will be sufficiently transparent and non-discriminatory.²⁰

Pharmaceuticals. Korea is the 12th largest pharmaceutical market globally with 1999 sales approaching approximately U.S.\$4.9 billion. Imports comprise approximately 20% of the total market. For years, the U.S. has raised complaints about a number of Korea’s practices in the pharmaceutical industry, particularly over Seoul’s testing requirements, which describes as “onerous” and non-science based.²¹ Recent complaints include: poor protection of intellectual property rights for medical patents; the lack of transparency of the Korean Ministry of Health and Welfare, particularly with regard to reimbursement policies for prescription drugs in Korea’s new national drug program; the vagueness of a July 2000 Korean law requiring that “cosmeceuticals” – cosmetic products that have a functional or therapeutic effect – be reviewed for safety and efficacy; and the discriminatory nature of Seoul’s requirements that foreign drugs must be retested on Koreans living in Korea, rather than on other ethnic Asians, as the U.S. has insisted.

Agricultural Issues. U.S. agricultural exporters have long complained about high tariff and non-tariff barriers maintained by Korea, which is the United States’ fourth largest market for agricultural products, to protect domestic Korean producers. Approximately 44% of Korea’s farm imports in 2000 came from the United States.²² In September 2001, Washington and Seoul settled their most contentious agricultural dispute in recent years, when the U.S. accepted Korea’s abolition of its requirement that imported beef be distributed and sold through different channels than domestic beef. In 2000, a dispute settlement panel requested by the U.S. and Australia had ruled that Korea’s beef import system discriminated against foreign suppliers. South Korea is the United States’ third largest market for beef.

Although the beef dispute has been temporarily settled, several other disagreements linger. U.S. trade officials complain about the clarity of Korea’s new labeling and rule of origin requirements for genetically modified foods. The U.S. has also charged that Korea’s quarantine policies and mandated shelf-life requirements are barriers to imports. U.S. agricultural groups contend that Korea’s import certification requirements and testing standards are unduly onerous.²³

Korean’s Complaints Against U.S. Anti-Dumping and CVD Practices. For over a decade, South Korea has chafed at the United States’ use of anti-dumping and counter-vailing duty (CVD) laws to raise tariffs on Korean exports. According to Choi and Schott’s study, in July 2000 the five CVD and 18 anti-

²⁰ United States Trade Representative, *2001 Special 301 Report*, p. 20-21.

²¹ United States Trade Representative, *2001 National Trade Estimate Report on Foreign Trade Barriers*, p. 288, 294-96.

²² ITC, *U.S.-Korea FTA*, p.3-10.

²³ Caroline Cooper, “KEI Trade Brief. U.S.-Korea Bilateral Trade Relations,” November 2001.

dumping orders against South Korean exports covered approximately \$2.5 billion, or over 7%, of U.S. imports from South Korea in 1999. Moreover, these tariff hikes have tended to be concentrated in a handful of Korean industries – semiconductors, steel, televisions, and telecommunications equipment – that have considerable political influence in Seoul.

During the Uruguay Round (1986-1993) of the General Agreement on Tariffs and Trade (GATT, the WTO's predecessor organization), Korea was one of several countries demanding revisions to global anti-dumping rules, changes the United States opposed because of fears they would constrain U.S. anti-dumping investigators. South Korea, joined most prominently by Japan, has taken up this issue again in the WTO's current round of negotiations, against U.S. opposition.

In 1999 and 2000, Seoul took the U.S. to the WTO over allegedly discriminatory U.S. anti-dumping duties placed on Korean exports of steel and semiconductors. In the latter case, in September 2000 Korea and the U.S. reached an agreement whereby the U.S. dropped anti-dumping duties imposed against Korean dynamic random access memory (D-RAM) chips. In exchange the Korean semiconductor industry pledged to collect D-RAM price and cost data, and provide this information to the U.S. if a new anti-dumping case is filed against Korean semiconductor imports. The agreement preempted a WTO panel decision that was widely expected to rule against the U.S., a ruling that could have required changes to U.S. anti-dumping regulations. As part of the agreement, Korea asked that the WTO suspend its panel covering the case.

Conclusion

The level of U.S.-South Korean trade friction is principally affected by three factors: the size of the U.S. trade deficit with South Korea; the state of the U.S. economy; and whether or not political or security issues override bilateral trade considerations. Since the spring of 2000 – a period of rising bilateral deficits and a slowing U.S. economy – trade tensions between Washington and Seoul have been rising, after a lull of about three years in which trade disputes were deemphasized to focus on Korea's recovery from its 1997 financial crisis. The change was more a result of shifting priorities on the U.S. side, rather than an increase in the number of disputes, as virtually all current areas of disagreement have been sources of tension for years.

For most of 1999 and 2000, with the notable exception of steel, the United States' focus on areas of trade friction was confined primarily to the executive branch. The 107th Congress, however, has intensified its interest in U.S.-Korean economic relations, principally on the issues of semiconductors and automobiles. In late 2001, tensions over assistance to the Hynix Semiconductor – which some Members of Congress closely tracked – very nearly caused a major trade dispute between the United States and South Korea to erupt, an indication that the United States' anti-terrorism campaign has yet to slow down the Bush Administration's trade policy, even when that policy threatens to antagonize diplomatic allies. Additionally, the months-long stalemates in North-South Korean and North Korean-U.S. relations

mean that Washington does not have to be as concerned that its trade policy will jeopardize Seoul's negotiations with Pyongyang.