

## The Economic and Geopolitical Implications of the ongoing China-Korea FTA Negotiations

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### Abstract

This paper examines the implications of the CKF, Korea's potential free trade agreement (FTA) with China. It documents Korea's previous FTA negotiation experiences and the lessons it has learnt since its first agreement was signed with Chile in February 2003. Pivotal to this discussion, is the role domestic politics, so-called 'loser groups', and previously hard fought FTAs play in shaping the nature of FTA outcomes. The paper also details the growing importance of China and Korea's economic relationship, the positive and negative impacts a free trade deal would likely have on both countries as well as the geopolitical implications of any potential CKF agreement. The negotiation strategies currently employed in the CKF are also documented and two tentative scenarios (the hard bargaining game and the dramatic conclusion of the CKF) are hypothesized as possible outcomes to future talks. This paper contends that since the benefits of a successful CKF would far outweigh the costs associated with any mutual concession, the motto adopted by both Korean and Chinese negotiators should be one that pursues long term gain over short term cost.

**Keywords:** Domestic Politics of FTA, US-China Hegemony  
Game, FTA Negotiation Strategies, Mid-level FTA

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## **I. Introduction**

At the China-Korea Leaders' Meeting in Beijing on 28th May 2012, Chinese political leader Hu Jintao and Korean President Lee Myung-Bak declared the official launch of the CKF. This is an ambitious step by China and Korea to initiate economic integration in East Asia. There is in fact room for debate on the economic benefits and costs of the FTA deal. The economic relationship in terms of trade and investment is so huge that CKF triggers strong political reactions from domestic constituencies in Korea and China, particularly coming from farmers' organizations and labor unions in Korea. Also, there is prevailing skepticism on the feasibility of this bilateral negotiation.

When we look at the new geopolitical landscape on what is happening in the trans-Pacific region, it is necessary to take into account not only economic factors, but also the geopolitical implications involved.

At the 14th Asia-Pacific Economic Cooperation (APEC) Leaders' Meeting in Vietnam in November 2006, US President George W. Bush called for a bold strategy for a trans-Pacific APEC-wide Free Trade Area as a long-term goal. This is an ambitious step taken by the US to encourage trans-Pacific economic integration to respond to the rapidly changing geopolitical landscape of the region- an emerging 'new regionalism in East Asia' and rising Chinese economy. Furthermore, the US initiated the Trans-Pacific Partnership (TPP) in 2008 as an effort to consolidate US President W. Bush's 'Hanoi Vision' (APEC-wide FTA).

**Table 1. Korea's FTAs with its Partners**

		<b>Under Nego.</b>	<b>Signed</b>	<b>Effective</b>
1	K-Chile FTA		Feb. 2003	Apr. 2004
2	K-Singapore FTA		Aug. 2005	Mar. 2006
3	K-EFTA FTA		Dec. 2005	Jul. 2006
4	K-ASEAN FTA		Dec. 2005	Jul. 2006 (Goods)
5	K-India FTA		Aug. 2009	Jan. 2010
6	K-EU FTA		Oct. 2010	Jul. 2011
7	K-Peru FTA		Mar. 2011	Aug. 2011
8	K-US FTA		Jun. 2007	Mar. 2012
9	K-Turkey FTA		Concluded	Aug. 2012
10	K-Colombia FTA		Concluded	Aug. 2012
11	K-Canada FTA	Jul. 2005		
12	K-Mexico FTA	Jul. 2006		
13	K-GCC FTA	Jul. 2008		
14	K-Australia FTA	May. 2009		
15	K-New Zealand FTA	Jun. 2009		
16	K-China FTA	May. 2012		
17	K-Vietnam FTA	Sept. 2012		
18	K-Indonesia FTA	Jul. 2012		

Source: Ministry of Foreign Affairs and Trade

The background of US initiatives such as 'Hanoi Vision' and 'TPP Initiative' is not drawing a line in the Pacific. It means that the US wants to actively participate in economic integration in East Asia not only for economic reasons but also for geopolitical reasons, to say invisible hegemony game between US and China in this region. In this sense, geopolitical implications of the CKF are far-reaching for both sides. It will enable China to respond more effectively to the US 'TPP Initiative', which could otherwise seriously undermine China's trade interests in the region. For Korea, as China's 4th largest trading partner, China is not only its economic partner but also a politically important country which plays very crucial role in the Six-party Talks on North Korea's nuclear issues as well as reunification in the Korean

peninsula. The success of the deal therefore could become an important factor not only in fostering its economic prosperity but also in consolidating its national security interests. When these geopolitical implications are included in the mix, it becomes evident to understand the reason for why China and Korea want to have a FTA.

This paper aims to analyze the geopolitical implications of the CKF and ongoing negotiation strategies between two countries. After examining Korea's FTA policy in Chapter II, Chapter III gives an overview on the China-Korea economic relationship and the economic effect of the CKF. Chapter IV, then provides some perspectives on the ongoing negotiation strategies and conclusions.

## **II. Korea's FTA Policy and Some Lessons from Korea's FTA Negotiations Experiences**

### **1. Korea FTA Policy**

Korea has achieved remarkable economic development through the international free trade system led by the GATT and WTO and therefore, considered regionalism as a 'stumbling block' which discouraged the expansion of WTO regime. In this sense, Korea was a 'Late-Mover' to FTAs, up to the end of the 1990s.

However, the rapidly changing global economy and emerging regionalism in North America (NAFTA, 1994) and in Europe (expansion of EU, EU+10, 2005) forced Korea to move

fast toward FTA. Korea, first, had a FTA with Chile in 2003 and then with Singapore (2005), EFTA (2005), ASEAN (2005), and India (2009)

Korea and the US reached an agreement on their FTA in June 2007 and Korea and the EU agreed to have a FTA in October 2010. The US-Korea FTA Bill, being confronted by fierce political opposition, could not be ratified for almost 4 years, but was narrowly ratified in December 2010. The EU-Korea FTA and US-Korea FTA, respectively, came into effect in March 2012 and July 2012.

As seen in Table 1,

- So far 8 FTAs have become effective
- Additional two FTAs (Korea-Turkey FTA and Korea-Columbia FTA) were concluded this year (2012).
- Finally, Korea has been negotiating for 8 FTAs including FTA with Canada (since 2005), Australia (since 2009), etc.

This year, Korea opened official negotiations with 3 countries, China (in May, 2012), Indonesia (in July, 2012), and Vietnam (in September, 2012). As a result, Intra-FTA trade in Korea represents around 35.8% of Korea's total trade in 2011, whereas 38% in US and 17.6% in Japan.

The basic direction of Korea's FTA policy is to strengthen its trading partner's economic cooperation through FTA, particularly with the US, EU, China and Japan. Korea is the first country which has concluded FTAs with the world's top two economic poles in the world (US and EU). Korea is also negotiating a deal with the world's second-largest economic power (China). Through

such an aggressive FTA policy, Korea would become an 'FTA HUB' in East Asia, and it would also spark a 'competitive liberalization' in this region.

## **2. Some Valuable Lessons to learn from Korea's FTA Negotiation Experiences**

Korea experienced a really hard bargaining game when negotiating FTAs with Chile and the U.S. Valuable lessons that Korea has learned through these difficult experiences can be summarized as follows;

First, the most important 'stumbling block' of FTA negotiation does not come from 'Level-I game' (international negotiation with Chile or the US) but from strong domestic political reactions and oppositions coming from so-called 'loser groups'. The major loser groups were farmers' organizations and labor unions.

Second, although the loser groups would usually oppose FTA conclusion for economic reasons, they began to make a political issue out of the economic trade issue. There was an escalation of conflict from the economic issue to the political campaign. When talks were under way for the US-Korea FTA, Korea's loser groups launched anti-FTA campaigns under the slogans such as 'Anti-America Movement', and 'US Troops Out of Korea'. Likewise, when negotiations for the Korea-Chile FTA were under way, they even staged an 'anti-WTO' campaign.

Third, through hard experiences with US-Korea FTA, Korea-Chile FTA, etc., Korean people were significantly educated about the true and real aspect of FTA. When Korea

began to negotiate with Chile for FTA, many people worried that the opening of the domestic market would damage the loser industries seriously. Korean Farmers' organizations and anti-FTA NGOs particularly expected the Korea-Chile FTA to bring catastrophic effects on their fruit-growing farms (particularly grapes); they believed the FTA would turn many of their fruit farm business into failure. It has been eight years since Chile-Korea FTA went into effect, but without causing any particular damages on Korean fruit growing farmers. Korean people have learned a lesson from this case, gaining 'significant confidence' about FTA. This kind of 'Korean confidence' would help move the on-going negotiations forward for China-Korea.

### **III. Overview on China-Korea Economic Relationship and Economic Effect of CKF**

#### **1. Overview on China-Korea Economic Relationship**

Korea has replaced the U.S. and Japan with China as its most important economic partner. China has become Korea's largest trade and investment partner. Looking back into modern history of Korean economy, the U.S. and Japan were the top two trade partners for Korea. It is largely because of the 'industrialization strategy' that Korean business used to deploy; After they imported parts and components from Japan, Korean companies assembled them into final products and exported these assembled goods to the US market. But, this trading pattern began to change after Korea normalized diplomatic relations with China in 1992. Trading cooperation between Korea and Japan no longer remained as close as it used to be. In

contrast, trading volume between Korea and China has, since, jumped dramatically. Looking at the trading pattern among China, Japan and Korea, Korea posts a surplus in trade with China in manufacturing. As for the agricultural sector, Korea posts a surplus in its trade with Japan, but posts a deficit in its trade with China. In 2011, Korea posted a deficit of 17,182 million USD in its trade with Japan, but Korea posted a surplus of 47,753 million USD in its trade with China. But, in the agricultural sector, Korea has posted a trade deficit of 5 billion USD on average during the 2006 to 2011 period; Korea's trade deficit with China in the agricultural sector was 5,667 million USD in 2006 and 5,191 million USD in 2011.

Let's compare export and import volumes of bilateral trade among Korea, China and Japan. Korea's shipment to Japan increased 2.6 times from 15 billion USD in 2002 to 40 billion USD in 2011. Korea's shipment to China surged 6 times from 24 billion USD in 2002 to 134 billion USD in 2011. As for import volumes, Japan had been the largest source country of imports for Korea until 2006. But in 2007, Korea's imports from China began to be greater than Korea's imports from Japan. In 2011, Korea's imports from China amounted to 86 billion USD, while Korea's imports from Japan stood at 68 billion USD, showing a distinct reversal of these two numbers. In addition, Korea's trade balance pattern with China was opposite to that with Japan. Korea's trade surplus with China has steadily increased from 6 billion USD in 2002 to 48 billion in 2011. In contrast, Korea continued to post a trade deficit with Japan during the 2002 to 2011 period. These statistics show the relative importance of Korea's economic relationship with China, compared to that with Japan.



**Table 3.1 Korea's Trade to China & Japan**

(\$ million)

	China		Japan	
	Export	Import	Export	Import
2012(01-09)	97,458	60,326	28,872	48,414
2011	134,185	86,432	39,680	68,320
2010	116,838	71,574	28,176	64,296
2008	91,389	76,930	28,252	60,956
2006	69,459	48,557	26,534	51,926
2004	49,763	29,585	21,701	46,144
2002	23,754	17,400	15,143	29,856

Source: Korea International Trade Association

**Table 3.2 Korea's Trade Balance with China & Japan**

(\$ million)

	China	Japan
2012(01-08)	32,013	-17,182
2011	47,753	-28,640
2010	45,264	-36,120
2008	14,459	-32,704
2006	20,903	-25,392
2004	20,178	-24,443
2002	6,354	-14,713

Source: Korea International Trade Association

**Table 3.3 Korea's Trade Balance in Agriculture with China & Japan**

(\$ million)

	China	Japan
2011	-5,191	2,827
2010	-5,060	1,293
2008	-7,515	732
2006	-5,667	812

Source: Korea International Trade Association

It is not only trade but also investment that has prospered between Korea and China. China is Korea's most important overseas investment destination. Korea's overseas investment in China jumped to 4,874 million USD (2,179 projects) in 2011.<sup>1</sup> Korea's investment pattern in China has also diversified from its initial focus on labor-intensive industries like textiles, toys, etc. to capital-intensive industries like electronics, automobiles, and shipbuilding. Hyundai-Kia Automotive Group decided to invest about 1 trillion won in constructing a third factory with an annual capacity of 300,000 units in Yancheng, Jiangsu in China. Once the new factory is completed, the automotive group's combined annual production capacity in China with its existing factory in Beijing is expected to reach 1.73 million units. Also, Samsung Electronics is building a semiconductor factory worth 7 billion dollars in Xian, China. Samsung has invested a total of 10.5 billion dollars in China as it produces home electronics, mobile devices and others in China.

### **3. Economic Effect of CKF**

SERI<sup>2</sup> analyzed the forecast impact of the CKF under the assumption of a scenario in which the liberalization rate of the manufacturing sector is 100% and the liberalization rate of the agricultural sector is 50%. Under the scenario, Korea's GDP is forecasted to increase by 2.72%, while China's GDP is expected to increase by 0.35%. Also, the SERI analysis shows that CKF is forecasted to contribute to a 1.25% increase in China's welfare.

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<sup>1</sup> Korean Exim Bank, Ministry of Knowledge Economy

<sup>2</sup> Samsung Economic Research Institute

**Table 3.4 Output and Welfare Effects of CKF**

(unit:%)

	China		Korea	
	GDP	Welfare	GDP	Welfare
ADB <sup>4</sup>	0.32	0.00	2.70	0.95
SERI <sup>5</sup>	0.35	0.22	2.72	1.25

(1) ADB: Asian Development Bank

(2) SERI: Samsung Economic Research Institute

The analysis shows that Korea has more to gain than China from the CKF. ADB<sup>3</sup> released some statistics that also show similar trends under the assumption of a scenario in which the liberalization rate of the manufacturing sector and agricultural sector are both 100%. The ADB report forecasted that Korea would see a 2.70% rise in GDP and China would see a 0.32% rise in GDP thanks to CKF. In addition, the ADB report predicted that China would gain virtually nothing in terms of welfare but Korea would have a 0.95% gain in its welfare as a result of CKF.

Besides, it should consider loser industries versus winner industries that would occur on both sides in Korea and China, if the CKF becomes effective. As Table 3.5 shows on the Korean side, the largest loser industry is the agricultural sector. First, Korea is worried about the possible damaging effects of the CKF on Korean farmers, as the CKF would spark a large inflow of Chinese-grown farm products like garlic, onions, red peppers and apples into the Korean market. Second, Korea is worried about the negative impact of the CKF on Korean small and

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<sup>3</sup> Asian Development Bank

<sup>4</sup> ADB: The report assumed that both manufacturing and agriculture would be fully opened.

<sup>5</sup> SERI: The report assumed 100% opening of manufacturing sector and 50% opening of agricultural sector and accumulation of capital.

**Table 3.5 Sectoral Impact of CKF: Winner Industries and Loser Industries in China and Korea**

	Korea	China
“Losers”	Agriculture -Garlic -Onion -Red Pepper -Apple Labor intensive products	<ul style="list-style-type: none"> <li>□ Automotive</li> <li>□ Petrochemical</li> <li>□ Service</li> </ul>
“Winners”	Automotive Petrochemical Service Finance, Insurance, telecom etc.	Agriculture -Garlic -Onion -Red Pepper -Apple Labor intensive products

Source: Korea International Trade Association

medium sized companies; it is worried the CKF will cause a large inflow of the Chinese-made price-competitive, labor-intensive products into Korean market. In contrast, CKF is forecasted to benefit such ‘winner industries’ as the Korean automotive, petrochemicals and service sectors. In the service sector, Korean finance, insurance and telecommunication sectors are forecasted to be particular beneficiaries of economic gains from the CKF. Meanwhile, China’s agricultural sector and labor-intensive sector are forecasted to be winner industries, while Chinese automotive, petrochemical and service sectors would be loser industries. Although both China and Korea have researched the impact of the CKF on the Chinese and Korean economies, the reality could be different from the research. When we look at cases of FTA in the US, Mexico, Israel, etc.,

FTA produced economic effects that are totally different from earlier forecasts. One example is US-Israel FTA(1985). When the Israeli government moved to sign an FTA with the US, it faced fierce political opposition from a lot of experts. They were worried about the huge trade deficit that they would incur as a result of an FTA between a small country like Israel and a global economic superpower like the US. Twenty years later, however, it has turned out to be opposite their expectations; Israel enjoys a trade surplus with the US.

Another example is NAFTA. At that time, US farmers' organizations were opposed to signing an FTA with Mexico; American corn-growing farmers were particularly worried about the massive import of Mexican-grown cheap corns into the US market. It turns out to be different from their worries, however. USDA analysis shows that the US shipment of corn to Mexico surged from 0.91 million tons before NAFTA (became effective) to 5.8 million tons in 2003 and 7.9 million tons in 2010 after NAFTA became effective.

In Korea, farmers expected Korea's FTA with Chile to almost destroy Korean fruit farms; Korean farmers worried FTA would spark a huge inflow of cheap Chilean grapes into the Korean market, which did not happen as they had worried. Considering these situations, it would not be desirable for both countries to show too much concern about their loser industries or show political reaction to their loser industries.

What FTA means literally is mutual opening of the market. In other words, FTA presents both crisis and opportunity for both the Chinese economy and the Korean economy. It would, therefore, be in their mutual interests for both countries – business community, government officials, researchers, NGOs,

farmer's organizations, trade unions, etc. - to seek to maximize opportunity factors and to minimize risk factors of the CKF. This way, it would be in their best interest for Korea and China to work together towards achieving a common goal of win-win outcome from the agreement.

## **IV. Perspectives on the On-going Deal between China and Korea**

### **1. Negotiation Strategies of both sides of the CKF deal**

Four rounds of the working-level negotiations have been held between the Chinese government delegation and the Korean government delegation since the declaration of the two political leaders in Beijing, May, 2012. The first round of negotiations was held in Beijing on May 14, and the latest round was held in Kyungju, Korea, from Oct. 30 to Nov. 1 later in the same year.

Represented by FTA chief negotiator of Trade negotiation headquarters, the Korean delegation consisted of officials from related ministries: the Ministry of Strategy and Finance, Ministry of Knowledge and Economy, Ministry for Food, Agriculture, Forestry and Fisheries, etc. Led by Chinese commerce deputy ministry, the Chinese delegation consisted of officials from related ministries. Negotiation is under way to prepare negotiation modality by sectors, including merchandise products, non-tariff barriers, etc. Also, experts' meetings have been held to cover service, investment, IPR, etc.

It seems that both parties are conducting a 'hard-positional bargaining'.

First, the Korean government's basic position in this deal is that 'the highly sensitive agricultural products' such as rice, garlic, etc should be excluded from the CKF framework. It is just like how rice is excluded from the US-Korea FTA. However, China, expecting a significant surge in exports of agricultural products to Korea through the CKF, takes a hard position that the market opening of agricultural products should be seriously discussed in CKF negotiation. In this sense, Agriculture is the hottest issue in CKF negotiation.

Second, when it comes to negotiation strategies, Korea and China have different preferences on "how to negotiate". Korea prefers 'single-understanding approach' to 'staging approach' whereas China prefers 'staging approach' to 'single-understanding approach.' China has already signed the FTA/EPA with ASEAN, Pakistan, Taiwan, etc. by using the "staging" method; China negotiated the manufacturing sector first, then, after that, it negotiated service, IPR, investment, etc. But, Korea thinks the CKF should be comprehensive. And Korea does not expect the staging method to lead to a comprehensive FTA. Because Korea worries that if they use the staging method as China would prefer, the CKF would not lead to a satisfactory level of liberalization. Instead, Korea thinks that the staging method would lead only to partial opening of service sectors. What Korea expects from the CKF is not only the market opening of the manufacturing sector but also the opening of the service sector as well as the removal of the 'invisible trade barriers'.

## **2. Two Scenarios**

Therefore, it is extremely difficult to forecast the future direction of ongoing CKF negotiations. However, this paper proposes two very tentative scenarios for a CKF

Our prior discussion makes it clear to consider the importance of not only economic factors but also geopolitical implications when we discuss the FTA negotiation between Korea and China. Therefore, if we are to predict the future direction of the CKF deal to move forward, we can analyze the geopolitical implicational domestic political factors. Then, with the analysis, we can predict two possible scenarios on how the CKF deal would go ahead as follows:

### **Scenario 1: Hard-bargaining Game**

Despite efforts by Chinese and Korean trade officials to move negotiations forward, progress remains very limited, since both governments continue to employ hard bargaining positions in order to maximize their individual trade interests at the expense of the other. Negotiations could be described as a ‘zero-sum game’

Considering the very close economic relationship between two countries, the economic impact of the CKF is so tremendous that Chinese and Korean negotiators are highly likely to decline to make any concession in what each considers highly sensitive items. In this regard, let us consider the FTA negotiation that has unsuccessfully taken place between Korea and Japan for the past ten years. Japan could not move forward because of a strong political reaction coming from farmers' organizations,



whereas Korea was confronted by fierce political opposition coming from SME and labor unions in parts & components industries. Something similar may happen again in Korea-China negotiation for CKF, if Korea and China take similar reactions. In this scenario, CKF is likely to remain at a stalemate for more than ten years as it has been with Korea-Japan FTA.

### **Scenario 2: Dramatic Conclusion of CKF**

CKF can be concluded dramatically at a much surprisingly earlier time than expected, if the two countries' leaders, particularly from the Chinese leaders, take the 'political consideration' of CKF. As mentioned in this paper, 'super powers', US and China, are sometimes likely to have 'political FTA'. A prime example is the conclusion of the FTA between the US and Jordan in 2000, and US-Israel FTA in 1985, and China-Pakistan FTA in 2009.

In this scenario, strong political leadership, particularly from the Chinese leader plays a crucial role and political concerns override economic ones. As a result, both sides create a 'package deal' or 'give and take deal.' This means that the politically highly sensitive items would be excluded or a compromise would be reached on certain points to find a solution which satisfies not only the two negotiating sides, but also domestic constituencies.<sup>6</sup>

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<sup>6</sup> Market opening of agriculture is one of the hottest issues in trade negotiations. Korea is demanding the exclusion of a number of specific sensitive items from the FTA, including rice, beans, beef, pork, chicken, garlic, apples, pears, grapes, and oranges. The US position on the agricultural market is a hardline demand that the market be fully opened without exception. At the final stage, both sides will work toward a compromise on certain points to find a solution which satisfies not only the other side, but also domestic interest groups.

There are several reasons that support the possibility of a ‘politically considered’ conclusion of the FTA from the Chinese side.

#### 4. Trade Diversion Effect of US-Korea FTA and EU-Korea FTA

The US-Korea FTA became effective in March 2012 and the EU-Korea FTA became effective in July, 2011. This partially explains why China has increased the need to strengthen its economic relations with Korea. The US had been Korea’s largest trade partner until 2003. In 2004, China replaced the US as Korea’s largest trade partner. The bilateral trade volume between China and Korea has, since, increased from \$79 billion in 2004 to \$221 billion in 2011.

**Table 4. Korea's Major Trading Partner**

	(Billion US\$)					
	2003	2004	2006	2008	2010	2011
US	59 (15.8%)	72 (15.0%)	70 (12.2%)	85 (19.5%)	90 (10.1%)	101 (9.3%)
China	57 (15.3%)	79 (16.6%)	107 (18.6%)	168 (38.7%)	188 (21.1%)	221 (20.4%)

Source: Korea International Trade Association

There is the trade diversion effect that resulted from the US-Korea FTA and EU-Korea FTA. The trade diversion effect may weaken the China-Korea economic relationship.

#### **4. Hegemony Game in East Asia**

It is not only the economic aspect but also the political aspect that China needs to strengthen relations with Korea. China needs to forge a stronger relation with Korea, as China plays a hegemony game with the US in East Asia, and China wants to create a Greater Chinese Economic Zone (GCEZ).<sup>7</sup> In East Asia, Japan maintains a solid alliance with the US both politically and economically. But Korea plays a role as an intermediary country between the US-Japan superpowers and China.

#### **5. US ‘Trans Pacific Partnership Initiative’ vs. China’s ‘Bilateral FTA Initiative’**

The impact of Trans Pacific Partnership (TPP) is also hard to ignore. China’s trade policy to initiate economic integration by creating GCEZ in East Asia conflicts with US interests. The basic direction of US trade policy towards East Asia is to “not draw the line in the Pacific between the US and E. Asia”. As part of this policy, former US President George W. Bush unveiled the “Hanoi Vision” at the APEC Leaders’ Meeting in 2006. After that, the US proposed TPP in 2008. Now ‘P9’<sup>8</sup> countries participate in the TPP. In November 2011, Japanese Prime Minister Noda expressed his intent to join the TPP when

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<sup>7</sup> Ahn, Se Young, “Geopolitical Implications of the US-Korea and its Domestic Politics,” paper presented at the Int’l Conference organized by CSIS (Center for Strategic and Int’l Studies) & ChosunIlbo, Washington, D.C., September 26-27, 2006.

<sup>8</sup> Australia, Brunei Darussalam, Chile, Malaysia, New Zealand, Peru, Singapore, Vietnam, and the United States

he attended the Honolulu APEC Leaders' Meeting in November 2011. Confronting the US's 'TPP initiative', however, China took the 'Bilateral FTA initiative' policy. Under this initiative, China leads the regional economic integration by signing FTAs with countries in the Asian region. In order for the 'Bilateral FTA initiative' to come true, China needs to sign an FTA with Korea. If the CKF is signed, Korea would have a reduced incentive to participate in TPP because Korea has already signed an FTA with seven countries like Chile and Singapore from among the nine participating countries of P9.

## **6. Easy Domestic Politics**

As shown by Korea's experiences in FTA deals with Chile and the US, FTA negotiation is typically a 'two-level game' as Putnam said. A Level I game is the official international negotiation between two governments to sign a tentative agreement. A Level II game is the domestic negotiation to persuade diverse domestic interest groups like the national assembly, farmers' organizations or labor union for its ratification. In this regard, China is almost free from political reaction to play at the Level II game. Therefore, China would face little burden when China tries to politically conclude the FTA with Korea.

Finally, Korea also has a non-economic reason for signing an FTA with China. Because China has a significant influence on the reunification of the Korean peninsula and the six-party talks on North Korea's nuclear weapon program. Korea thinks that if CKF is concluded, they can upgrade Korea's relationship with China from 'economic partner' to 'economic alliance'.

In the second scenario, under strong leadership, the two

countries would recognize the highly-sensitive items as exceptional items to be excluded from their coverage, negotiating their way to sign the deal. For example, Korea would try to exclude some farm products such as rice or garlic from the negotiation, while China would try to exclude some of manufacturing sectors like petrochemicals from the negotiation.

## V. Conclusion

CKF is a key leverage to move forward economic integration in East Asia.<sup>9</sup> The research of this paper can lead to the conclusions as follows:

First, geopolitical and historical ties between two countries provide a strong foundation for China and Korea to have a 'Mixed-FTA',<sup>10</sup>

Second, if the China-Korea FTA deal is concluded through this kind of political leadership, it will eventually become a 'comprehensive and mid-level FTA'. The China-Korea deal will include a broad range of issues, from trade and investment to intellectual property rights, service, trade remedies, competition, and more. In this sense, the China-Korea FTA will certainly be a comprehensive one.

When it comes to highly sensitive issues that have the potential to be deal-breakers, a mid-level FTA would allow China and Korea to exclude certain items from CKF frameworks.<sup>11</sup>

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<sup>9</sup> Jianping. Zhang, "Analysis on Issues and Prospects of China-Korea FTA," The Paper for KIEP Visiting Scholar Project, Seoul, 2006.

<sup>10</sup> economic and geopolitical FTA

<sup>11</sup> During negotiations of an FTA between the US and Australia, sugar proved to be a deal

This is possible, of course, only as long as these ‘significant exceptions’ are not against the GATT/WTO regulations, particularly the GATTXXIV-8.<sup>12</sup>

For all the reasons discussed so far, a mid-level FTA would be a much more desirable outcome for both sides than not having an FTA between the two countries. Chinese and Korean negotiators must find some room for productive concessions in upcoming talks. The market-opening of Korean agriculture is a case in point. Korean farmers are demanding the exclusion of most agricultural products from the deal, whereas China is in a firm position of complete market opening.

The extent to which the China-Korea FTA will affect the two countries is not predetermined but will depend greatly on the negotiation game in upcoming rounds. While judgment must be reserved until a final deal becomes public, “Short term cost for long term gain” should be the motto to be adopted by both parties since a successful FTA could far outweigh the costs of mutual concessions on limited economic issues.

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breaker, and subsequently, was completely excluded from the US-Australia FTA.

<sup>12</sup> GATT XXIV-8: “In regard to interim agreements, the working party may in its report make appropriate recommendations on the proposed time-frame and on measures required to complete the formation of the customs union or free-trade area. It may if necessary provide for further review of the agreement.” The full text of the GATT agreement can be found at [http://www.wto.org/english/docs\\_e/legal\\_e/10-24\\_e.htm](http://www.wto.org/english/docs_e/legal_e/10-24_e.htm)

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