

Korea-Canada FTA Negotiations and the Beef Problem

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Korea-Canada FTA: Introduction

- Negotiations for this agreement began formally in 2005, with much positive anticipation
- Yet since Mar 2008, progress glacially slow
- What is stalling agreement?
 - Usual localized opposition in areas where increased import competition, adjustment costs appear high?
 - More opposition due to current recession?
 - Is there more?
 - Agriculture is particular source of conflict and delay, and the focus of this presentation

Background

- Few dispute potential value of the agreement:
 - 2-way good trade \$8.4B (2007)
 - 2-way services trade \$1B (2005)
 - 2-way investment flows \$1.1B (2006)
 - Korea is 10th largest export destination for Canada
 - Korea's is rapidly growing economy, plus access to North Asia
 - Gains to Canada from lowering of Korea's tariff and non-tariff barriers in forestry, fish and agriculture
 - Gains to Korea from lowering selected industrial product tariffs in Canada (e.g., auto tariffs=6.1%)
 - Net value to Canada estimated to be positive and high
 - Alternative, no agreement while our competitors have new FTAs with Korea, judged to be costly to Canada

Value of Korea-Canada FTA

- Potential gains high, to *both* countries
- Economies mostly complementary; few sectors competitive
 - Exceptions: parts of agriculture and manufacturing (autos, auto parts)
- But Canada-Korea trade relations widely judged by researchers in both countries to be “underperforming”

For example, compare Canada and Australia in their trade with Korea:

1996-2007 Total Trade	Growth Rates by country pair
Korea-Canada	+75%
Canada-Rest of World	+114%
Korea-Rest of World	+160%
Korea-Australia	+125%
World Trade (all countries)	+137%

Source: Table from data in Ciuriak, 2008

Value of Korea-Canada FTA

- Canadian trade with Korea can be compared with Australia as good yardstick because of many similarities w/ Canada
- Total Canadian trade with Korea growing much more slowly than Australian-Korea trade
- Applies to exports of goods, services, and investment
- Goods export stagnation striking: 1996-2007 period
 - Canada: +19% growth
 - Australia: +111% growth
- Much potential for Canada to expand exports to Korea
 - Regarding agricultural exports to Asia more broadly, same story
 - Canada substantially outcompeted by Australia in beef and pork trade to Asia since 1990
- Conclusion: CDN economic relations have underperformed; substantial gains from moving ahead, including with a FTA

Quantitative Estimates of Benefits to FTA

- 2004 estimates from CGE models of Korea and Canada (Source: Choi Se-Kyun, Seoul National University, 2006)
- Korean GDP will increase by 0.4%; Canada, GDP +0.5%
- Korean consumer welfare increases by 0.4%; Canada by 0.3%
- Exports will increase by 0.9%; Canada by 0.5%
- Korean Agricultural output will fall by US\$65 million; Canadian Ag output will incr by US\$142 million
- Korean imports of CDN meat +\$13m (low?); livestock +\$12m; dairy (net) +\$5m (Latter quite unlikely due to WTO expt subsidy ruling)
- Overall, net increase in Agric imports into Korea, +\$44m
- Conclusion: sensitive products into Korea: beef, pork, manufactured milk products, malt, potatoes, canola oil, mftd foods
- Possible Korean Exports: ramen, noodles, fresh mandarins, pears

Key Issues in Negotiations

1. Agriculture

- By far most important of all agricultural issues is removal of Korean import ban on Canadian beef, even though prior beef trade only 2-3% of total expts
- This and other agricultural exports important to Canada, worrisome for Korea

2. Autos

- Important to both countries, given this is easily the largest trade category between the two countries
- Biggest potential gain to Korea, Canadian concerns about possible domestic losses

What Canada wants most

1. Removal of import ban on beef
 - Canada used to be 4th largest import source of beef into Korea
 - Without FTA, trade diversion to US and EU substantial
2. Better market access for pork, barley; also for fisheries and forestry products
3. Reluctance to open up CDN market access for automobiles to Korea due to competition for domestic auto industry and fear of job losses
4. Gaining greater access to Korean auto market also important

What Korea wants most

1. Better access for manufactured goods, particularly autos (tariff-free access sought)
2. Exclude 240 agricultural commodities from tariff reduction (No increased access for selected agricultural products produced within Korea)
 - Particularly no access to Canadian beef, given BSE risk
 - More protection measures against possibilities of imports (broaden/extend Safeguards measures to limit damage from import surges)
 - Issues re TRQ administration (Korea tends to give TRQ access with country-specific quotas)

Barriers to Agreement: from Canada

- Auto vehicle access
 - Existing tariff small (6.1%) but some producer sector losses from opening up
 - Domestic market sales estimated to fall by only 0.5% (~2000 vehicles)
 - Korean sales estimated to incr by 9.7%
 - Most of effect would be market share losses on competing importer suppliers
 - Overall small (0.35%) decrease in average vehicle prices, increase (0.25%) in aggregate sales, decrease in margins of competing importers, increased Korean car firm margins
 - Largest effect on tariff revenue (-22%)
 - Such small effects on Canada should hardly stop agreement
 - But Korean market access key counterpart demand

(Govt of Canada estimates)

Barriers to Agreement: Canada II

- Agricultural market access in Korea: possibly most critical
- Wider market access sought for beef, pork, grains (wheat, barley, malt, flax), apples and honey, potatoes and fries, canola and soybean and their oils, maple syrup, and fish products
 - Seeking reduction of areas of high tariffs in context of overall average Korean gds tariff of 12-13%
 - Ave. tariff of 46-53% on ag products
 - Ave. tariff of 17-18% on fish products
- Willing to accept exemptions for Korea's sensitive commodities: rice, ginseng, mushrooms, hot peppers, dairy products

Barriers to Agreement: from Korea

- Concerns over industrial tariffs, especially for autos, also over standards and labelling
- But biggest barrier is agriculture
- Korea wishes to exclude 240 ag products (16.7% of all listed ag products) from tariff elimination
 - Wants longer adjustment period to tariff reduction for fruits and vegetables
 - Canada has agreed to some exemptions from tariff reductions
 - Political backdrop: Strong domestic lobby fears losing income, livelihood from reducing existing high levels of protection
- Ag Commodities where imports into Korea expected to increase: livestock products, fruit juices, livestock feed, whiskey (mostly goods with highest tariffs)
 - Maritime products where imports into Korea expected to increase: frozen lobster, crab and herring, mackeral

Focus on Agriculture/Beef

- Main issue in agricultural component if not the whole negotiations
- Key objective of Canada: re-open mkt access (2003 Korean ban on CDN imports after discovery of BSE in Canada's livestock herd)
- Canada's response to BSE discovery allowed it "controlled risk" classification (2007) by World Organization for Animal Health (OIE)
- Result: most countries, including US, accepted CDN meat imports subject to standard set of conditions (e.g., no SRMs, no meat from animals over 30 months)
- Canada and US now have same OIE classification (also UK, Japan)
 - New "normal": under 30 months, boneless meat trade
- Korea has not yet tested for BSE and has no confirmed risk status
- Korea and EU have recently completed agreement also allowing beef import access
- But despite KOR-US FTA agreement allowing US beef exports (and in KOR-EU FTA), Korea will not extend this option to Canada

Why no resolution? Two reasons

1. For Korea, desire to avoid extra competition against Korean beef producers
 - Follows long history of protection and subsidization of Korean beef sector, complete with previous GATT/WTO Panels
2. But main issue for Korea now to avoid more Korean consumer protests against foreign beef, even with v. small risk of BSE from CDN beef
 - After KORUS Agreement signed, several very large consumer protests in Seoul
 - Candlelight protests May-Aug 2008; million demonstrators in streets in total
 - Early days of Pres. Lee administration; demonstrations caught Korean govt by surprise (“miscalculated”?)
 - Strong desire to avoid a repeat; wait until protests settle down
 - Too late to stop US beef access, but not too late to stop Canadian beef;

Post-protest delays in Can-Korea FTA

- Given last year's political problems in streets of Seoul, Korean govt not unhappy with WTO Panel
- Why not await outcome of WTO Dispute Panel?
 - If ruling in favour of Korea, problem solved
 - If ruling against Korea, access for Canadian beef can be blamed on WTO rules and process, not on Korean government
- But Canada aggrieved by not only US beef access ahead of Canada (despite KORUS FTA negotiations starting a year after Canada's) but also Korea-EU FTA agreement, including beef market access (in principle)
 - sense of unfairness contributes to Canada's desire to hold out for beef agreement
- Lesser issue of negotiating capacity (analytical and legal); many trade agreements being negotiated

Is there real food safety issue re Cdn beef?

- Is BSE more prevalent in Canada than. United States?
 - More cases found in Canada (17 Cdn cows vs 2 US cows)
 - But “cattle industries in both countries are virtually identical. For example, the relative proportion of beef and dairy cattle (80% and 20% respectively), management practices (such as breeding, feeding and rearing), and slaughtering practices are essentially the same in both countries” Source: USDA risk assessment 2006
 - NA cattle industry deeply integrated; cows/meat moving across border, both directions, at different stages of production
 - Expected incidence should be similar – should be more observed cases in US than 2 (US cattle herd 7 times larger)
 - Why low observed incidence? Open question. Possible answers:
 - Under-reporting in US (some evidence)
 - Testing protocols largely ignore healthy cows; focus on high risks cases
 - Bad luck for Canada (higher initial exposure from UK)
- [Ciuriak, 2009]

WTO Challenge

- Because of no movement on issue by Korea, in April 2009 Canada undertook trade action against Korea via a WTO challenge
 - With persistence of both sides to maintain own positions, difficult for FTA negotiations to proceed until beef challenge resolved, hence Canadian action
- No further action on FTA likely until Panel reports
 - Korean and CDN business argument: Set aside beef, let Panel report, conclude FTA now without beef (\$3.5 billion in exports affected, beef accounts for max 2% of exports)
 - Canada: Politics demand beef *must* be resolved in FTA
 - plus belief WTO case is likely to be won

WTO Challenge, Details I

- 9 April 2009: Canada requested consultations w/ Korea re importation of beef meat and meat products from Canada
- 7 May 2009: Consultations held in Geneva to resolve issue; failed to settle dispute
 - Canada requested Panel to examine case under Dispute Settlement Understanding (rules and procedures governing settlement of disputes)
- 31 Aug 2009: Panel established
- Korea argues: right to SPS measures for protection of human, animal health or life, given no treatment for BSE
 - Canada has had 16 BSE outbreaks since 2003, 2 “recently”
 - Korea has never had an occurrence of BSE; SPS regulations indispensable to prevent introduction of BSE into Korea

Beef Case: WTO Challenge, Details II

- Canada argues: Korea's adopted measures place unjustified restrictions on resumption of imports of beef meat and meat products from Canada
- Canada further argues the identified measures are inconsistent with Korea's obligations under the SPS Agreement (Art 2.2, 2.3, 3.1, 3.3, 5.1, 5.5, 5.6, 8, Annex C(1a))
 - Measures not applied only to extent necessary to protect..., not based on scientific principles, maintained without sufficient scientific evidence
 - Measures unjustifiably discriminate between Members where identical conditions prevail
 - Measures not based on international standards, guidelines, recommendations... nor on proper risk assessments and techniques ...
- Canada also considers each of these measures inconsistent with following GATT provisions: Art I.1 (MFN), Art III.4 (National Treatment), Art XI.1 (Elimination of Quantitative Restrictions)
- Panel likely to report findings in ~ 9 months (i.e., summer 2010)

Merits of the WTO case

- Ciuriak [2009] argues:
- International consensus on handling BSE risk in trade
 - Korea not obliged to import from controlled risk countries but WTO commitments require consistent treatment
- Canada and US have virtually identical risk profiles
 - Korea will emphasize different reported rate of incidence
- Korea was last major market to re-open to US and still bans Canada (but HK, Taiwan, Japan, and recently China do not)
 - Consistent with history of Korean protection for beef
- Korean acceptance of US appears politically motivated – day before Camp David meeting between Korean and US presidents to facilitate KORUS
- Korea has since inked FTA with EU that in principle opens its markets to controlled risk beef from EU exporters
- Korean defense in WTO case looks tenuous
- But clinching pt: Korea-US protocol allows meat from Canadian cows that have spent 100 days in US feedlots

Economics of protecting Korean beef

- What effect of imports on high quality “Hanwoo beef”?
- Markets for imported and Hanwoo beef appear not to be well integrated
 - Price paths quite different
 - Collapse of NA beef imports post-BSE shows fall in domestic consumption, increase in Australian imports, but no effect on Korean beef production
- Conclusion: Imported beef appears to have low rate of substitution for Hanwoo beef (despite rhetoric)
- What about low quality Korean beef (mostly dairy)?
 - Casual evidence suggests closer substitution between imports and low quality Korean beef (needs further checking)
- Appears that imports only affect price of Korean dairy beef (much smaller issue)

Korean beef prices: domestic v. imported (from Ciuriak, 2009)

	2006 won/kg	2007 won/kg	2008 won/kg
Domestic beef			
1st grade			
Rib	63 424	64 192	66 816
Chuck eye	69 008	65 880	62 876
Grilled or roast beef (bulgogi)	41 314	35 750	32 968
3rd grade			
Rib	38 126	41 062	40 038
Chuck eye	47 500	41 538	37 788
Grilled or roast beef (bulgogi)	34 762	31 222	28 130
Australian beef			
Chilled			
Rib	25 154	22 538	22 038
Chuck eye	44 002	40 050	41 112
Grilled or roast beef (bulgogi)	14 262	13 410	15 024
Frozen			
Rib	19 000	18 714	19 034
Chuck eye	12 194	11 736	12 548
Grilled or roast beef (bulgogi)	10 450	9 660	10 638

Note: (1) The average exchange rates for 2006, 2007 and 2008 were 956 won, 929 won and 1103 won per US dollar, respectively. (2) Prices of imported Australian beef cuts are compared, as Australian beef accounted for the majority of Republic of Korea's total beef imports. Price data for US beef cuts over this period are not available.

Source: KAMIS 2008.

Korean beef imports and production following BSE ban on NA imports (from Ciuriak, 2009)

TABLE 6.1 Beef: Korea's production, consumption, trade, and key factors affecting demand, 2002–07

Market data	2002	2003	2004	2005	2006	2007
Beginning stocks (1,000 mt cwe)	25	40	61	1	3	5
Production (1,000 mt cwe)	192	182	186	195	200	205
Imports (1,000 mt cwe)	442	457	224	250	298	315
Total supply (1,000 mt cwe)	659	679	471	446	501	525
Exports (1,000 mt cwe)	0	0	0	0	0	0
Domestic consumption (1,000 mt cwe)	619	618	470	443	496	515
Ending stocks	40	61	1	3	5	10
Exchange rate (KR won/U.S.\$)	1,251.10	1,191.60	1,145.30	1,024.10	954.8	929.3
GDP/capita (U.S.\$/person)	11,504	12,711	14,181	16,444	18,392	19,624
Population (millions)	47.6	47.9	48	48.1	48.3	48.4
Wholesale beef price index	100	99	92	115	115	122
Annual beef per capita consumption (kg)	13.0	12.8	9.7	9.1	10.2	10.5

Source: Production, consumption, and trade data from USDA, FAS, unless otherwise noted. Exchange rate, GDP per capita, and population data from IMF. Wholesale beef price index calculated from FAPRI database.

Economics of protecting Korean beef II

- In NA beef market, deep integration does not allow sustained price differentials to emerge between Canadian and US beef
 - Tightening supply situation from US exports to Korea results in increased shipments from Canada to US
 - Prior to health issues, Canadian beef was regarded as highly comparable to US beef by Korean consumers
- When exported to Korea, price premium enjoyed by exporters
- Therefore: Main impact of current Korean ban is on who gets the premium in shipping to the Korean market – Canadian or US exporters, producers
 - Korean production little affected

Conclusions

- 2 key reasons for lack of progress
- Beef: reluctance of Korea to accept Canadian beef imports, substantially due to political opposition by consumers and farmers
 - Complicated by Korean acceptance of US beef, Canada meeting internationally-agreed animal health standards; Cdn beef exported via US is ok
 - Different interpretation of rights and protections of WTO SPS agreement between Korea and Canada
 - Must now await outcome of WTO Panel; possibly a precursor to concluding FTA, which means no earlier than 3rd quarter, 2010
- Barrier on Canadian side of protecting auto industry
 - Resolvable: no reason for this to be serious barrier (very small loss to industry, overall gains to Canada, econ. recovery)
 - With Korean auto assembly plants opening in US, Korean autos will soon enjoy duty-free NAFTA access to Canada anyway

Resolving Korean beef protection issues

- Generally (“overly”) pessimistic view in Korea of agric. sector’s ability to adapt under increased import competition
- But high quality beef sector not actually at risk from imports
- For low quality beef sector
 - Alternative strategies for industry’s commercial success and policy support could be given more consideration
 - Many adjustment policies possible to assist agricultural sector
 - Research into lower costs, higher value production (e.g., organic, niche mkts)
 - Selected adjustment grants for adopting chosen measures
 - Government stabilization policies
 - Private/public marketing programs to encourage buying of Korean products
 - Compensation payments to those in income distress (as has already been argued many times in Korean press)
- No comparative advantage
- If these issues given more attention, one barrier to the Korea-Canada FTA could be removed

Resolving Consumer Issues

- Consumer protests were against US beef and especially *manner* in which FTA agreed (apparent US pressure to secure KORUS FTA, trade trumping health)
 - Not at all clear Canadian beef would cause same sensitivity
 - Political security of current administration greater now; may not be so worried about such protests
- WTO Panel case offers politically attractive resolution for Korean government
- WTO-related question: Is this case where consumers, on a scientifically valid basis or not, do not want trade in certain products opened up, similar to
 - GM products and Beef Hormone cases in EU
- Not at all clear this is dominant issue
- But if so, it may be another case where consumers, rather than producers are demanding protection, raising question, do existing WTO SPS rules cope well enough?