

## Impacts of US Protectionism on Korea

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US President Donald Trump's pledges for trade policy is expected to deepen the trend of ever-growing protectionism. His trade policy can be categorized into three lines; re-negotiation or abolition of free trade agreements, tariff and non-tariff measures to pressure trade partners, and stronger trade pressure via currency manipulator designation. Korea should improve readiness to deal with various possibilities, such as the renegotiation of the Korea-US FTA, slowed exports to the US due to non-tariff measures including import restrictions, decreased exports to China due to the intensified US-China trade conflict, currency manipulator designation, etc. Taking all of those possibilities into account, Korea should fully review the Korea-US FTA in advance, assess the impact of non-tariff measures on the Korean economy, devise possible countermeasures, and consider higher flexibility in its foreign exchange market policy.

Since globalization became a buzzword in the 1990s, many countries have competitively joined free trade agreements in a bid to maximize their economic benefits from free trade. As a result, tariff rates have continuously fell. On the other hand, the level of non-tariff measures has climbed up for the sake of trade protectionism. US President Donald Trump's pledges for trade policy, under the circumstances, is expected to solidify the protectionism trend via various tariff and non-tariff measures. Taken this into account, it is time for Korea to assess the impacts of US policies on the Korean economy, and draw out the implications.

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\* All opinions expressed in this paper represent the author's personal views and thus should not be interpreted as Korea Capital Market Institute's official position.

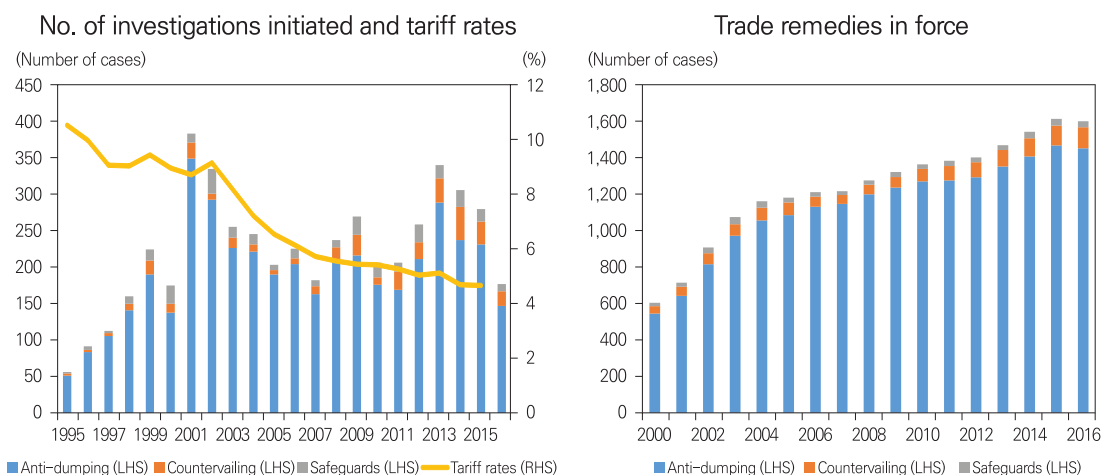
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### Non-tariff measures

Non-tariff measures refer to either the trade remedies stipulated in the GATT or WTO agreements, or a series of domestic regulations and measures in place for the sake of safety, environment, and public health, etc. Legitimate trade remedies include anti-dumping,<sup>1)</sup> countervailing,<sup>2)</sup> and safeguard<sup>3)</sup> measures, etc. Because trade remedies can be adopted by an importing country either in response to any unfair trade activity of its trading partner, or in an attempt to protect domestic industries, they are viewed as a common barometer for a country's protectionism. Figure 1 shows that the number of trade remedy cases initiated by the WTO every year peaked in 2001 before moving in a downward trend, but resumed its upward trend in the 2010s to top in 2013 before declining again.

However, the number of trade remedies actually being implemented has been on the rise since 2013 as shown in Figure 1 because trade remedies once coming into force tend to prolong for several years before being scrapped. This evidences ever-growing protectionism in global trade.

**Figure 1. Trade remedies**



Note: 1) Trade remedy data are as of the third quarter of 2016, while tariff rates refer to effective tariff rate data as of 2015.

2) The number of trade remedies actually imposed are the sum of the remedies actually being implemented in that year among the remedies imposed between 1995 and the third quarter of 2016.

Source: WTO; WITS.

- 1) Article 6 of the GATT allows countries to impose anti-dumping tariffs on the imported products that are dumped to cause material injury to the competing domestic industry. If any anti-dumping action causes injury, an extra duty equal to the difference between the product's export price and the nominal value is charged.
- 2) Countervailing measures are in general taken by an importing country to increase the duty for the purpose of offsetting any subsidy given to the manufacturer or exporter of an exporting country.
- 3) Safeguards under Article 19 of the GATT are a measure to protect a domestic industry from any unexpected increase in imports. If imports of a certain product rise too rapidly to cause injury to domestic businesses, the importing country can take import restrictions by increasing the import duty or allocating an import quota.

### **President Trump's trade policy**

Such a strengthening of protectionism based on trade remedies is expected to deepen under Donald Trump's presidency. Although there is no clear picture about his trade policy, his campaign pledges for trade policy seem to head in three directions: abolishing or renegotiating trade agreements; imposing tariff and non-tariff measures; and designating a trade partner a currency manipulator. The first direction includes dropping out of the Trans-Pacific Partnership (TPP), and immediately renegotiating NAFTA. Also included are plans to abolish existing trade agreements if no progress is made on renegotiation. Second, tariff and non-tariff measures are to be included, such as imposing high tariffs on China and Mexico with which the US runs the highest trade deficit, and bolstering monitoring on any violation of trade agreements, bringing any unfair trade activity to the WTO, and other tariff and non-tariff measures using existing trade laws. The last policy direction is about designating China as a currency manipulator because of China's alleged currency devaluation for running trade surpluses against the US.

President Trump's campaign pledges related to trade suggests a high possibility of "America first" protectionism going forward. The proposed measures mentioned above, such as trade retaliation and high tariffs against China and Mexico, reveal the new administration's sensitivity to the adverse effects of those trading partners' increasing exports on the weakening of US manufacturing and consequent job losses. A prominent case evidencing Trump's aversion to job losses was his reaction to the automobile industry's plan to build a manufacturing facility in Mexico. After Trump's pressure to impose higher tariffs on GM and Toyota cars manufactured overseas when those cars are imported to the US, those car makers announced their new plan to build additional facilities in the US.

**Table 1. Trump's pledges for trade policy**

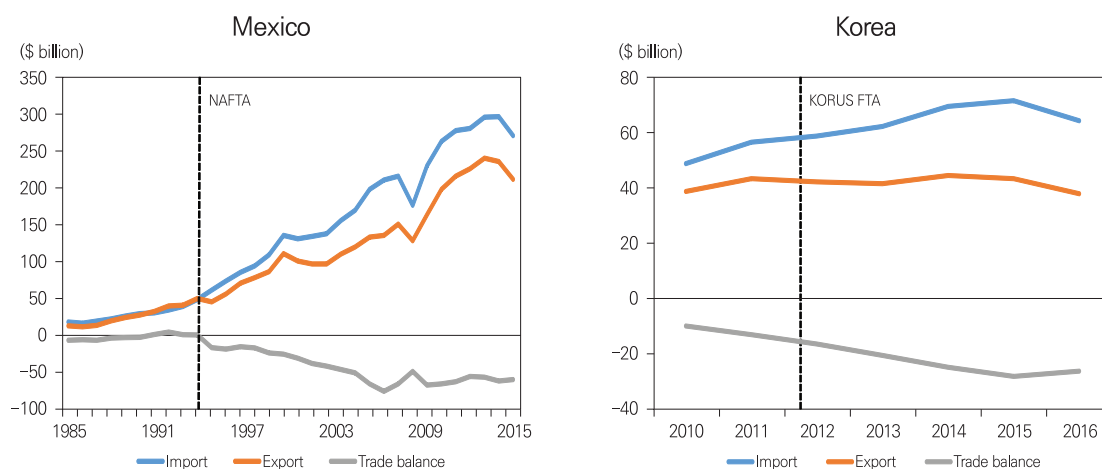
	Details
Abolition and renegotiation of trade agreements	<ul style="list-style-type: none"> <li>• Abolish the TPP</li> <li>• Renegotiate trade agreements such as NAFTA, and abolish them if renegotiation is impossible</li> </ul>
Impose tariff and non-tariff measures	<ul style="list-style-type: none"> <li>• Impose retaliatory tariffs on China and Mexico</li> <li>• Strengthen monitoring on violations against trade agreements</li> <li>• File the WTO complaint on China's illegal export subsidies and other unfair trade practices</li> <li>• Implement tariff and non-tariff trade remedies stipulated in Section 201 of the Trade Act, and Section 232 of the Trade Expansion Act</li> </ul>
Currency manipulator designation	<ul style="list-style-type: none"> <li>• Designate China as a currency manipulator</li> </ul>

Source: [www.donaldtrump.com](http://www.donaldtrump.com).

### Impacts of US trade policy on the Korean economy

President Trump's campaign pledges for trade policy are expected to have certain impacts on the Korean economy. First, Korea should prepare for a possible renegotiation of the Korea-US FTA. Trump's negative view on trade agreements stems from those agreements' ineffectiveness to improve the US trade balance. Figure 2 presents the US trade balance against Mexico and Korea after the Korea-US FTA and NAFTA took into effect. The US trade deficit against Mexico jumped dramatically from 1995, a year after NAFTA came into effect in January 1994. The primary cause behind this was a large increase in US imports in terms of dollar amount.

**Figure 2. US trade balance against Mexico and Korea**



Note: The 2016 data are for January through November 2016.

Source: US Census.

Since the Korea-US FTA officially entered into force on March 15, 2012, US imports of Korean goods have persistently grown for four years, whereas US exports stalled at \$43.45 billion in 2015 and \$43.46 billion in 2011. This exacerbated the US trade deficit against Korea from \$10.05 billion in 2010 to \$28.33 billion in 2015 and \$26.47 billion in November 2016.

The rising US trade deficit after the FTA seems only natural given emerging markets' edge in manufacturing. Also, the trade balance excludes other high-value areas besides manufacturing, e.g., financial and service industries where the US has the upper hand. However, President Trump is deeply concerned about job losses in manufacturing, which makes a negative stance in trade agreements more likely going forward. Under the circumstances, the US will possibly call for renegotiations of existing FTAs, with the Korea-US FTA and NAFTA being the most likely target.

Furthermore, it is important to note that Korea can be affected both directly and indirectly by US tariff and non-tariff trade remedies although those remedies primarily target China and Mexico. Such targeting is largely attributable to the US trade balance. As of 2016, the US trade deficit reached \$319.28 billion against China, and \$58.79 billion against Mexico, the first and fourth largest, respectively. Among emerging markets, the US has run huge trade deficits against Vietnam and Korea. Hence, Korea may be affected to a certain degree if the new Trump administration bolsters protectionism. An increase in non-tariff measures can have adverse effects on Korean exports in both direct and indirect ways. If the US imposes a non-tariff trade remedy on Korean products, Korean exports of the affected products to the US will be directly hit. If the US imposes a trade remedy on China, this will slow Chinese exports to the US, which in turn has indirect, negative impacts on Korean exports to China.

**Table 2. Export increase rates under US import restrictions**

(Unit: %)

Items Affected	Measures	Initiation	Average Export Increase Rate	
			Without Restrictions	With Restrictions
Hot-rolled steel flat products	Anti-dumping/ Countervailing	Sep. 1, 2015	0.48	-7.21
Cold-rolled steel flat products	Anti-dumping/ Countervailing	Aug. 17, 2015	0.30	-3.13
Heavy walled rectangular welded carbon steel pipes	Anti-dumping	Jul. 21, 2015	1.31	-6.03
Corrosion-resistant steel products	Anti-dumping/ Countervailing	Jun. 23, 2015	0.57	-0.52
Welded line pipes	Anti-dumping	Nov. 5, 2014	2.12	-3.37
Steel nails	Anti-dumping	Jun. 19, 2014	-0.38	-0.32
Non-oriented electrical steel	Anti-dumping	Oct. 22, 2013	-0.88	-2.45
Oil country tubular goods	Anti-dumping	Jul. 10, 2013	10.69	-0.04
Residential washers	Anti-dumping/ Countervailing	Jan. 9, 2012	2.36	-1.21
Large power transformers	Anti-dumping	Jul. 14, 2011	1.51	0.49
Light-walled rectangular pipes	Anti-dumping	Jul. 18, 2007	-17.35	0.97
Prestressed concrete steel wire strand	Anti-dumping	Feb. 27, 2003	0.13	-0.06
<b>Average</b>			<b>0.07</b>	<b>-1.91</b>

Note: The figures indicate the monthly export increase rate computed by adding up the exports of each item affected by US import restrictions (in terms of 6-digit HS Codes) during the period between January 2000 and December 2016.

Source: Korea International Trade Association (ntb.kita.net); Korea Customs Service.

As of December 2016, a total of 184 trade remedies have been imposed on Korea. By country, restrictions by India, the US, and China accounted for about 37% of the total, while steel, metal, and chemical (75%) and textile (7.6%) were the mostly affected areas.<sup>4)</sup> As of 2016, the number of import restrictions in force by the US against Korea amounted to 18, of which 12 were anti-dumping and 6 anti-dumping/countervailing measures. To find out the impacts of US trade remedies on Korean exports, I looked at the differences between export increase rates of 12

4) Korea International Trade Association, Monthly Review on Import Restrictions on Korea, December 2016.

measures initiated after 2000, out of the total 18 measures currently in force. The result shows that the monthly export increase rate during the periods unaffected by the measures averaged to 0.07%, while that during the affected periods reached -1.91%, evidencing the substantial, negative impacts of trade remedies on Korean exports.<sup>5)</sup> Although it is difficult to assess the indirect, negative impact, the Bank of Korea (2016) estimated that a 10% decrease in Chinese exports to the US would lead to a 0.36% cut in Korean exports.<sup>6)</sup> This implies that stronger protectionism resulting from the trade conflict between the US and China will have indirect and negative impacts on Korean exports.

The last direction related to currency manipulator designation targets China, but this issue may have grave impacts on Korea as well. In his pledges for trade policy, President Trump promised to name China an FX manipulator, suggesting his heavy focus on the impact of artificial currency devaluation on the US trade balance. The US Department of the Treasury unveils a semi-annual FX report, via which to set out the criteria to be named as a currency manipulator and to be included in the Monitoring List. A country is designated as a currency manipulator if meeting all of the following three criteria: 1) its trade surplus against the US exceeds \$20 billion per year; 2) the current account surplus over GDP is larger than 3%; and 3) it intervenes in the FX market for the purpose of devaluing the currency (a net purchase of foreign currency amounting to over 2% of GDP, or a net purchase for more than 8-month out of the recent 12-month). A country will be designated as a currency manipulator if meeting all three criteria, and be included in the monitoring list if meeting two out of the three criteria. The FX report unveiled in October 2016 listed six countries including Korea, China, Germany, Japan, Taiwan, and Switzerland on the monitoring list. Although China meets the trade surplus criterion only, it was included in the list because of the provision stating that any country once included in the monitoring list shall stay listed at least for two times. Under the 2016 Bennet-Hatch-Carper amendment, any country designated as a currency manipulator will be subject to various sanctions, e.g., international sanctions via the IMF and WTO, a restriction on attracting investments from US firms, and a ban on firms in the country from entering the US procurement market.<sup>7)</sup>

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5) To find out the increase rates of Korean exports to the US that are subject to US import restrictions, I used the Korea Customs Service data on imports and exports by country and item. However, the data are available from 2000, so that the four cases of anti-dumping and two cases of anti-dumping/countervailing that occurred before 2000 were excluded from the analysis.

6) Bank of Korea, Final destinations of Korean exports to China and impacts of US trade protectionism on Korea's economy, Press Release, December 7, 2016.

7) Seong-Hoon Kim, Bennet-Hatch-Carper amendment and implications, Korea Economic Research Institute, KERI Brief 16-05, 2016.

China's trade surplus against the US exceeded \$20 billion, whereas its current account balance relative to GDP remained below 3%, slightly falling for the recent four quarters from 3% in 2015 to 2.4% in the second quarter of 2016.<sup>8)</sup> Rather, Chinese authorities have net sold dollar in the FX market since its currency depreciated amid concerns over capital outflows in 2016, which is not applicable to the FX market intervention criterion. Given the fact, it is impossible to label China a currency manipulator, and will be impossible to do so without making any amendments on the designation criteria. It is worth noting that China satisfies one criterion whereas Korea meets two criteria. If China is named as a currency manipulator, so will Korea. As of October 2016, Korea was included in the monitoring list because it met the trade deficit criterion and the current account balance relative to GDP criterion. However, the FX market intervention criterion was not applicable for Korea. Given that Korea's trade surplus and current account balance are expected to remain status quo going forward, caution is necessary when policy authorities implement FX market policy actions. Especially, a balance should be considered when they carry out smoothing operations.

**Table 3. Currency manipulator criteria**

	Trade Surplus (\$ billion)	Current Account/GDP (%)	FX Market Intervention	
			Net Purchase/GDP (%)	Continuous FX Market Intervention
China	356.1	2.4	-5.1	×
Germany	71.1	9.1	-	×
Japan	67.6	3.7	0.0	×
Mexico	62.6	2.0	2.2	×
Korea	30.2	7.9	-1.8	×
Italy	28.3	2.3	-	×
India	24.0	-0.8	0.3	×
France	18.0	0.4	-	×
Taiwan	13.6	14.8	2.5	○
Switzerland	12.9	10.0	9.1	○
Canada	11.2	-3.4	0.0	×
UK	-0.3	-5.7	0.0	×

Note: Trade surplus data are the sum of the trade balance for the recent four quarters before the announcement.

Source: US Department of the Treasury.

8) The World Economic Outlook by the IMF forecast that China's current account to GDP would reach 2.4% in 2016, and 1.6% in 2017.



### Implications

Globally, trade protectionism via non-tariff barriers has increased, rather than decreased. In addition, the US's trade protectionism is expected to grow further given President Trump's pledges to impose tariffs on China and Mexico, strengthen non-tariff measures, and to respond aggressively to currency manipulation.

In response to the growing trade protectionist moves, Korea should remain wary of the followings. First, Korea should analyze the losses and gains from the existing Korea-US FTA and formulate its counterplans against a potential renegotiation request from the US. If the US toughens non-tariff measures and import restrictions, this will surely slow Korean exports to the US, and possibly lead to indirect impacts because a deepening trade conflict between the US and China will affect Korean exports to China. Thus, both indirect and direct impacts should be thoroughly monitored. Last, policy authorities should carefully cope with the US's currency manipulator designation. Because it is impossible for Korea to move away from the trade surplus and current account/GDP criteria in the short run, Korea's FX market policy should head toward flexible, carefully-planned smoothing operations considering the currency manipulator criteria.