



PROGRESSIVE ECONOMY POLICY MEMO: FTAS WITH COLOMBIA, KOREA, AND PANAMA SHOULD PASS

Ed Gresser
Director, ProgressiveEconomy
October 7, 2011

The United States needs a source of growth to revive a sluggish post-crisis economy and begin creating jobs again. America's reduced family wealth and changing savings habits suggest that this source of growth is likely to be abroad rather than at home. Therefore the U.S. needs exports to grow, and the three free trade agreements with Korea, Panama, and Colombia provide an immediate opportunity. They should pass speedily.

INTRODUCTION: Each agreement is an intensively negotiated (in fact twice re-negotiated) document which scraps border barriers, contains in-depth sections dealing with services trade, intellectual property, and Internet issues, and has labor and environmental sections based on full enforcement of domestic law and international standards. The agreements with Panama and Colombia are accompanied by new accords, respectively covering tax transparency and labor rights. In all these areas they ask a lot of our partners, and relatively little from the U.S.

The debate over these agreements has continued for five years. This leaves relatively little new to say about the topics which have received the most attention – the labor, environmental, and automotive policies renegotiated between 2007 and 2011; the possibility of tariff differentials diverting trade away from American products should the agreements not pass; and the agreements' significance for American strategic relationships with allies in Asia and Latin America. Rather than repeat often-made points on these issues, therefore, this memo will offer looks at four other aspects of the agreements which have received less attention:

- (1) The basic case for exports in America's recovery from the crisis;
- (2) The relevance of tariff reform, seen through the lens of the Colombia agreement;
- (3) The value of services-trade liberalization, with the Korea agreement as an example;
- (4) The potential export value of opening government procurement markets, with the Panama agreement as an especially important current case.

(1) **GROWTH THROUGH EXPORTS:** Since the 2008-2009 financial crisis, exports have grown more important to the United States than at any time since the early 19th century. This is because American family wealth has plunged since the crisis, changing the public's habits profoundly, and in ways that make a return to growth led by domestic demand difficult.

Federal Reserve data show family wealth embodied in houses down from \$13 trillion in 2007 to \$7 trillion in 2011. This lost paper wealth was a foundation of family planning for retirement and a cushion in the event of job loss. As it disappears, families are responding by saving: annual personal savings has risen from \$250 billion in the years before the crisis to \$600 billion. This is a shift of nearly 3 percent of GDP from domestic consumption to savings. That in turn means domestic businesses remain depressed - for an illustrative case, new car sales have dropped from 16 million in 2006 to 11.5 million in 2010ⁱ - and are unlikely to regain their strength until families rebuild their lost wealth. This in turn creates a cycle typical of depressed economies, in which low demand makes even profitable businesses wary of investing and hiring - which in turn keeps unemployment high and further reduces consumer confidence. In this environment, the best hope for growth is to tap foreign demand through exports, which is why President Obama calls for a doubling of exports by 2014.

To some extent export growth is happening on its own. With WTO agreements keeping world markets open, and businesses looking for foreign customers to replace lost domestic demand, U.S. exports have risen from \$1.5 trillion to \$2.2 trillion since 2009, or from 11 percent to 14 percent of GDP. But anything government policy can do to accelerate the process is a good thing - and the three agreements are a chance to do so.

(2) THE PARTNERS & THE AGREEMENTS: Korea, Panama, and Colombia are considerable buyers of American goods and services. Korea is the US' 7th-largest overall export market, and ranks 5th for farm products and 4th for seafood, as well as America's largest supplier of computer chips and electric guitars, and a partner in education and scientific research. Colombians, enjoying an economic boom as a long civil war approaches its end, doubled their purchases of American goods from \$5 billion to \$11 billion between 2005 and 2010. And Panama, though a small nation of 3 million, buys more American goods than much larger countries like Russia or South Africa - and ranks 3rd among the world's 195 countries as a per capita buyer of American goods.

The agreements thus build on fairly large and very successful trade relationships. Reviews done by International Trade Commission staff suggest they can add \$12 billion in export growth above existing trends. (And similar reviews of earlier agreements, for example of the US-Peru agreement in 2007 underestimated the export growth that actually followed implementation of the agreements.) The three agreements also take up important and little-understood issues which offer benefits that analyses like those of the ITC cannot yet quantify, but are also good arguments in the agreements' favor. A quick look at each helps to illustrate:

(a) Colombia & Tariffs: As trade debates focus more intently on advanced issues such as electronic commerce, labor and environmental chapters, product approvals, and similar topics, tariff policy has acquired an image as being boring and of diminishing relevance. This is mistaken. American exporters and American shoppers alike can gain much from tariff reform, in general and in the U.S.-Colombia agreement.

American tariffs average about 1.3 percent. This is not the world's lowest rate - Hong Kong and Singapore have no tariff systems at all - but is well below the world average. In dollar terms, the

U.S. collected \$26 billion on \$2.4 trillion in imports in 2010, while foreign governments likely imposed more than \$40 billion in tariffs on America's \$1.9 trillion in exports.

Colombia is a typical case. Its tariff system averages about 11 percent, which is a standard figure for South America. In practice this meant a \$1 billion tariff penalty on the \$11 billion in planes, cars, jewelry, foods, mining equipment, and other American exports to Colombia. The tariffs will disappear with the agreement in force. By contrast, the United States has essentially no tariffs on Colombian goods. (To be precise, last year the Customs Bureau collected \$9 million in tariffs on \$15 billion in Colombian goods.) This reflects the fact that U.S. tariffs on resources like emeralds and tropical agriculture products like coffee are permanently zero, and a special developing-country preference system known as the Andean Trade Preference Act (ATPA) waives those normally applied to other major Colombian exports like flowers, jewelry, and clothes.

In these circumstances, tariff elimination in the Colombia agreement – and by extension other agreements – has great value for Americans. Removing the residual U.S. tariffs will be no burden for American businesses. Making the ATPA permanent, meanwhile, will be a friendly step for American shoppers because it will keep prices low for some consumer goods. Some of the largest benefits will go to couples at Valentine's Day, as about half the V-Day roses sold in American florist shops are flown in from winter gardens around Bogota. These flowers normally would have a 6.5 percent tariff, meaning that the agreement will permanently reduce couples' Valentine costs each year from \$5 million to \$10 million, while simultaneously allowing florists to earn a bit more money on every stem.

(b) *Korea & Services*: About a third of America's exports are services like movies and news, health care delivered via telemedicine, education at American universities, loans and insurance policies, express delivery fees, and so on. These exports support especially skilled, technically advanced, and high-wage industries; and the U.S. relies more heavily on these exports than any major economy but Britain. The U.S. in fact exports 3 more services than the world's 2nd and 3rd-ranking services exporters combined. With open markets, this is likely to be a great source of strength for the United States in the decades ahead, as the global Internet creates a world market in services comparable to those which exist now in manufactured goods, agriculture, and natural resources.

Like many newly industrialized states, Korea has become a very large American manufacturing and agricultural market, but retains many limits on services exports. It is therefore only a medium-tier buyer of American services at \$13 billion in 2009, a total comparable to mid-sized European countries like Switzerland and the Netherlands. KORUS, likely the most sophisticated and thorough services agreement the United States has ever negotiated, is likely to transform this situation. It includes market access guarantees for almost all services industries, and helps to develop new high-tech delivery methods through guarantees of open e-commerce and movement of data. This is especially important, given Korea's status as one of the world's most wired and technologically sophisticated economies.

(c) *Panama & Government Procurement* – Government public works projects are among the world's biggest buyers of heavy-industry manufacturing, engineering services, and computer

systems design, and similar big-ticket goods and services. In the United States, governments at federal, state, and local levels offer about \$500 billion in such contracts each year, and the totals abroad are proportionately higher.

American procurement programs are usually (though not always) open to foreign companies. This is good for taxpayers because it keeps down costs, and also good for producers as long as foreign procurement markets are reciprocally open to American bids. Most developed countries are open, because of the WTO's Government Procurement Agreement. Most developing countries are not. FTAs can eliminate the imbalance, and have done so in cases like Morocco, Chile, Mexico, and Central America. Panama is an unusually important case, as its \$5.25 billion re-digging of the Panama Canal to accommodate modern container ships and tankers is among the largest public-works projects in the world today. The agreement's government procurement clauses will create a mutually open procurement market, ensuring a favored place for American engineering, heavy manufacturing, and similar big industries as the Canal project's contracts go out, and of course as Panama pursues other public works projects and routine procurement.

CONCLUSION: Finally, the more familiar arguments for the agreements are frequently stated but still correct. They are professionally done accords with friendly governments and important trade partners. They have been renegotiated twice to meet a long list of progressive concerns. Failure to pass them will risk placing American farmers and factories at tariff disadvantages in competition with other countries. And they will provide an important boost to the American economy at a time when we badly need it. It is time for them to pass.

ⁱ Department of Commerce, Office of Automotive Affairs, "WQuick Facts," at http://trade.gov/wcm/groups/internet/@trade/@mas/@man/@aai/documents/web_content/auto_stats_mv_qfacts_pdf.pdf; visited 9/29/2011.