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The Impacts of US Agricultural and Trade Policy on Trade Liberalization and Integration via a US-Central American Free Trade Agreement

Dale Hathaway

Special Initiative on Trade and Integration

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This document is part of the first component of the Initiative.

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THE IMPACTS OF US AGRICULTURAL AND TRADE POLICY ON TRADE LIBERALIZATION AND INTEGRATION VIA A US-CENTRAL AMERICAN FREE TRADE AGREEMENT

Dale Hathaway [*]

This study looks at several major legislative actions in 2002 that will substantially affect trade negotiations with the United States, and examines the US import protection for agricultural products that will be critical in trade negotiations with Central American countries.

The two important legislative actions were the passage of the 2002 Farm Bill and the passage of Trade Promotion Authority, which provides for "fast track" treatment of trade agreements.

The 2002 farm bill was widely denounced as a major reversal of US farm policy, away from the earlier move toward reduced levels of support and toward decoupled supports for key commodities. In fact, however, the 2002 farm bill contained the same support mechanisms that were in the highly touted 1996 farm bill. The support levels for some commodities were raised, but the projected spending under the new legislation is at the same level as the subsidy levels for the supported commodities as was spent in the immediately preceding year. Even though the changes in the policies were less drastic than the critics claim, the US domestic subsidy programs are a major barrier to the achievement of a successful regional free trade agreement. It is unrealistic to believe that countries will open their domestic markets and local producers to competition from highly subsidized US commodity producers.

The 2002 farm bill also reauthorizes the various export programs that the US government uses to support the increased exports of US farm products. The most important of these is the export credit programs that include some elements of subsidies to commodity exports. However, these programs are not likely to create significant problems in a regional trade agreement since they are of primary concern to competing exporters. The various market development programs appear to have little or no market distorting effects. The direct US export subsidies are limited to a modest program on manufactured dairy products and should not be a problem for a regional free trade agreement.

The Trade Promotion Authority contains several new restrictions on US negotiators. It lays out a list of sensitive agricultural products and requires special procedures before any negotiations to liberalize access can occur. The list of US sensitive products includes a number of agricultural products of particular interest to Central American countries. Many of these products are already under TRQs in the US, and in some cases the survival of domestic programs are dependent upon the continued restriction of imports.

In addition to the list of sensitive products the US has some significant tariffs on a number of products that the Central American countries export to the US. Elimination of these tariffs can provide significant gains in market access for some products.

In summary, the successful negotiation and approval of a US-CAFTA will require major political will on both sides to overcome the major hurdles that exist.

INTRODUCTION

This paper assesses the implications of several major US legislative and executive actions on the issues of importance in negotiating a US-Central American Free Trade Agreement (US-CAFTA). It looks briefly at the political interest groups that dominate US domestic and international trade

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policy in agriculture, examines the legislation that will shape the US positions in the trade negotiations, and assesses the implications of these measures for the possible integration of US and Central American markets for agricultural products.

Under the United States Constitution the authority to deal with international trade rests with the Congress. The authority to negotiate trade agreements is delegated to the executive branch by congressional action, but the rules which accompany the delegation of authority generally reflect the same political pressures underlying domestic and international policy in agriculture.

The Congress also largely determines agricultural policy in the United States. Thus, the same political forces that influence domestic agricultural policy are dominant in the congressional actions regarding agricultural trade.

In the United States a number of key commodity groups, two general farm organizations, and their allies in the processing and exporting industries heavily influence agricultural policy. In the US system the crucial decision-making groups in the Congress relating to agricultural issues are the Committee on Agriculture of the House of Representatives, and the Senate Committee on Agriculture and Forestry. These two committees consist of individuals mostly representing states are heavily supported and lobbied by the commodity groups and their allies.

Some commodity groups have great political influence. Two of the most influential groups are the alliance of sugar and sweetener producers (including the corn growers) and sugar processors, and the organizations of dairy producers. Their strong influence is partly due to the location of the industries and partly due to their willingness to spend substantial amounts of money to support or oppose individual political candidates.

It should be noted that the commodity groups and their allies are groups whose economic base is in domestic production and exports. Consumer groups have little or no influence in agricultural support and trade policy, but the agricultural industry has made a truce with environmental groups so that current agricultural policies contain a substantial element of environmental protection.

During 2002 the US Congress passed two major pieces of legislation that will have significant impact on the ongoing and pending trade negotiations in the World Trade Organization (WTO), the FTAA, and CAFTA. They are the 2002 Farm Bill and the Trade Promotion Authority (TPA) that provides the executive branch with the authority to engage in trade negotiations and the legislative rules needed to approve trade agreements after they are negotiated. In addition in July 2002 US trade negotiators presented the US proposals for modalities to be used in the Doha Round of agricultural negotiations already underway in Geneva.

This report analyses each of these three policy documents and discusses their probable impact on the negotiations for a US-CAFTA.

SOME BACKGROUND OF CURRENT US FARM POLICY

The US government began its intervention in agricultural commodity markets in the 1930s. The original crops that were supported were corn, wheat, cotton, rice, peanuts, and tobacco. Domestic sugar production also was protected beginning in the 1930s. By the 1950s the list of supported commodities expanded to include soybeans and dairy products.

The original policy was to support the market price of the protected products. This was accomplished by direct government purchases, supply controls, and price support loans to producers. The policy instrument of non-recourse loans to producers was developed and the level of loan rates became the major focus of policy debates.

Under this program producers were eligible to receive a loan for their commodity at the support level. At the end of some specified period they were required either to repay the loan plus interest, or in lieu of repayment, deliver the product to the government. If the loan rates were above the world market price, exports were impossible without export subsidies, and if the loan rates were above market prices the government accumulated stocks of the supported commodities. Over time the commodity loan programs developed serious problems of surplus stock accumulation, but despite these problems the use of non-recourse loans persisted for the next 70 years.

These difficulties were recognized shortly after World War II and in 1949 the Truman administration proposed a shift to direct payments to farmers in a proposal called the Brannan Plan. US farm groups, especially the American Farm Bureau, strongly opposed the use of direct payments to farmers, and the plan was defeated. It is interesting to note that the Farm Bureau claimed that farmers wanted their income from the market place and would not accept direct government payments.

Throughout the 1950s and 1960s there was a continuing battle over loan rate levels. Some advocates wanted high loan rates and effective production controls to prevent surplus stock accumulation. This approach was followed for tobacco and peanuts but the producers of the other crops resisted the imposition of effective production controls. Thus, for other supported crops land retirement programs became the primary method used to limit production. Land retirement programs usually operated by paying producers to idle land normally planted to the supported crop.

In 1973 a new policy instrument was introduced to deal with the problem of stock accumulation resulting from high loan rates. Target prices became the way in which producer prices were assured. Under the target price system the loan rates were set at a low level to reduce or eliminate surplus stock accumulation and producers were paid the difference between the target price and the generally lower market price by the government. If supplies were excessive, land set-asides were put into place which producers had to comply with to receive target price payments.

In the 1980s two new policy instruments were developed. They were the Payment In Kind (PIK) program and the marketing loan. Under the PIK program farm producers that followed certain program guidelines were give PIK certificates that qualified them to redeem a given quantity of a commodity owned by the government. Farmers could sell these certificates to processors or exporters who then redeemed the product for use or export. This reduced the government inventories of surplus commodities and provided back door financing for huge program costs during the Reagan administration.

In the late 1980s the marketing loan was introduced as a way to avoid surplus accumulation. Under the marketing loan program the producer receives a price support loan as they did under the old loan program. Under the marketing loan program, however, the producer does not have to repay the entire loan. Instead, the producer can sell the product at the prevailing market price and the loan is considered as fully repaid by the amount received from the sale.

The marketing loan concept was first developed for cotton because payment limitations restricted the use of target price payments for large-scale cotton producers. Marketing loans essentially converted the price support programs to income support programs.

When the farm bill came up for renewal in 1995 a new force entered the picture. The Republicans seized control of the Congress during the so-called "Republican Revolution" of the 1994 elections and the new House leadership wanted to reform the old agricultural subsidy programs. This occurred at a time when world prices for agricultural commodities were booming, so producers were not receiving target price payments. Projections indicated commodity prices would remain high and target prices would not be paid during the next several years.

The Federal Agricultural Improvement and Reform Act (FAIR Act) known as Freedom to Farm was passed in early 1996. At the time it was heralded as a major new direction in US farm policy. It abolished the use of land set-asides as a production control policy and ended target prices. It maintained, however, the use of loan rates and marketing loans, and added a new instrument called Loan Deficiency Payments (LDPs).

The LDPs shifted entirely from supporting prices to supporting producers' incomes. For example, using the LDP the producer of a commodity covered (covered or supported commodity) in the farm bill indicates he intends to sell his product and wants a loan deficiency payment. He gets authorization to sell the product and he receives a direct payment from the government for the difference between the market price at the time of sale and the loan rate.

Finally, the Freedom to Farm Act authorized new payments called Agricultural Market Transition Assistance (AMTA) payments. These payments rewarded producers for giving up target prices. Congress scheduled a reduction in AMTA payments over the six year life of the bill with the payments to end at that time. These payments were based on past production and were designed to qualify as Green Box payments under the new Uruguay Round Agricultural Agreement.

In 1998 world prices for agricultural commodities fell drastically, and the enthusiasm for the new program faded rapidly. As prices fell the marketing loan and LDP costs soared. Beginning in 1999 and continuing through 2001 the Congress passed emergency legislation each year that continued the AMTA payments and used them as a base to provide substantial assistance to producers of covered commodities. Thus, the stage was set for the 2002 farm bill.

THE 2002 FARM BILL

The Agricultural Committee of the House of Representatives began to prepare for a new farm bill in 2000. The committee held hearings in rural areas, inviting interested parties to appear to give their opinions on what was needed in a new farm bill. Of course, the interested commodity groups were the ones that were best represented at the hearings.

The House Agricultural Committee leadership decided in 2001 to move ahead with the passage of a farm bill even though the Freedom to Farm legislation ran through the 2002 crop year; and therefore, a new bill was not necessary before 2003. There were two reasons for the early action. One was that the Agricultural Committee wanted to pass a farm bill using the 2001 budget projections made in 2000, which did not reflect the economic downturn and thus allowed much higher spending for farm programs. Second, the committee wanted to have a new farm bill in place before the 2002 congressional elections.

The entire House passed the committee bill in late 2001. Meanwhile, Congressional Republicans told the White House that the passage of a generous new farm bill was important in the 2002 congressional elections and that the Republicans could not be seen as opposing it.

The Senate bill also was heavily driven by election politics. Senate majority leader Tom Daschle had five Democratic Senators up for reelection in 2002 from states where the farm vote is important. Finally, the Senate Agricultural Committee produced a bill that was even more generous than the House bill. After a long and difficult debate the Senate passed it. The final bill was a compromise between the House and Senate versions that the President signed into law on May 14, 2002.

The new farm bill aroused great controversy abroad even before it was signed. Many ministers of agriculture and trade of other countries condemned the bill as grossly unfair and likely to jeopardize the WTO negotiations on agriculture. When the President signed the bill it was compared to the administration's decision to place tariffs on steel imports. Internationally, both are viewed as an as indication that the US is not really interested in trade liberalization.

Provisions for Program Crops

Most of the attention has focused on the commodity provisions of the new bill relating to the so-called program crops: wheat, corn, cotton, rice, and soybeans. They are extensive and complex.

First, the 2002 farm bill retains all of the policy instruments of the Freedom to Farm and adds new ones (see Table 1). The AMTA payments, which were to be phased out, are continued under the name of direct payments. A variation of the target price payments, which ended with the Freedom to Farm Act, is reintroduced as counter-cyclical payments.

TABLE 1
POLICY INSTRUMENTS USED IN US FARM POLICY, 2002

Policy Instrument	Purpose	New	WTO Category
Loan Rate	To guarantee specific price to producer	No	Amber
Marketing Loan	To prevent stock accumulation	No	Amber
Loan deficiency payment (LDP)	To provide loan rate without stock accumulation	No	Amber
Direct Payments	To compensate producers for program changes	No	Green
Countercyclical payments	To compensate for low market prices	Yes	?
Dairy Payments	To compensate small dairy producers for low prices	Yes	Amber
Peanut Quota Buyout	To compensate quota holders for abolishing quotas	Yes	Green
Conservation Reserve	To retire fragile land from crop production	No	Green
Working Lands Conservation Program	To improve conservation on tilled land	Yes	Green

Much of the international protest over the new farm bill is aimed at higher loan rates for the program crops. Tables 2 and 3 show the loan rates for the various crops for the periods 2002 and 2003, and for 2004 to 2007. Some of the loan rates increased for 2002-2003, but these increases are modest compared to the impact of the new target prices, which will add substantially to the effective price as far as producers incomes are concerned.

TABLE 2
COMMODITY LOANS AND PAYMENT RATES FOR 2002-2003 UNDER THE 2002 FARM BILL

Commodity	Unit	Loan Rate		Direct Payment	Minimum Effective Price	Target Price	Maximum Counter Cyclical
		2001	2002-2003				
Wheat	US$/Bu	2.58	2.80	0.52	3.32	3.86	0.540
Corn	US$/Bu	1.89	1.98	0.28	2.26	2.60	0.340
Sorghum	US$/Bu	1.71	1.98	0.35	2.33	2.54	0.210
Barley	US$/Bu	1.65	1.88	0.24	2.12	2.21	0.090
Oats	US$/Bu	1.21	1.35	0.02	1.374	1.20	0.026
Upland Cotton	Cents/lb	0.52	0.52	6.67	58.67	72.4	13.730
Rice	US$/cwt	6.50	6.50	2.35	8.85	10.5	1.650
Soybeans	US$/Bu	5.26	5.00	0.44	5.44	5.80	0.036
Other oilseeds	US$/cwt	n/a	9.60	0.80	10.40	9.80	0.000
Peanuts	US$/ton	610.00 *	355.00	36.00	391.00	495.00	104.00

Note: * The support level for Quota Peanuts is US$610/ton. This support level reflects the value of the Quota. The support rate for Additional Peanuts was US$132/ton.

Source: USDA, Economic Research Service.

TABLE 3
COMMODITY LOANS AND PAYMENT RATES FOR 2004-2007 UNDER THE 2002 FARM BILL

Commodity	Unit	Loan Rate		Direct Payment	Minimum Effective Price	Target Price	Maximum Counter Cyclical
		2001	2004-2007				
Wheat	US$/Bu	2.58	2.75	0.52	3.27	3.92	0.650
Corn	US$/Bu	1.89	1.95	0.28	2.23	2.63	0.400
Sorghum	US$/Bu	1.71	1.95	0.35	2.30	2.27	0.270
Barley	US$/Bu	1.65	1.85	0.24	2.09	2.09	0.120
Oats	US$/Bu	1.21	1.33	0.02	1.35	1.44	0.086
Upland Cotton	Cents/lb	0.52	0.52	6.67	58.67	72.40	13.730
Rice	US$/cwt	6.50	6.50	2.35	8.85	10.50	1.650
Soybeans	US$/Bu	5.26	5.00	0.44	5.44	5.80	0.036
Other oilseeds	US$/cwt	n/a	9.30	0.80	10.10	10.10	0.000
Peanuts	US$/ton	610.00 *	355.00	36.00	391.00	495.00	104.000

Note: * The support level for Quota Peanuts is US$610/ton. This support level reflects the value of the Quota. The support rate for Additional Peanuts is US$132/ton.

Source: USDA, Economic Research Service.

The target prices that were added for the program crops in the 2002 farm bill will have significant income impact. As long as world prices are below the target price, the target price payments will increase returns to the producer above the loan rate for the favored commodities. For instance, the 2001 loan rate plus direct payment for wheat gave producers US$3.10 per bushel, whereas the new target price level is US$3.86 per bushel. The comparable figures for corn are US$2.17 and US$2.60, and for rice US$8.85 to US$10.50 per cwt.

The counter-cyclical payments will be based on a fixed historical production base period and will vary with prices received for the covered crops. Both direct payments and target price payments will be paid to eligible producers based on past production and yields. Producers are given the option of updating their acreage and yield base to take advantage of the new payments.

Most observers believe that the new target price payments will be classified as "amber box" (trade distorting) in the WTO because they are related to current prices. If so, there is a good possibility the US will exceed its limits for trade distorting domestic supports if world prices of the supported commodities stay low.

Peanuts, Dairy and Additional Commodities

After 64 years the old quota program for peanuts was completely revised in the 2002 farm bill. The quotas were abolished, with generous compensation to the quota holders that will cost several billion dollars. The new peanut program is similar to the program for other program crops. It includes loan rates, marketing loans, LDPs, direct payments, and target price payments. The change in the peanut program means that the Tariff Rate Quotas (TRQs) for peanuts could be enlarged or abolished without jeopardizing the program or producer's incomes.

The 2002 farm bill expend support to some additional commodities. They include pulses, wool, mohair, and honey (see Table 4). However, these products are not eligible for either direct payments or target prices. They do have price support loans, marketing loans, and LDPs.

TABLE 4
COMMODITY LOANS AND PAYMENT RATES FOR NEW COMMODITIES UNDER THE 2002 FARM BILL

Commodity	Unit	Loan Rate			Direct Payment	Target Price
		2001	2002-2003	2004-2007		
Graded wool	US$/lb	None	1.00	1.00	None	None
Nongraded woll	US$/lb	None	0.40	0.40	None	None
Mohair	US$/lb	None	4.20	4.20	None	None
Honey	US$/lb	None	0.60	0.60	None	None
Small chickpeas	US$/cwt	None	7.56	7.43	None	None
Lentils	US$/cwt	None	11.94	11.72	None	None
Dry peas	US$/cwt	None	6.33	6.22	None	None

Source: USDA, Economic Research Service.

The dairy price support program is continued as it was under previous legislation, and the support rate was not increased. Dairy price supports are implemented by government purchases of manufactured dairy products: butter, cheese, and dry skim milk powder if the market price of milk drops below the support level. In addition the domestic market for manufactured dairy products is protected from low cost imports by a series of TRQs with high over-quota tariffs.

A new dairy support program called the Dairy Market Loss Payments (DMLP) is added to boost the income of smaller dairy producers. Payments are triggered when the price of fluid milk in the Boston market falls below a specified level. The program makes direct payments monthly to producers on their first 2.4 million pounds of milk marketed per year. This is approximately the milk marketed from a herd of 120 cows and thus will offer little assistance to the large-scale dairy producers in California, New Mexico, and a few other states.

Sugar [5]

The price support program for sugar is continued with the same nominal support level -18 cents per pound for raw sugar and 22.9 cents per pound for refined sugar-. However, the 2002 Farm Bill effectively increased the support price for sugar by abolishing the penalty for putting sugar under loan and the fee for loan default. These changes have the effect of raising the effective support rate by two cents per pound. Non-recourse loans are authorized for raw and refined sugar products and the loans are extended to in-process beets and cane syrup. However, in the sugar price support program the loans are extended to the processors of sugar beets and sugar cane with the stipulation that the processors pay producers a specified price.

If the market price of processed sugar is too low to cover the loan rate plus the interest on the loan the processors turn the sugar over to the government. Then the government has to pay the storage costs and dispose of the sugar, usually at a loss. Thus, if the US government is to avoid acquiring surplus sugar it must maintain the internal price of processed sugar above the loan rate plus the interest and other costs of the processors.

The 2002 legislation instructs the Secretary of Agriculture to operate the sugar program at no cost to the treasury by avoiding loan forfeitures under the loan program. The legislation provides two policy instruments to avoid stock accumulation. One is a producer PIK program that will pay producers to plant or market less sugar beets or cane. The other is a marketing allotment program that gives the Secretary of Agriculture the authority to impose marketing allotments on domestic producers to avoid loan forfeitures and to comply with US commitments under the WTO.

The tariff rate quotas established under the Uruguay Round provides that the US will allow 1.256 short tons raw value (STRV) of sugar to enter at nominal tariffs. In addition, the NAFTA agreement with Mexico provides that Mexico can ship sugar into the US market at steadily declining tariff levels. The quantity of sugar that Mexico can export to the US is under dispute and has been since the Congress required a side letter with Mexico regarding sugar access to the US market before they would approve the NAFTA agreement.

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[5] For a detailed analysis of the sugar program see Orden [2002], Chapter 9.

The 2002 farm bill states that if the USDA estimates that total sugar imports will exceed 1.532 STRV the authority to impose domestic marketing quotas is suspended.

At the end of 2002 the prospect of additional sugar imports from Mexico became so politically difficult that the US trade negotiators negotiated a new framework agreement with Mexico that would put Mexican sugar exports to the US under a fixed TRQ arrangement, thus removing the prospect that rising imports from Mexico would make the US support program for sugar inoperative.

Conservation Programs

The 2002 farm bill substantially increases spending for conservation programs. It authorizes funding for some 18 different conservation programs that pay farmers for certain conservation practices, including the retirement of land from cultivation. It has programs for all areas of the country and for all kinds of farming.

Despite the large increase in funding for conservation programs there has been no criticism of the increased expenditures because the spending for conservation programs is not considered trade distorting. Conservation programs are classified as green box in the WTO. Some US environmental groups, in fact, criticized the farm bill for spending too little on conservation programs. Senator Tom Harkin wanted to spend more on some new conservation programs but other members were not willing to cut price support benefits to increase spending on conservation programs.

US Export Competition Programs

The US government has a series of programs authorized in the farm bill designed to increase exports of US farm products. These programs are extremely popular with US commodity groups and export firms; and therefore, are extremely popular with the Congress. It is not unusual for Congress to appropriate more funds for these programs than the administration requests.

The export competition programs fall into several different categories. They are:

- Direct export subsidies,
- Export credit programs,
- Food aid programs,
- Generic market development programs, and
- Market access programs.

Direct Export Subsidies. The US made limited use of export subsidies prior to the Uruguay Round and pushed hard to roll back or eliminate export subsidies in that negotiation. As a result of the export subsidy rollback in the Uruguay Round the US was left with relatively few export subsidy rights. The remaining rights are largely for wheat and/or wheat flour and dairy products.

The export subsidy for wheat is rarely used since the free trade agreement with Canada went into effect, since if the export subsidy results in slightly higher prices for wheat in the US there is an immediate inflow of Canadian wheat into the US that drives the price down. Therefore, the only use that the US is making of its export subsidy rights is a modest program on dairy products.

In the NAFTA negotiations the Mexican government wanted to ban the use of export subsidies by the US in the Mexican market, and the US refused, because they were concerned that if they did so the EU would subsidize products into the Mexican market at the expense of US exports. The US-Canada agreement does have a clause barring the use of export subsidies into each other's market.

As long as the EU has the right to use export subsidies the US will probably resist a ban on the use of export subsidies in Western Hemisphere markets, despite the limited subsidy rights the US retains. This is related to the US agricultural groups concern to avoid any action that will provide an advantage to the EU.

Export Credit Programs. The US government has several export credit programs. Some of them provide either direct US government credit or private credit guaranteed by the US government to foreign buyers of US farm products. These credit guarantee programs are especially popular with some US financial institutions, and they have lobbied strongly to avoid having them subjected to international constraints as to length of term or interest rates.

In the Uruguay round it was agreed that a new international agreement governing the terms and conditions for export credit programs for agricultural products would be negotiated in the Organization of Economic Cooperation and Development (OECD), which is where the agreement on nonagricultural export credit programs was negotiated. However, the opponents of change in US export credit programs successfully blocked the US from negotiating an agreement acceptable to competitor countries, so the negotiation on export credit terms has now been moved to the agricultural negotiations in the Doha Round. The EU has stated that it will not discuss phasing out direct export subsidies unless subsidized export credits and food aid are brought under WTO rules relating to export competition.

The US also has a credit program to guarantee credit to countries to build import facilities to enable them to import agricultural products. This supports the building of import elevators and similar facilities. This program is rarely used.

The US also has a supplier credit guarantee program that provides a guarantee to US exports for a portion of the funds that US suppliers provide to foreign buyers. The program covers only a portion of the supplier's credit and it only covers credit granted for up to 180 days.

Food Aid Programs. The US has had a major food aid program since 1954. It is generally called the PL 480 Program after the law that first authorized it as a surplus disposal program. Over time the program shifted from being largely a surplus disposal program to an aid program. The program now consists of two categories. One is grant food aid, which is largely done through multilateral programs such as the World Food Programme. This category also includes grants of surplus commodities and farmer-to-farmer programs. The US also gives direct humanitarian assistance to other countries in the case of disasters.

The second type of food aid program is the sale of food under a long-term credit program, sometimes as long as 30 years with relatively low interest rates. This program has sometimes been used as a form of balance of payment assistance to provide commodities to importing nations that have economic difficulties. This is the portion of the food aid program that is attacked by competing exporters who claim the program is a form of export subsidy designed to protect US market share in some markets.

The food aid programs deal largely in bulk foodstuffs such as wheat, maize, rice, soybean oil, and non-fat dry milk. The US government does not distribute the products provided as food aid but merely turns the product over to the international agency, local government, or nonprofit assistance groups. The long-term sales are made to governments or government agencies in the receiving countries.

Market Development Programs. The Market Development Program is one of the oldest programs of export assistance. It is often known as the Cooperator Program. Under this program a number on non-profit organizations called "cooperators" have been formed to promote the exports of US farm products. These groups operate on government funding. They carry on generic promotion of products such as US wheat. They send teams to foreign countries to discuss country requirements, offer seminars on wheat quality and use, develop model bakeries and help foreign buyers understand the US marketing system and how to operate in it. For example, the soybean cooperators have conducted seminars on animal feeding and nutrition. These groups also participate in trade fairs and other promotional activities in foreign countries. When foreign buyers come to the US to investigate US products the cooperators develop programs to acquaint them with US products, exporters, and financing opportunities.

Much of the activities of the cooperator programs could be termed technical assistance for foreign buyers and users of US farm products. The Market Development Program is not classified as an export subsidy program under WTO rules.

Market Access Program. The Market Access Program is a program that reimburses exporters for some of their expenses for promoting their products abroad. It goes to promoters of branded products such as MacDonald's hamburgers or US wines or processed foods. The program has been attacked as corporate welfare since it reimburses companies for expenditures they would probably make in the absence of government assistance. However, it is very popular with the companies concerned and the Congress continues to fund it generously despite the criticism.

Trade Provisions of the Farm Bill

The 2002 farm bill has a trade title with a number of important provisions, some of which may influence the US position in the WTO negotiations or in negotiations of regional agreements. Most of the trade title is devoted to renewal and funding of the various export competition programs.

The bill extends the export credit program and provides funding for it through 2007. The bill requires the Secretary of Agriculture and the US Trade Representative (USTR) to consult regularly with the relevant committees of the Congress on the multilateral negotiations in the WTO and the OECD regarding the agricultural credit guarantee programs.

The farm bill requires consultations regarding export credit negotiations because the US cotton industry and CoBank (a large cooperative bank) are heavy users of the export credit program. So far, they have successfully blocked the negotiation of an acceptable agreement in the OECD and they want to block any agreement in the WTO that would limit their programs.

The bill authorizes and provides funding levels for several market development programs for agricultural products. The largest is the Market Access Program, which is authorized to spend US$100 million next year and up to US$200 million in 2006 and 2007.

The traditional Foreign Market Development Program is continued with its funding level increased to US$34.5 million annually. An Emerging Markets Program requires that the USDA award not less than US$1 billion of export credits or export credit guarantees to emerging markets.

The trade section of the farm bill also extends the funding of the Export Enhancement Program. It provides US$478 million per year for export subsidies for the life of the bill even though the level of export subsidies used by the US is constrained by the Uruguay Round agreement. The Dairy Export Incentive Program (DEIP) which is the export subsidy program for dairy products also is extended through 2007.

The bill also re-authorizes various US food aid programs. This includes grant aid; grants of surplus commodities; farmer-to-farmer programs; and a new program to provide food aid to encourage school attendance, especially by girls, in developing countries; as well as concessionary sales with long-term repayment features.

One of the more controversial portions of the bill is a requirement that retail offerings of meat, fish, fruit, and vegetables carry a country of origin label by 2004. This feature has aroused a good deal of controversy with Canada, which believes it is a move to discriminate against Canadian beef and pork sold in the US. It also is bitterly opposed by food processors and marketers who argue that the record keeping and tracking system to insure authenticity of the country of origin will be very expensive. The US Department of Agriculture has estimated that the establishment of records and their maintenance will cost US producers and the marketing chain as much as US$2 billion. It will of course also add to the cost of marketing imported products. Despite the fact that country of origin labeling already is common in US supermarkets, US producers believe that US consumers will prefer domestically produced products; and therefore, the producers view the labeling as a legal trade policy that will give them a competitive advantage in the US market.

Finally, the bill authorizes the Secretary of Agriculture to adjust expenditures for commodity programs if the Secretary determines that the US will violate its Uruguay Round agreement to limit spending on trade-distorting domestic subsidies to US$19.1 billion. However, prior to proceeding, the secretary must report the nature of these adjustments to Congress. While this feature is a bow to the WTO limit on domestic subsidies the likelihood of any Secretary of Agriculture proposing a downward adjustment in support levels to meet prior WTO commitments is remote, and especially in an election year, which is every other year.

Program Costs

There has been a great deal of misleading information regarding the potential cost of the new farm bill. Many press stories indicated that the new bill would add US$73.5 billion to US spending for agricultural subsidies. That number is derived from the original estimate of the cost of the Freedom to Farm bill when it was passed in 1996. Of course, the actual spending under the Freedom to Farm was much higher because the spending on marketing loans and LDPs were much higher than anticipated and, in addition, Congress passed emergency legislation each of the past several years to provide additional funds for favored commodities.

Table 5 shows the spending levels under the Freedom to Farm Act and the projected spending for commodity subsidies under the new farm bill. It shows that spending under the Freedom to Farm for the six years 1996 through 2001 was US$95.6 billion and the six-year projected spending total under the new farm bill is US$118.2 billion. It should be noted that spending projections are almost always low.

TABLE 5
COMMODITY PROGRAM COSTS UNDER FAIR ACT FROM 1996-2001 AND THE 2002 FARM BILL FROM 2002-2007
(US$ billions)

Year	Actual	Year	Projected
1996	4.6	2002	18.4
1997	7.3	2003	21.9
1998	10.1	2004	21.3
1999	19.2	2005	20.0
2000	32.3	2006	18.9
2001	22.1	2007	17.7
6 Year Total	95.6	6 Year Total	118.2

Source: United States Senate Budget Committee, May 2002.

THE IMPACT OF THE 2002 FARM BILL ON INTERNATIONAL TRADE, TRADE NEGOTIATIONS, AND TRADE AGREEMENTS

The passage of the 2002 Farm Bill brought unprecedented criticism from countries around the world. Most objected that the new farm bill would increase the trade distortions in international markets. The EU and Japan, which have domestic subsidies even higher than the US, accused the US of hypocrisy for advocating increased dependence on world markets for their farmers while further isolating US producers from world markets.

There are two questions to be addressed in evaluating the impact of the farm bill on international trade and trade agreements. One question is the effects of the bill on the output of supported products in the US and the consequent impact on world prices of the supported commodities. The second question is how can a system of free trade exist among countries whose producers have drastically different levels of prices and incomes due to government subsidies when producing the same commodity.

There has been a good deal of discussion as to whether the 2002 farm program is more damaging to other countries than the policy that proceeded it, but this is an irrelevant issue. The 2002 Farm

Bill is the established US policy for the present and for the immediate future when the trade negotiations are likely to take place. Therefore, the relevant issue is what does the new policy imply for the next few years, for the trade negotiations and for the integration of agriculture under a US-CAFTA.

It is not quite accurate to say that the US farm program isolates the US from world markets. For most commodities it isolates the income of US producers of supported commodities from world markets, but apart from sugar, tobacco, and dairy products US consumers get their food supplies at world market prices, except for tariffs on imported items. In addition it should be remembered that the US farm programs cover a relatively few commodities, primarily field crops that are sold into world markets in bulk unprocessed form.

This does not mean that the US support programs do not have an adverse impact on the world prices of the supported commodities. That effect comes primarily from the effects of the US program on the output of the supported commodities and the fact that under the marketing loan system the supported commodities flow unimpeded into international markets at the prevailing world price without government supports.

Professor Bruce Gardner has estimated the agricultural output and price impact of the 2002 Farm Bill (Gardner [2002] Chapter 4). He concludes that the output effects are relatively small resulting in a reduction of about six percent in world prices compared to the situation if there were no loan program. Economic Research Service (ERS) researchers have estimated price effects of 1.5 to 4 percent for grain and soybean and up to 10 percent for cotton. A new ERS study suggests that the 2002 Farm Bill has little or no impact beyond that of the 1996 FAIR Act that was so widely lauded when it was passed. Both Gardner and the new ERS study suggest that the greater land retirement under the increased conservation funding may completely offset the output effects of the higher loan rates.

Oxfam has issued a stinging report on the adverse impact of the US cotton subsidies on world cotton prices and the adverse impact of the lower cotton prices on cotton farmers in Africa. They use price estimates from a model developed by the International Cotton Advisory Committee. It shows that the US support program for cotton reduced world prices for cotton by 3 cents/pound in 1999-2000, 6 cents for 2000-2001, and 11 cents/pound in 2001-2002. It should be noted that all of these years were under the 1996 FAIR Act and not the 2002 Farm Bill. However, under the 2002 Farm Bill the area planted to cotton in 2002 fell by a significant amount.

The section of the farm bill dealing with export competition is unlikely to present any serious threat to the CACM countries. They are not generally in competition with the US in third country markets, and the US programs for export credit and food aid rarely involve commodities of major export interest to the CACM countries.

Despite the fact that the 2002 Farm Bill is estimated to have little effect on the world price of most supported commodities, it still presents great difficulties to negotiators of a free trade agreement. It is highly unlikely that the Doha Round of WTO negotiations will bring about elimination of trade-distorting domestic subsidies in OECD countries. Therefore the negotiators of regional agreements will have to deal with the huge differences in subsidy levels between producers of the same commodities in different countries. If the aim of free trade agreements is to foster integration of agricultural markets in the region certainly one of the greatest barriers to successful integration is the generous subsidies paid to favored producers of selected commodities in the US.

TRADE PROMOTION AUTHORITY

After several unsuccessful tries and months of difficult negotiations, the Congress finally passed Trade Promotion Authority (TPA), previously called "fast track", and the President signed the new negotiating authority on August 6, 2002. This was the first time since the authority expired in 1994 that the executive branch has had trade negotiating authority and the ability to have a trade agreement that is negotiated considered under the special "fast track rules".

The fast track authority means that the Congress must consider any trade agreement as a whole and must vote the entire agreement up or down without amendment. It also requires that congress act on any trade agreement legislation within a specified period after it is submitted, and the period that the Congress has to debate the agreement is limited. In return for the special legislative rules that limit the ability of the individual members of Congress to amend an agreement to death, special rules are set for the executive branch in terms of consultation with the Congress during the negotiations and the preparation of the implementing laws.

The new TPA passed the House of Representatives by a single vote along partisan lines with virtually every Democrat in the House voting against it. The Senate Finance Committee insisted that a partisan bill could not pass and they added a key feature, which is the Trade Adjustment Act (TAA). This provides for federal payments to workers who are shown to be displaced by imports. It includes compensation, training, and a subsidy to provide health insurance for unemployed workers. The Republicans initially resisted the addition of the TAA to the fast track legislation, but after long negotiations the White House agreed that they would accept the Senate provisions for TAA.

The compromise bill that emerged from the House-Senate conference omitted some of the worst features of the two versions of the bill. For instance, the Dayton-Craig amendment in the senate bill that would have prevented any agreement that changed US trade remedy laws from enjoying fast track treatment was omitted.

The final bill places many limits on the trade negotiators. A special Congressional Oversight Group is authorized to oversee the negotiations. It consists of the chairman and ranking member of the House Ways and Means Committee and three other members of that committee. It also includes the chairman and ranking member of the Senate Finance Committee plus three others from that committee, and the chairman and ranking member of any committee that would have jurisdiction over laws affected by the trade agreement. This means, of course that the oversight group will have, among others, the chairmen and ranking members of the House Agricultural Committee and the Senate Committee on Agriculture and Forestry.

The Congressional Oversight Group will be accredited as part of the US trade negotiating team that gives them access to all documents and discussions. In addition the US Trade Representative is required to develop written guidelines to facilitate the flow of information between the USTR and the Oversight Group.

There are additional special consultation rules for agricultural products. The bill defines import sensitive agricultural products as all products for which TRQs are in place and all products on which tariffs were reduced by the minimum amount (15 percent) in the Uruguay Round Agricultural Agreement. For all import sensitive agricultural products the USTR is required to consult with the Committee on Agriculture of the House and the Committee on Agriculture and Forestry of the Senate as to which products it would be appropriate to agree to negotiate further tariff cuts. The International Trade Commission (ITC) is then required to assess the impacts of further liberalization on the industry. Finally the USTR is required to inform the two agricultural committees as to which products they intend to seek liberalization and the reasons for such tariff liberalization.

As a result of the TPA definition of sensitive products, a large number of tariff lines for agricultural products are subject to the special rules. The TRQs cover beef, tobacco, cotton, peanuts, sugar, and dairy products. These products with TRQs cover 24 percent of US tariff lines (see Gibson, Wainio, Whitley and Bohman [2001]). In addition, products classified as sensitive because they received minimum cuts in the Uruguay Round amounted to another 184 tariff lines.

The bill also sets out negotiating objectives for the various sectors. In agriculture it calls for obtaining competitive opportunities for US agricultural products in foreign markets equivalent to the opportunities that foreign exports have in US markets.

For import sensitive crops subject to tariff reduction the bill mandates these reductions allow for "reasonable adjustment period". It also calls for the elimination of subsidies that distort agricultural markets or that create market-depressing surpluses. This comes from the same Congress that only a few months earlier passed the 2002 Farm Bill that includes new and higher subsidies for producers of US program crops that will certainly add to the distortions in agricultural markets for these products.

The US negotiating objectives in agriculture include eliminating practices that adversely affect perishable or cyclical products and the development of an improved import relief mechanism for perishable or cyclical crops.

The negotiating objectives also include the preservation of the US export credit program and food aid program.

In general, the TPA includes many provisions to protect the interests of producers of the import-sensitive products. It requires consultation with the Congress before negotiations can begin on sensitive products, and it will give the affected commodity groups ample warning and plenty of time to rally opposition to any tariff reductions being considered on their products.

In early September 2002, the US Trade Representative requested that the ITC determine the potential impact of completely removing tariffs on all the sensitive products imported from the 33 Western Hemisphere countries and the potential effect of eliminating or cutting in half the tariffs on sensitive products from all countries. The ITC promised that the analysis would be completed by mid-November 2002, but said the results would be classified.

Import Protection for US Farm Products

US trade negotiators like to point to the fact that the US has the lowest average tariff rate for agricultural products of any major agricultural producing country, with an average tariff rate of 12 percent. However, this relatively low figure masks some high levels of border protection for some important products.

It is useful to review the history of US border protection for agricultural products in order to understand the current forms and levels of border protection.

As mentioned in the section on US support programs, the US government began supporting internal commodity prices in the 1930s. In order to raise internal prices above the low world commodity prices it was necessary to put border protection in place to prevent low-cost imports from undercutting domestic prices. When the rules for the General Agreement on Trade and Tariffs (GATT) were written in 1947 the US insisted that agriculture be exempt from the general rules prohibiting the use of import quotas. Instead the rules for agriculture said that import controls could be used for agricultural products if there were domestic production controls on the product in question.

The US also insisted that the GATT rules for agriculture allowed the use of export subsidies, since it was recognized that it would be impossible to compete in export markets without export subsidies if domestic price support programs maintained the internal price of the product above the world price.

In the 1950s the US demanded that it be granted a GATT waiver that would allow it to use import quotas for agricultural products that had price supports regardless of whether or not they had domestic production controls. The US threatened to withdraw from the GATT if the waiver was not granted, so the other members of the GATT agreed to the waiver. The commodities covered by this waiver came to be known as the Section 22 commodities after the US law that authorized the quotas. Using the Section 22 authority the US applied import quotas to sugar, wheat, cotton, tobacco, peanuts and dairy products. Two major export crops, corn and rice did not use the import quotas because there were no significant imports of these products into the domestic market of a low cost producer.

In addition to the Section 22 commodities, starting in 1964 the US had a law that required export restraints by beef exporters to the US market. The beef restraints, like the Section 22 quotas, were allocated to exporters on a historical basis.

The Section 22 quota on wheat was abandoned as a result of the US-Canada Free Trade Agreement. This was one of the features that Canada insisted on as part of the agricultural agreement. The US wheat growers strongly opposed abandoning the Section 22 authority on wheat, but it was agreed to by the US administration and approved as part of the US-Canada Free Trade Agreement. The remainder of the import quotas persisted until the end of the Uruguay Round.

One of the major results of the Uruguay Round was the conversion of all non-tariff barriers to tariffs. This converted all of the import quotas and export restraints into tariffs, many of which were very high. In order to insure some market access for these products each country was required to establish tariff rate quotas (TRQs) of at least 3 percent of domestic consumption of the product or current imports, whichever was greatest. As a result the US established TRQs covering some 24 percent of agricultural tariff lines. For most products the tariff level for in-quota quantities is fairly low, but the over-quota tariff levels are set at levels intended to prohibit imports, and except in rare cases they do so.

In the Uruguay Round the tariff cutting formula was designed to allow countries to protect their sensitive agricultural products. Countries were required to reduce tariffs by an average 36 percent with a minimum cut of 15 percent on each tariff. To protect sensitive products, countries cut tariffs by large percentages on products with already low tariffs and on products not considered import sensitive. For sensitive products, they cut tariffs the minimum amount.

Apart from the products covered by the TRQs the US tariffs on most agricultural products is relatively low by world standards. However, the tariffs on some import sensitive products are at levels intended to provide protection for the products concerned. These include orange juice, melons, some fresh vegetables, and some fruits.

THE US WTO AGRICULTURAL PROPOSAL

On July 24, 2002 the US presented its proposal for the modalities for agricultural reform under the agricultural negotiations of the Doha Round. The proposal closely followed the earlier submission on agriculture made in May 2000, thus with few exceptions it contained few surprises.

The US proposed in the area of export competition that all direct export subsidies be phased out over a period of five years. The US agreed that export credit rules need to spell out the acceptable practices insofar as subsidized credits are concerned.

While the US maintained food aid programs remain outside the WTO discipline; it instead called for increased reporting of food aid activities to the WTO to strengthen the market displacement analysis in the international bodies that monitor food aid.

The US proposed prohibiting export trading monopolies. In addition, the US proposed that any special financial privileges granted to state trading enterprises be ended and that state-trading enterprises be subjected to greater transparency in the WTO.

The US proposal regarding market access is quite bold. It recommended that tariffs be reduced by a formula that would cut high tariffs more than low tariffs, leave no tariff above 25 percent and agree to a date when all tariffs on agricultural products will be eliminated. It was recommended that for products with TRQs all in-quota tariffs be abolished and that the TRQs be enlarged by 20 percent. In cases where the TRQs are administered by a government agency the US proposed that some part of the imports be allocated to non-government entities, and that, the allocation to non-government entities be increased over time.

While the US proposed that the special agricultural safeguard established in the Uruguay Round be eliminated, it also recognized that there is a need for an improved safeguard mechanism for seasonal and perishable products.

The rules on trade-distorting domestic support, according to the US proposal, should be drastically changed. First, the so-called "blue box" should be abolished, leaving only two categories of domestic subsidies, trade distorting and non-trade distorting.

Rather than basing cuts in domestic subsidies on a historical base the US proposed that the limits on trade-distorting domestic subsidies be set as a percentage of total agricultural GNP. They proposed a level of 5 percent of agricultural GNP as the ceiling after the five-year adjustment period. The US also suggested that a date be set by which all trade-distorting domestic subsidies would be eliminated.

The US proposed several measures of Special and Differential Treatment for developing countries. They suggest that a share of the expanded TRQs be allocated to developing countries. The US also proposes that developing countries be allowed to use export taxes on agricultural products, while such measures would be prohibited for all other countries. Finally, the US proposed that specific support programs orientated toward subsistence, resource-poor and low-income farmers in developing countries be identified and be exempt from spending limits.

In general, the US proposal is aimed at the EU, Japan and a few other countries that have very large domestic subsidies relative to their agricultural output and very high tariffs on some products even after the reductions made in the Uruguay Round. Incidentally, the US proposal would also have a significant impact on US policies. It would require the US to reduce spending on trade-distorting domestic subsidies by half from the levels provided in the 2002 Farm Bill. The proposal to expand TRQs by 20 percent, if adopted would probably force changes in two of the most politically sensitive domestic programs -dairy and sugar-.

It remains to be seen how the US commodity groups will react to the US proposal if it becomes a serious model for the modalities. It is questionable whether some commodity groups are interested in giving up their domestic subsidies and their high border protection to achieve a more level playing field across all countries and all commodities. It is clear that the EU and Japan will oppose the US proposal for both market access and domestic support. It is not clear how developing countries will react. Many would gain substantially better access under the US proposal, but some developing countries have very high tariffs, and many Latin American countries have TRQs on a number of products.

It is interesting to note that if the US proposal on market access were to be accepted it would put a number of US support programs in jeopardy. The US sugar and dairy programs could not survive if the maximum tariffs were to be cut to 25 percent, and they could not survive a 20 percent increase in TRQs. It is possible that the US is depending on the EU and Japan to prevent an agreement on access rules that would render US programs inoperative.

THE POTENTIAL IMPACT OF THE US WTO AGRICULTURAL PROPOSAL ON THE US-CAFTA

The US proposal to the WTO for the modalities for agriculture in the Doha Round offers positive directions for the US-CAFTA. The suggestion for a 20 percent increase in the TRQs to be allocated to developing countries opens the path for TRQ reform, and the suggestion of a maximum tariff of 25 percent for agricultural products would make most of the US TRQs inoperative.

The US WTO proposal also opens the way for an improved program of agricultural safeguards. Apparently, the safeguard in the Chile FTA is the model that the US wants to use for all subsequent agreements.

Whatever the outcome of the WTO negotiations they will not approach a free trade agreement. Even if the US WTO proposal were adopted, the US-CAFTA would still give the participants a significant preference in the US market.

US IMPORT RESTRICTIONS AND US-CACM FREE TRADE AGREEMENT

While the US has one of the lowest average tariffs for agricultural products, that low average masks some substantial import barriers. These are shown in the profiles on import restrictions shown in Table 6.

TABLE 6
OVERVIEW OF AGRICULTURAL TRADE RESTRICTIONS IN SELECTED WESTERN HEMISPHERE COUNTRIES, 2000

	N° of Tariff Lines		Distribution of Tariff Rates							
	Ad Val	Non Ad Val	0%	0-15%	15-30%	30-50%	>50 %	Mean	Max	N° TRQs
USA	989	747	372	1,083	161	59	61	11.4	350.0	376
Costa Rica	1,138	n/a	238	796	n/a	64	40	13.8	162.0	73
Guatemala	811	60	208	215	388	n/a	n/a	9.2	20.0	31
Honduras	869	n/a	n/a	425	426	13	5	11.5	55.0	0
Nicaragua	869	n/a	197	638	18	7	9	7.3	76.7	17
El Salvador	937	25	217	217	429	49	n/a	11.2	40.0	37

Source: Jank, Fuchsloch and Kutas [2003], Appendix A, Table A.1.

First, the US, along with the EU and Japan has a large number of TRQs with high over-quota tariffs designed to prevent imports of more than the quota. In many cases these over-quota tariffs are mega-tariffs, over 100 percent.

If one looks at the US tariff profile you find there are a large proportion of non *ad valorem* tariffs, which are generally more protective, especially when prices are low. In addition, even though the US has a substantial number of tariff lines with zero tariffs, there are a significant number of agricultural tariffs that are over 15 percent. Many of these are on products where Central American countries may have a comparative advantage.

If one looks at the export patterns for the Central American countries it is clear that US protection adversely affects them. First, the export of products under TRQs in the US is important to some or all of them. This includes sugar, beef, and tobacco products. Beyond these products there are a number of fruits, vegetables, melons, and juices that are important that are on the US list of sensitive products.

The US list of sensitive products as defined in the Trade Promotion Authority covers 184 tariff lines in addition to the several hundred tariff lines covered by TRQs. Of special interest to CACM countries are products such as fresh and chilled tomatoes, head lettuce and other lettuce, carrots, cucumbers, peppers, sweet corn, watermelon, cantaloupes, citrus juices, apricots, and peaches. It is not possible at this time to predict how the US negotiators will respond to requests for liberalization of these products on the sensitive list, but the very fact that the products had enough political support to be on the sensitive list implies that US producers of those products will exert considerable pressure to continue their protection.

The countries negotiating with the US on improved access for their agricultural products face a dilemma when dealing with the products having TRQs. The US TRQ system allows the exporting country to receive the quota rent, and thus, countries want to be able to export more sugar or dairy products to the higher-priced US internal market. In the case of both dairy and sugar if the TRQs were substantially enlarged the support program that the TRQs protect could not be sustained in its present form. Thus, the internal price of the products concerned would fall to the world price and the advantage of the preferential access would disappear. This problem arises in all preferential agreements and has caused some countries to decide that quota rents from preferential agreements are more important than greater market access.

In addition to the TRQs and tariffs the US has a substantial number of sanitary and phytosanitary (SPS) rules that limit trade. It currently is impossible for other countries to export poultry products to the US because of SPS regulations, and SPS regulations limit access to the US market for fresh or chilled beef.

The US also has a number of technical barriers to trade (TBTs) that impede trade in agricultural products. These TBTs include marketing orders that when applied to domestic production also apply to imports. These limit the size or other characteristics that products must meet in order to enter the US.

It is unlikely that the US will agree to waive any of the SPS or TBT restrictions. The US consumers as well as the producers will support the continuation of rules designed to maintain food safety and/or quality. Therefore, the best arrangement to strive for is some kind of arrangement that can simplify and speed up SPS approvals for exports going to the US.

It is clear that the negotiators for the CACM countries face a formidable task. Their interests in greater access will focus on either products that are protected by TRQs or products that are on the sensitive products list. In both cases they have the problem of not only improving their own access but also the problem of setting a precedent for the FTAA negotiations.

COUNTRY INTERESTS AND ISSUES IN A US-CAFTA

In examining individual country interests and possible issues it is assumed that they will be largely driven by the individual country's economic interests in possible trade gains with the US and with concerns about protecting domestic agricultural industries, especially against the effects of US policies that provide US producers with subsidies and protection that will create unequal competitive advantage.

Six questions need to be answered in order to answer this question. The examination needs to be done for each country and then the analysis needs to be aggregated for the five countries to see what might be addressed in a regional trade agreement.

The six questions are:

1. To what extent do US subsidy programs for key commodities have an impact on exports of Central American countries by depressing prices for their export commodities or by crowding them out of world markets?

2. To what extent do US subsidies create potential problems for Central American producers by producing unfair competition in domestic markets in the absence of border protection?

3. What other US policies relating to export competition may adversely affect Central American producers either in their domestic market or in third country markets?

4. What are the impacts of US TRQs on Central American exports to the US?

5. Which products from Central America are on the list of sensitive products specified in the TPA beyond the products having TRQs?

6. What are the sensitive products for the Central American countries, and do US policies raise special concerns for these products?

In this examination the trade patterns for each country's exports to the US and the extent to which they might change or improve if the US tariffs were reduced or TRQs increased or eliminated, are reviewed.

In four of the five CACM countries agricultural imports are controlled in part by TRQs. It is assumed that these TRQs are evidence of import sensitivity for the products concerned. A key question becomes what might happen if those TRQs were relaxed or abandoned. This issue will be examined in two regards. First, would US exports of the products be likely to substantially increase if the TRQs were relaxed or eliminated? Second, are any of the sensitive products in the CACM countries products on which the US has significant support programs?

COSTA RICA

The list of sensitive products for Costa Rica includes several products protected by TRQs. The list includes pork, poultry, dairy products, beef, rice, corn (maize), beans, sugar, and tobacco. Several products on this list are products that have generous domestic support programs in the US. This includes sugar, tobacco, dairy products, rice, and corn. However, the current US support programs for dairy, tobacco, and sugar maintain domestic prices above world prices and therefore preclude exports without export subsidies, and the US has no export subsidy rights except for modest rights for dairy products. Thus, the US support program for these products would appear to offer little threat to the producers in Costa Rica if the TRQs were phased out. On the other hand the heavy subsidies to US rice and corn producers combined with the US program of marketing loans on these products clearly provides a competitive advantage for US producers that could threaten small producers of maize and rice in Costa Rica.

The situation for maize if quite different than for rice. Costa Rica has very little domestic maize production and therefore is almost totally dependent on imports of maize. Therefore, phasing out tariffs and quotas on maize would benefit livestock and poultry producers and other consumers of maize without creating significant adjustment problems for domestic producers in Costa Rica.

The situation for rice is quite different. Rice imports only account for 22 percent of domestic supplies, therefore there is a substantial domestic rice production industry which could be put under severe pressure by eliminating the tariffs and quotas on rice so that subsidized US production could flow freely into the market.

A similar situation might exist for beans. About one third of bean supplies are from domestic production. If the new subsidies on edible beans in the US bring a significant increase in output and results in lower market prices the domestic producers in Costa Rica could face significant problems if trade is fully liberalized.

The pattern of US exports to Costa Rica includes some of the Costa Rican sensitive products, namely corn and paddy rice. Wheat, apples, and grapes, also are high on the US list of agricultural exports to Costa Rica. Beans, which are not on the list of US exports to Costa Rica might present a new threat to Costa Rican producers if the new US support program with its accompanying marketing loans results in significant increases in output and exports.

Poultry products, which are on the list of sensitive products for Costa Rica and several other countries, present an interesting case of how SPS regulations can distort trade. The US domestic market has a significant preference for white meat. Poultry producers in the US must as a result find an export market for their excess production of dark meat. Many countries would be willing to accept the US exports of dark meat if their local producers could export white meat to the higher priced US market. However, current SPS rules prohibit poultry meat imports into the US. As long as this disparity in market access continues it will be hard to convince smaller countries with limited markets to drop their import controls on US poultry products.

The US is a major market for Costa Rican agricultural exports. The top ten agricultural exports from Costa Rica to the US account for 74 percent of Costa Rican agricultural exports and the exports of those ten products to the US account for 77 percent of their agricultural exports. The top ten agricultural exports do not include sugar and beef, which are also major exports that are heavily dependent on the US market.

Surprisingly, only two of the top ten Costa Rican agricultural exports face substantial tariffs in the US market. They are food preparations (n.e.s.), which are controlled by TRQs on sugar related products, and fresh melons which still have a significant tariff.

Costa Rican exports of sugar, beef, and tobacco products to the US clearly are constrained by TRQs on those products. The TRQ on beef is a holdover from the time when the US was a significant net importer of beef. Now the US is a net exporter of beef and receives major beef imports of beef from Canada outside the TRQs. The recent US-Chile FTA gives Chile an immediate access to the US market for a significant quantity of beef and completely phase out the quotas and tariffs on beef over time. It should be possible for Costa Rica, which already has some access under the beef TRQ, to negotiate increases in that quota and its eventual elimination.

The TRQs on tobacco and sugar present different problems. The US sweetener industry has already said they will vigorously oppose any relaxation of the US sugar quotas in regional FTAs. They insist that sugar TRQs can only be dealt with on a global basis. They will be monitoring the US-CAFTA negotiations both for what is done for sugar, and for the precedent it might set for the FTAA. The political power of the sweetener industry is shown by their apparent success in forcing the US government to renegotiate the section on sugar in the NAFTA agreement to impose quotas on the entry of Mexican sugar to forestall the duty free entry of significant quantities of Mexican sugar.

The TRQs on tobacco pose a similar problem. The US producers have great political power to protect their program, which can only be sustained by import controls and domestic production controls. Politically, the tobacco producers are unlikely to get a buyout of the quotas and a generous payments program as peanut producers enjoyed because it is politically unacceptable to spend large sums of public money to support production of a product considered to be injurious to public health. Thus, relaxation of the TRQs on tobacco is unlikely.

Based on the pattern of trade between the US and Costa Rica it appears that the US farm bill will have only a limited impact on the trade interest of Costa Rica. Clearly, the higher level of supports for program crops in the US will increase the huge disparity between subsidies to producers in the US and Costa Rica. This is probably most important for rice where the US programs will give US producers an advantage in world markets and over the local producers of those crops.

The continuing US export programs seem unlikely to adversely affect Costa Rican trade interests. The US export credit program generally is not used for products of significant export interest to Costa Rica. In any event, it is highly likely that the export credit program will come under new international rules, as a result of the Doha Round.

The new law that will require country of origin labeling beginning in 2004 is unlikely to adversely affect Costa Rican exports to the United States. US livestock producers hope to gain an advantage over Canadian beef and pork exported to the US under the US-Canada Free Trade Agreement that promoted it. It is likely that Costa Rican beef exported to the US is used in processed form and thus would not be subject to labeling.

The US TPA will affect the export interests of Costa Rica to the extent that the special emphasis on the handing of sensitive products impedes the ability of the US negotiators to make realistic concessions on products on that list. Clearly the special rules will change the political dynamics of negotiations on these products, but it is not possible to predict exactly how this will affect the outcome of negotiations.

EL SALVADOR

The US subsidy programs may create problems for El Salvador. El Salvador has a number of sensitive products that are protected by TRQs and some additional sensitive products that are protected by relatively high tariffs.

The products that are protected by TRQs include beef, dairy products, yellow corn, vegetable oils, sugar, and tobacco. In addition, officials view polished rice, white corn, poultry, and local varieties of beans as sensitive products where significant imports could threaten the survival of local producers or processors.

The potential problem seems most acute for maize. El Salvador uses about one million tons of maize per year, with about 40 percent imported and 60 percent produced locally. Thus unlimited imports of heavily subsidized US maize could have an adverse impact on a significant sector of Salvadorian agricultural production. The implications of this can be seen in the actions of small maize producers in Mexico who are staging violent protests against the elimination of tariffs on US maize.

The problem is similar for rice. About 40 percent of the rice consumed in El Salvador is produced domestically and 60 percent is imported, primarily from the US. If US subsidized rice is allowed to enter duty free it can create major adjustment problems for domestic rice producers.

The situation for beans is less clear. First it is not clear what the impact of the new subsidies for beans in the 2002 Farm Bill will be on production or prices. Second, it is not clear whether the US production would be a close substitute for domestic varieties.

It should be noted that the possibility of achieving substantially lower prices for maize and rice offers significant possible gains to consumers of those products. This, in turn, implies lower prices and a better competitive position for poultry, pork, dairy, and beef producers at a time when competition in those products will increase. In addition, since rice is consumed by lower income consumers, lowering internal prices would have important welfare benefits.

El Salvador is one of the Central American countries that is less dependent on the US market for its agricultural exports. Although El Salvador's agricultural exports are highly concentrated on a few products, with the top ten accounting for 81 percent of agricultural exports. The US market only accounts for 29 percent of those exports.

El Salvador's two major agricultural exports are coffee and sugar. The US is an important market for both, but the TRQ for sugar clearly limits sugar exports to the US. The US is the major market for undenatured ethyl alcohol, vegetables, nuts and unrooted cuttings. US TRQs on dairy products prevent the export of specialty cheeses to the large immigrant population of Salvadorians in the US.

El Salvador is one of the top 30 markets for US agricultural exports. The major agricultural imports from the US are maize, wheat, paddy rice, oil cake, apples, and grapes. Despite the El Salvador TRQs, the US exports to El Salvador are significant, and US exporters hope to expand them if trade is liberalized.

The US farm bill is unlikely to have additional adverse effect on El Salvador trade interests beyond those already coming from earlier US agricultural policy. The US TRQs that limit sugar exports to the US are long-standing. The additional domestic subsidies to the producers of corn, rice, cotton and peanuts seem unlikely to produce additional downward pressure on world prices, so that the major impact will be to the widening of the already huge disparities between the producers of commodities in the US and in El Salvador.

US export promotion programs seem unlikely to adversely affect El Salvadoran trade interests. US programs do not generally involve commodities that are of export interest to El Salvador and unless it is requested by El Salvador importers US export credit is unlikely to be used.

GUATEMALA

Guatemala's list of sensitive products as expressed by their TRQs contains many of the same products as other Central American countries and some that are unique to Guatemala. The TRQs cover maize, rice, sugar, tobacco, and dairy products. In addition, they have TRQs on wheat, apples and pears, grapes and raisins, sorghum, soy meal and oil.

As is the case for several other Central American countries, Guatemala has a substantial domestic production of maize. It provides for 75 percent of consumption and imports only account for a quarter of consumption. Thus, if the trade in maize is totally liberalized the maize producers in Guatemala will be subjected to major downward price pressure from the import of subsidized US maize.

A similar situation might arise for rice. There is a significant domestic production which accounts for over 40 percent of consumption, liberalizing rice imports could mean major adjustment problems for local producers.

The situation for wheat is somewhat puzzling, since Guatemala has no domestic production of significance. Therefore, the reason for the existence of the TRQ on wheat is not clear.

The export competition aspects of the US policy appear to provide no major distortions for the markets for Guatemalan exports.

Guatemala is less dependent upon the US market for its farm product exports than several of its CACM partners. The top ten agricultural exports account for 78 percent of its agricultural exports, but only about 35 percent of Guatemala's top ten exports go to the US. Exports to the US account for 39 percent of all Guatemalan agricultural exports.

Guatemalan exports to the US are limited by TRQs on sugar and tobacco products and by a significant tariff on melons. However, a number of major exports face no significant barriers in the US market. This includes flowers, unrooted cuttings, fresh or chilled peas, and vegetables. There are a number of products for which the US is the dominant export market. An examination of these products suggests that tariffs are not a factor limiting access to the US market.

Two of the top ten agricultural exports face TRQs in the US market. These are sugar and tobacco products. In addition, one of the top exports is fresh melons, which face a significant tariff. Beyond these barriers there are not significant tariff barriers for the major Guatemalan agricultural exports to the US market.

It is highly unlikely that the US export promotion activities will distort markets for Guatemalan agricultural products. There is a possibility that, if requested, the US might grant export credit for cotton purchases by Guatemala, but this will be limited in the future by whatever is agreed in the WTO on export credits.

HONDURAS

Honduras is the only country in Central America that has no TRQs. Domestic agricultural producers are protected only by ordinary *ad valorem* tariffs. In the case of rice, the tariff on milled rice is much higher than on rough rice, which means that the rather large rice imports, that constitutes a major source of rice consumed, are in the form of paddy rice. Domestic rice production is insignificant, so the differential tariff protects the domestic rice milling industry, not rice producers.

Honduras imports about 30 percent of the maize available in the country. The border protection is in the form of a tariff, which is significant in terms of protecting domestic producers. Thus, maize producers in Honduras will be subjected to considerable adjustment pressures if the tariffs on US maize are removed and maize is allowed to enter without duties.

Except for the tariffs on maize, Honduras apparently has adjusted to the competition from subsidized US production of several of the commodities they import. Since the 2002 Farm Bill did not add significantly to the output incentive for most supported commodities, it appears that maize is the only product where the competition from imports is likely to create major pressures on domestic producers.

There is little likelihood that the US export programs will impede agricultural exports from Honduras. The US programs apply primarily to commodities that Honduras imports, not to exports to either the US or third country markets.

The agricultural exports from Honduras are heavily concentrated on a few products. Coffee and bananas account for 74 percent of all agricultural exports and the US is the destination for over half of the coffee and over 80 percent of the banana exports. In addition, the US market is the destination for over 90 percent of the fresh melons, and is the major market for some tobacco products. Honduras also has exports of sugar and beef to the US market, but the exports of those products to the US market only account for about one third of the total exports of those products. Thus, tobacco, beef, and sugar TRQs in the US are limiting Honduras exports to the US.

Based on the trade patterns in agricultural products between the US and Honduras it appears that the 2002 Farm Bill will have little adverse impact beyond that already experienced under previous legislation. Of course the higher subsidies for US producers will widen the already great disparity between US and Honduras producers of crops such as maize.

The array of US programs to enhance US export competition is unlikely to create serious export competition problems for Honduras' producers. As said before, most of the US export competition programs are for products that Honduras imports, not on products in competition with Honduras agricultural exports.

The new law requiring country of origin labeling is unlikely to create difficulties for Honduras exports. It is likely that Honduras beef exports are used in processed form and would not require major record keeping. Country of origin labeling on melons and fruit already exists in most retail outlets and should create no new problems.

The US Trade Promotion Authority will only adversely affect Honduras agricultural export interests to the extent that it causes US negotiators to be more protective of those products labeled as sensitive products.

NICARAGUA

Nicaragua has a short list of products with TRQs. It includes a number of commodities for which the US has significant subsidies. It includes maize, rice, both rough and milled, sorghum, vegetable oil and beans. It also includes beef, poultry, milk products, and sugar.

In addition to the TRQs, Nicaragua has some hefty tariffs on maize and sorghum. There is a 50 percent tariff on milled rice and only a slightly lower tariff on paddy rice, but the difference is enough to make imports almost entirely paddy rice. Thus, the rice tariffs are designed to protect both the significant domestic production of rice and the domestic rice millers. Even so, about one-third of the rice is imported, and if subsidized US rice is allowed into the country duty-free it will place significant pressure on domestic producers and rice millers.

The same is true for maize. Nicaragua produces about 85 percent of the maize used in the country. Local maize producers could come under severe pressure from subsidized US maize production if trade is completely liberalized.

Nicaragua is the only Central American country that is not among the top 30 export markets for US farm products. Even so, it is an important market and one where the US would like to expand its agricultural exports. The US export programs are unlikely to create any competition for agricultural exports from Nicaragua either in Nicaragua or in third country markets.

Nicaragua is the least dependant on the US market for its agricultural exports of any Central American country. Less than one fourth of the top ten agricultural exports go to the US, and only 27 percent of all agricultural exports go to the US. The major exports to the US are coffee, beef, sugar, bananas, and cigars. Of course all of these except coffee and bananas have limited access to the US market because of US TRQs.

Based on the trade patterns between the US and Nicaragua the major impact of the US farm bill will be to widen the already large difference in the levels of subsidies of producers of a number of key commodities. This includes both maize and rice, where dropping import protection could put significant pressure on Nicaraguan producers and create significant agricultural adjustment problems.

US export promotion programs are unlikely to create problems or competition for Nicaraguan exports. They are primarily focused on products that Nicaragua imports, not on those it exports.

The new country of origin labeling requirement is unlikely to create problems for Nicaraguan exports. The beef exports are likely to be used in processed form and not subjected to substantial record keeping. For melons, and fruits country of origin labeling is already in effect for most products.

The US Trade Promotion Authority will create problems to the extent that it makes it more difficult for US negotiators to relax TRQs and tariffs on sensitive products. Given the fact that Nicaragua's exports are heavily concentrated in the so-called sensitive products, the way in which these are handled will have a major impact on the ability of Nicaraguan producers to gain benefits from a free trade agreement.

TAKING A REGIONAL VIEW

Since the proposed FTA is for the region, it is important to look at the extent to which individual country interests are similar and where they might diverge. Where country interests are similar it will be easy to get agreement on a common position and negotiating objectives. Where country interests differ it will be necessary to achieve a common compromise position.

Country interests in improved access to the US market appear to be relatively uniform. For all countries the TRQs on beef and sugar limit exports of products for which Central American countries are low cost producers. For some countries the US TRQs on tobacco products and dairy products also block the possibility of expanding exports.

Second, all of the Central American countries would benefit from eliminating US tariffs on fruits, vegetables, and melons. They also would benefit from the elimination of any seasonal tariffs designed to protect US producers during the US production period.

Finally, most of the countries in Central America would benefit substantially if the current SPS barriers to their exports to the US could be removed. This needs to be done in a way that allows the Central American exporters to meet US SPS rules easier and more rapidly, not to relax the SPS rules.

On the import side all of the Central American countries, except for Costa Rica in the case of maize, have an interest in protecting their producers of rice and maize from highly subsidized US rice and maize. Costa Rica has the problem with rice. All of them have an interest in protecting their poultry producers unless they have access to the US market for chicken parts.

The new US requirements for country of origin labeling should not pose any problems for Central American exporters. Imported fruits and melons are already labeled and no significant record keeping would be involved since none of the Central American exports would be trying to qualify as US production.

DEALING WITH THE US IN AGRICULTURAL TRADE NEGOTIATIONS

There are several things that should be kept in mind when negotiating with the US on agricultural trade issues. They come from the unique political and economic system in the US that shapes both domestic agricultural legislation and agricultural trade policy. They are:

1. Do not assume hat granting improved access into your markets for nonagricultural goods and services will get you improved access to US markets for agricultural products. US farm groups strongly resist trade-offs between sectors. Agricultural groups will only support giving more access to US markets if they see some sectors of US agriculture gaining greater access. This is the reason that US agricultural groups strongly oppose an FTA with Australia, where they see increased competition at home and few opportunities for expanded exports to Australia.

2. Look for products where concessions will gain important allies among US commodity groups. For instance, offering to relax controls on wheat imports will gain support from an important commodity group. The relaxation of import controls on grapes and apples would also gain support.

3. Look carefully at recent FTAs to see what the US negotiators were hoping to gain and to see what US negotiators have judged to be politically feasible and economically important. For instance, the US refused to agree to forgo the use of export subsidies in the NAFTA agreement with Mexico, but has such a clause in the US-Chile FTA. In the US-Chile agreement the US gave Chile significant access to the US market for beef. This implies that US negotiators have concluded the TRQs on beef can be enlarged or abandoned since the Canadians now have access. The US-Chile agreement contains a new safeguard mechanism that the US has said will be a model for subsequent agreements. Can that safeguard arrangement deal with the Central American concerns about being flooded with imports that will adversely affect local markets for sensitive products?

4. Insist on reciprocity. If the US, as expected, refuses to increase the access for sugar and dairy products under the TRQ system, insist on the same logic and treatment for some of the Central American sensitive products such as rice and maize.

5. Make use of the huge disparities in subsidies to producers. Look at the possibility of maintaining some protection against highly subsidized crops until there is some parity in levels of subsidies and protection. The US-Canada agreement had a feature of this type that allowed the Canadians to protect against some US exports.

6. Make decisions on your own timetable. The US has substantial resources of people and domestic political linkages already in place. Do not allow the US timetable to rush decision making to the point where it is not possible to get regional consensus and local consultations to bolster positions. Both the Doha round and the FTAA are unlikely to stay on schedule, so rushing to complete a US-CAFTA before these others are done is unnecessary.

BARRIERS TO ECONOMIC INTEGRATION VIA FREE TRADE AGREEMENTS

Even if there is a comprehensive free trade agreement between the US and Central American countries there are a number of other issues that will determine the extent of true economic integration of the agricultural sectors. We can observe the experience of other free trade agreements such as the US-Canada agreement, the European Union's Common Agricultural Policy, and Mercosur.

The key issues are:

- Significant differences in agricultural policies and policy instruments,
- Significant differences in the level of subsidies and protection,
- Significant exchange rate instability,
- Differences in the ability to adjust to trade liberalization,
- Difference in the potential impact of liberalization,
- Differences in level of political commitment.

Differences in Agricultural Policies and Policy Instruments

Despite the existence of a free trade agreement and highly integrated economies, the US-Canada agreement has not resulted in substantial integration of agricultural markets for many products. The two countries have markedly different policy and policy instruments for wheat, poultry and dairy products. The use of marketing boards in Canada has been a constant source of frustration for US producers and, as a result, there have been constant political frictions between the two countries.

Policy differences between the US and Mexico for products such as maize and sugar have prevented the integration of markets for those products.

The European Union recognized from the beginning that they could not integrate their agricultural markets without a common agricultural policy and common policy instruments. Thus, they gave up national sovereignty over agricultural policy in order to achieve an integrated market. This has not occurred in any of the US free trade agreements.

Differences in the Level of Subsidies

Differences in levels of agricultural subsidies represent a major barrier to the integration of agricultural markets. This is one of the factors that prevent the integration of the market for maize between the US and Mexico. There is no question that the newly enacted US farm bill, with its higher subsidies for producers of program crops will prevent real integration of agricultural markets. These subsidies override the idea of comparative advantage and fair competition.

Exchange Rate Fluctuations

The EU found it could not achieve complete integration of agricultural markets until it achieved stable exchange rates between member countries. Until that time they had to resort to "green currencies" to allow products to move between countries. There is no question that the slow decline of the Canadian dollar against the US dollar has been a major source of the friction between the two countries over wheat exports to the US, beef exports to the US, and the ongoing soft-wood lumber friction. In the mid 1990s, the Mexican economic crisis and consequent devaluation created serious problems and led to special import restrictions on some agricultural products.

Differences in the Potential Impact of Liberalization

There are major differences in the impact of trade liberalization in different countries. One important factor is the size of the economy. Additional imports of agricultural products into the US economy will have far less impact on markets in the US than would similar quantities of additional imports in small countries. The impact also is affected by the price and income elasticity for the product involved. For instance, the impact of increased imports of melons into the US market would be small because they have relative elastic demand and high income elasticity. On the other hand, it is likely that the price and income elasticity of rice and maize in Central American countries is quite low, so that higher imports will put significant downward pressure on local prices.

Difference in the Ability to Adjust to Liberalization

There is no question that trade agreements and trade liberalization produces winners and losers in all of the countries involved. And, each country differs in its economic and political abilities to adjust to these gains and losses.

The ability of the countries to adjust to trade liberalization depends on a number of factors. One is the general health of the economy, especially of its labor markets. In countries where displaced farm workers can find alternative employment easily the adjustment process will be less difficult. In countries where there is high unemployment, especially in rural areas, the adjustments are more difficult.

The political issue of adjustment is not necessarily related to the economic difficulties of adjustment. In the US the resistance to trade liberalization is so strong that it was necessary to include Trade Adjustment Assistance in order to pass the authorization for negotiating authority. Most developing countries cannot afford policies such as the TAA, thus they must face the political problems created by adjustment to trade liberalization without programs to compensate the losers.

Different Levels of Political Commitment

The achievement of true market integration requires major political commitment on the part of the countries concerned. The commitment was clearly present in Europe where they saw economic integration as a method of preventing the conflicts that had plagued the continent for generations.

The political commitment to the integration of agricultural markets was clearly lacking in the US-Canada agreement. Canada was unwilling to give up its marketing boards and protection for some key agricultural products. On the US side the US agricultural groups were highly skeptical of real economic integration with low cost competitors, and they still are.

The political commitment in the US-Mexico agreement was greater but not enough to override the objections and political power of the US sugar and sweetener industry.

There are questions about the US political commitment to fully integrate agricultural markets via a US-CAFTA. While the US agricultural industry would not see Central America as a major threat to their well being, the sugar and sweetener industry clearly will do everything within their political power to prevent it. Unlike Europe, the US does not have a compelling political need to achieve true market integration and, thus, is likely to pursue free trade agreements without pursuing true integration.

AN OVERVIEW OF THE FACTORS LIKELY TO AFFECT US-CACM FREE TRADE NEGOTIATIONS

All agricultural groups in the US, countries participating in the FTAA, and countries negotiating in the agricultural negotiations of the WTO will closely watch the US-CACM negotiations for a free trade agreement. In many ways these various interested parties are likely to view the US-CACM negotiations as an indicator of where the FTAA, and even parts of the WTO negotiations may go. That means that US negotiators and other interest groups that are concerned with the other negotiations will not only be interested in the possible effects of a given arrangement on the CACM countries, but they also will be concerned about the impact on other countries if the precedents set in the CAFTA were applied more broadly.

Some of the same factors that are likely to influence the US negotiations in the FTAA and the WTO will influence negotiations between the US and the CACM for a free trade agreement. They include:

- US economic/political interests and pressures,
- US legislative framework relating to agricultural and trade issues, and
- The US position in other ongoing trade negotiations.

US Economic and Political Pressures

Unfortunately, there is no compelling economic and/or political interest in the US to have a US-CACM free trade agreement. This is especially true for the agricultural sector in the US. While the agricultural interests in the US are unlikely to actively oppose a US-CAFTA, as they may the FTAA, US agricultural groups see little to gain in terms of opening new markets for their products, and some potential threats in opening the US market to more agricultural trade from Central America.

There are several reasons for this attitude. One is the fact that the Central American markets are relatively open to US agricultural exports already. Four of the five Central American countries are among the top 30 export markets for US agricultural products currently. Second, the CACM countries have relatively small populations and modest income levels. These factors combined suggest that the gains for US agricultural exports will be modest. Jank ([2003] Chapter 1) suggests that the US should trade greater access for nonagricultural exports in CACM for greater CACM access on agricultural products. US agricultural interests have strongly opposed this trade-off in the past and there is no reason to believe they will do otherwise now. Simply, US agricultural groups oppose agreements that do not offer some sectors of US agriculture increased export possibilities.

US Legislative Framework Relating to Agricultural Trade: The 2002 Farm Bill, the Trade Promotion Authority and the US WTO Agricultural Proposal

The US-CACM negotiations will be the first regional negotiations conducted within the context of the current US legislative framework relating to agricultural trade. Thus, members of Congress and their agricultural constituents will be watching to insure that the US negotiators adhere closely to the intent of the laws they developed to protect the various agricultural interests.

The Potential Impact of the 2002 Farm Bill on CAFTA Negotiations. Despite all of the concerns expressed by other countries about the US farm bill passed in 2002, the changes it brought from previous legislation appear unlikely to have a severe direct impact on the countries of Central America. The effects of the new bill on output of the supported commodities appears likely to be relatively small and the trade aspects of the bill seem unlikely to create additional competition for Central American products in world markets or their domestic markets. Of course, the additional subsidies for US producers of program crops will widen the already large disparities between US producers and producers of the same products in all developing countries.

Despite the fact that the 2002 Farm Bill is estimated to have little effect on the world price of most supported commodities, it still presents great difficulties to negotiators of a free trade agreement. It is highly unlikely that the Doha Round of WTO negotiations will bring about major reductions in the level of domestic subsidies in OECD countries. Therefore, the negotiators of regional agreements will have to deal with the huge differences in subsidy levels between producers of the same commodities in different countries. If the aim of free trade agreements is to foster integration in the region certainly one of the greatest barriers to successful integration is the generous subsidies paid to favored producers of selected commodities in the US.

The Potential Impact of the Trade Promotion Authority on CAFTA Negotiations. The US TPA legislation that provided congressional authorization for the trade negotiations clearly raises some problems for negotiators for CACM countries. Those problems are related to the strong congressional defense of so called "sensitive commodities" and the special treatment they receive in terms of congressional control and oversight and the limits these are intended to put on US negotiators. The list of sensitive products includes all products with TRQs in place, and a number of perishable products that are of export interest to CACM countries. This, together with the relentless pressure from some of the protected commodity groups to continue their TRQs and protective tariffs, will create difficulties for the negotiators.

Given the fact that the US-CACM agreement will be viewed as precedent setting for subsequent agreements it is the agreement that the US may attempt to use to carry out the TPA mandate regarding the development of a workable and politically acceptable arrangement to deal with perishable and cyclical products. This seems to be important to US producers of perishable products and might go a long way toward reducing their opposition to market liberalization. It is important that any such agreement be viewed as the framework for the much greater pressures likely to come from a FTAA.

The US Position in other Ongoing Trade Negotiations

The US-CACM negotiations are beginning at a time when both sides are already fully engaged in two broader negotiations, in the WTO and the FTAA. US negotiators will be careful to not undercut their positions in other negotiations by provisions they agree to in a regional free trade agreement. Conversely, US negotiators may try to use the regional agreements to develop mechanisms of special interests to US producers. For instance, the US is likely to use the regional agreement to lay out a satisfactory safeguard agreement for perishables which could then be transferred to the WTO.

The US agricultural interests and the US negotiators will insist that some issues of major interest in the regional negotiations can only be handled on a global basis in the WTO negotiations. This will include the issues of limiting or reducing the use of trade-distorting domestic subsidies; limiting the use of some export competition measures including export subsidies and export credit; and any changes in treatment of commodities with TRQs.

Sugar and sweetener interests have already declared that they will strongly oppose any attempt to deal with or loosen sugar TRQs in regional agreements. They probably have the political power to block any regional agreement that loosens sugar TRQs. Tobacco interests will be equally opposed, and the dairy interests will be strongly opposed to opening dairy imports to Central American countries because it could be viewed as a precedent for the FTAA.

Negotiators of the US-CAFTA agreement face a major dilemma. If they make it completely clear that certain issues are off the table in the US-CACM negotiations it is likely that the FTAA negotiations would be badly damaged or killed. On the other hand, if the US agrees to consider certain issues, such as changes in TRQs, some of the most powerful, protectionist agricultural interests in the US will make every effort to block approval of the agreement.

It is clear that certain issues, that have already been mentioned, will be important and the most difficult in the CAFTA negotiations. How they are handled in the negotiations may well point the way to deal with them in other agreements. The first of these issues is how do the free trade agreements (FTAs) handle the problem of huge differences in the level of domestic subsidies to agricultural producers in the different countries. No one can claim there is a level playing field if US rice producers receive subsidies that provide them with twice the returns that rice producers in other countries receive. A similar point can be made regarding all the US supported commodities especially cotton, corn, and wheat. For a number of Central American countries corn (maize) and rice are sensitive commodities produced by small farmers who are likely to be vulnerable to intense subsidized competition.

The second important and difficult issue is how the problem of sensitive products is handled. If the sensitive products are all pulled out the CAFTA negotiations the results are bound to be modest. Therefore, the negotiators need to agree at an early stage as to how they will approach the issue of sensitive products that are a major concern to both sides.

Finally, expediting the process of SPS clearance into the US market requires serious attention. One approach that warrants close examination is a regional clearance system that would reduce the cost of developing the facilities and controls necessary to satisfy US requirements. No one should want to reduce the safety of food products entering the US or any other country but the time has passed when these requirements should be viewed as hurdles and barriers to reduce the flow of competing products into US markets. The US more than any other exporter should fight to avoid using food safety and other SPS issues as major trade barriers.

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