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Agricultural Trade in a U.S.-Central American Free Trade Agreement (CAFTA)

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Summary

Negotiating open market access for agricultural products in a free trade agreement between the United States and 5 Central American countries (Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua) has been contentious and difficult. With December 2003 set as the target date for concluding an agreement, both sides now face wrestling with how to transition their most sensitive agricultural commodities and food products (protected by high tariffs, restrictive quotas, or other barriers) towards free trade. In their October negotiating session, both sides exchanged market access offers on all (including sensitive) agricultural products, and agreed on immediate access for most horticultural products. The most difficult issues dealing with sensitive products were deferred to the December negotiations.

In 2002, U.S. agricultural exports to these 5 countries totaled $1.0 billion, and represented 2% of U.S. worldwide sales. Leading exports were coarse grains, wheat, rice, soybean meal, and animal fats. U.S. farm exports accounted for 11% of U.S. merchandise exports to the region, and have grown significantly in value terms over the last decade. Agricultural imports from these countries equaled $1.9 billion (or 4.5% of U.S. farm and food imports from the world), and represented 16% of U.S. merchandise imports. Purchases of bananas, raw coffee, and fresh fruit led the list.

The United States and the 5 Central American countries primarily use tariffs and quotas to protect their agricultural sectors. The average tariff applied by all 6 countries involved in these negotiations masks the high level of border protection each provides its most sensitive agricultural products, primarily through the use of restrictive quotas. U.S. agricultural objectives in the CAFTA negotiations are to eliminate tariffs, quotas, and other barriers to trade, and provide adequate transition periods and relief mechanisms for the U.S. farm sector to adjust to increased imports of sensitive products. The Central American countries seek increased access to the U.S. market for beef, sugar, fruits and vegetables. However, fears exist that opening up their markets to U.S. corn and rice will undermine their small subsistence farmers, unable to compete against subsidies U.S. producers receive under farm programs.

U.S. agricultural and food sector interests have mixed views about what CAFTA might mean. Several organizations support the negotiating objectives, anticipating benefits for their producers from more open markets. Some groups condition support on the ability of U.S. negotiators to actually eliminate tariffs and address specific issues. Others have strong reservations about CAFTA, or have requested that their commodity be excluded from the agreement's scope.

Congressional committee leaders have expressed concern about the "unrealistic demands" that Central American negotiators have made to protect their sensitive agricultural commodities. They have signaled that if CAFTA does not result in real market access for commodities with U.S. export potential, some Members of Congress may not support the agreement. Some Members oppose including sugar in CAFTA, fearing increased imports would undermine U.S. sugar policy and the viability of the domestic production sector. This report will be updated.

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Introduction

As part of its overall trade strategy, the Bush Administration over the last year began negotiating bilateral free trade area (FTA) agreements with four regional blocs or countries. Negotiations on a U.S.-Central American Free Trade Agreement (CAFTA) involving Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua began in late January 2003 and are currently scheduled to conclude this December. While negotiators have reportedly made progress in a number of areas, efforts to formulate a framework for handling agricultural trade have been slow.[1]

Unique to free trade agreements, as illustrated by the North American Free Trade Agreement (NAFTA), are provisions designed to liberalize trade by reducing and eliminating tariffs, quotas, and non-tariff barriers between partners within an agreed-upon time period (usually 10 to 15 years). FTAs are generally comprehensive in scope, and in addition to including provisions on agricultural trade, cover trade in all other goods and services, investment rules, and intellectual property rights, among many other issues. While some U.S. agricultural groups and food manufacturers welcome the market openings these prospective bilateral FTAs might provide, producers of import-sensitive U.S. commodities will carefully monitor and seek to shape those provisions that affect them. Closely watched will be the transition periods that U.S. negotiators agree upon for sensitive agricultural products that enter the U.S. market from a FTA partner. Domestic interests that see potential in free trade in prospective FTA markets will watch to see what pace of access U.S. negotiators can secure for U.S. agricultural products that these partners consider as import sensitive. Other provisions negotiated in FTAs that affect agricultural trade include rules of origin,[2] safeguards against import surges, rules to address various other trade barriers, and the terms under which rules to ensure food safety and plant and animal health are applied. Bilateral FTAs, however, have not addressed the issue of trade-distorting domestic farm subsidies.

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[1] For broader context, see CRS Trade Briefing Book entry titled U.S.-Central American Free Trade Agreement; CRS Report RL31870, *The U.S.-Central America Free Trade Agreement (CAFTA): Challenges for Sub-Regional Integration*, April 25, 2003, by J. F. Hornbeck; and CRS Report RL31356, *Free Trade Agreements: Impact on U.S. Trade and Implications for U.S. Trade Policy*, July 25, 2003, by William H. Cooper.

[2] Rules of origin specify what is required for a product to be considered to have been produced or processed in a country that is a party to a trade agreement. They are used to implement FTAs to determine whether a product benefits from the agreement's duty and quota preferences.

U.S. Agricultural Trade with CAFTA Countries

The United States in 2002 recorded an agricultural trade deficit (- $847 billion) with the CAFTA region. U.S. agricultural exports to these 5 countries increased 74% over the last decade (1993-2002) to just over $1.0 billion, while agricultural imports from the region rose 28% to $1.9 billion. Guatemala and Costa Rica ranked as the region's top two markets for U.S. agricultural products last year; they also were the leading suppliers of farm products to the U.S. market (Table 1).

Table 1. U.S. Agricultural Trade, and Agricultural Products' Share of Total U.S. Trade, with CAFTA Countries, 2002

Country/ Region	U.S. Agricultural Exports	Ag Export Share of U.S. Exports	U.S. Agricultural Imports	Ag Import Share of U.S. Imports
	million $	*percent*	*million $*	*percent*
Costa Rica	226	7.8	803	25.5
El Salvador	212	13.2	74	3.8
Guatemala	341	17.3	687	24.7
Honduras	184	7.3	232	7.1
Nicaragua	85	20.0	97	14.3
Total, CAFTA	1,047		1,894	
CAFTA Share	2.0 % [a]	11.1 % [b]	4.5 % [c]	16.0 % [d]

Source: U.S. Department of Agriculture (USDA), Foreign Agricultural Service; and U.S. International Trade Commission (USITC)

[a] of U.S. agricultural exports of $53.1 billion to the world.
[b] of U.S. merchandise exports of $9.4 billion to these 5 countries.
[c] of U.S. agricultural imports of $41.9 billion from the world.
[d] of U.S. merchandise imports of $12.2 billion from these 5 countries.

Exports

U.S. agricultural exports to the 5 CAFTA countries represented 2% of all U.S. agricultural exports in 2002, and 11.1% of total U.S. merchandise exports to the region. Exports of bulk commodities accounted for almost half of agricultural sales. The balance was nearly equally divided between intermediate (semi-processed) products and consumer-oriented food products. Reflecting this composition, leading exports were coarse grains, wheat, rice, soybean meal, and animal fats (totaling $516 million – half of all U.S. agricultural sales to CAFTA countries).

Imports

CAFTA's share of all U.S. agricultural imports was 4.5%, and represented 16% of all U.S. merchandise imports from the region, in 2002. Consumer-ready food products accounted for nearly three-quarters of agricultural imports from the 5 countries, with bulk commodities making up most of the balance. Reflecting this, leading imports were bananas, raw coffee, and other fresh fruit (totaling $1.3 billion – 69% of all agricultural purchases from the region).

Entries under two U.S. trade preference programs (primarily the Caribbean Basin Initiative, or CBI) accounted for 43% of U.S. agricultural imports – meaning they enter duty free. The share of imports covered by these preference programs varied from 30% for Honduras to 56% for Nicaragua (Table 2). A large portion of agricultural imports (tropical products such as bananas and raw coffee) that are subject to the most-favored nation rate enter duty free.

Table 2. U.S. Agricultural Imports from CAFTA Countries, by Most-Favored Nation Designation and by Trade Preference Program: 2002

	Agricultural Imports, 2002	Most-Favored Nation [a]	Generalized System of Preferences	Caribbean Basin Initiative	Total, Trade Preference Programs [b]
	million $	*percent*			
CAFTA, Total:	1,913	57.4	1.2	41.4	42.6
Costa Rica	820	49.0	0.5	50.5	51.0
El Salvador	74	53.0	7.4	39.6	47.0
Guatemala	688	65.6	1.7	32.7	34.4
Honduras	231	69.9	1.0	29.1	30.1
Nicaragua	99	43.7	0.0	56.3	56.3

Source: Derived by CRS from USITC data

[a] MFN, or Normal Trade Relations (NTR), refers to equal treatment of all countries (other than those specifically denied it) with regard to tariff concessions.
[b] The United States grants primarily developing countries unilateral preferential tariff treatment under various programs, meaning imports are eligible for lower than NTR rates (in practice, zero or very low duty) and giving them a competitive advantage in the U.S. market.

Barriers to Agricultural Trade

The United States and the 5 CAFTA countries use tariffs and tariff-rate quotas (TRQs)[3] to protect their agricultural sectors. The 5 countries committed under the multilateral Uruguay Round's Agreement on Agriculture to bind their average tariffs on agricultural imports at relatively high levels (ranging from Nicaragua's 73% to Honduras' 35%), compared to the U.S. commitment to bind its average rate at 12% (Table 3).[4] However, in practice, the Central American countries generally have imposed much lower average tariffs on agricultural imports (with applied tariffs ranging from 6.7% in Nicaragua to 14.6% in Costa Rica), and at times have allowed larger amounts of commodities than spelled out in their TRQ minimum commitments to enter duty free or at a lower duty.[5] The average U.S. applied tariff on imports from just the 5 Central American countries is considerably lower when trade preference benefits are taken into account (Table 2). These applied tariff averages, however, mask the range of protection provided commodities and food products in the 5 countries and the United States, and do not always reflect the full impact of the much higher level of protection provided by specific-product TRQs.

Issues Identified by the United States

The Office of the U.S. Trade Representative (USTR) has identified market access issues and related policies that the Central American countries use to limit or restrict imports of U.S. agricultural products.[6] U.S. negotiators have indicated they will seek to address them in CAFTA negotiations.

USTR noted three countries that have high tariffs on sensitive agricultural products. Costa Rica imposes a 65% rate on dairy product imports, and 150% on poultry products. El Salvador imposes a duty of 40% on dairy products, rice and pork, 30% on beef, and 30% (plus additional taxes) on alcoholic beverages. Guatemala imposes high protective tariffs on above-quota quantities that enter under its agricultural TRQs.

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[3] A TRQ combines two policy instruments that nations use to restrict imports: quotas and tariffs. In a TRQ, the quota component works together with a specified tariff level to provide the desired degree of import protection. Imports entering during a specific time period under the quota portion of a TRQ are usually subject to a lower, or sometimes a zero, tariff rate. This "in-quota" amount represents the minimum that a country has committed to allow to enter under multilateral or other trade agreements. Imports above the quota's quantitative threshold (referred to as above-quota) face a much higher (usually prohibitive) tariff.

[4] The global average bound tariff on agricultural imports is 62% (U.S. Department of Agriculture (USDA), Economic Research Service, *Profiles of Tariffs in Global Agricultural Markets*, January 2001, p. 11).

[5] For example, on October 25, 2002, the Government of Guatemala temporarily eliminated the TRQ on corn imports, and decided to impose a 15% tariff on all yellow corn imports.

[6] These are detailed in the country chapters of the *2003 National Trade Estimate Report on Foreign Trade Barriers*, released April 1, 2003 by USTR.

Table 3. Average Tariffs and Tariff Rate Quotas on Agricultural Imports: United States and CAFTA Countries

	WTO Bound Rate [a]	Applied Tariff Rate	Tariff-Rate Quotas
	percent		
United States	12.0	12.0 [b]	dairy products, sugar, sugar-containing products, peanuts, tobacco, cotton, beef
Costa Rica	48.0	14.6	pork, poultry, dairy products, beef, rice, corn, beans, sugar, tobacco
El Salvador	43.2	10.3	beef, dairy products, yellow corn, vegetable oils, sugar, tobacco
Guatemala	58.3	9.9	corn, rice, sugar, dairy products, tobacco, wheat, apples, pears, grapes & raisins, sorghum, soymeal, soyoil
Honduras	35.0	11.1	None - uses a price band for grains and a commodity absorption arrangement
Nicaragua	73.4	6.7	corn, rough & milled rice, sorghum, vegetable oil, beans, beef, poultry, dairy products, sugar

Source: USTR and USITC; paper prepared for IADB conference (footnote 9)

WTO - World Trade Organization

[a] 2001 for the United States, 2000 for the Central American countries.
[b] Considerably lower on agricultural imports from the 5 Central American countries, reflecting trade preference programs and the commodity/product composition of imports.

Other measures are used to limit certain agricultural imports. For example, Honduras administers a price band on imports of yellow corn, sorghum, and corn meal.[7] Honduras (for grains) and Nicaragua (for rice and pork) support domestic prices of important commodities through import quota schemes, sometimes called commodity absorption agreements. These require domestic end users and processors to purchase a certain percentage of local production at high prices before they are issued a license to import lower world-priced commodities (e.g., yellow corn at preferential tariffs). Such imports are sometimes also subject to high duties. El Salvador requires licenses for imports of basic grains and dairy products.

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[7] Price bands serve to insulate producers and processors when the world price for any commodity falls below a calculated reference price (e.g., a price target comparable to a commodity support level). Protection is provided the domestic sector by levying a variable duty on the imported commodity, which when added to the lower world price, raises the importer's cost to the reference price.

USTR also noted that some countries rely extensively on overly strict sanitary and phytosanitary (SPS) rules[8] to restrict agricultural imports. Honduras and El Salvador have effectively imposed bans on U.S. poultry imports, imposing "arbitrary" restrictions that call for zero salmonella tolerance or negative laboratory tests for certain poultry diseases. Additional U.S. poultry sales of $15 to $20 million to these two markets likely would occur if these bans were removed, according to USTR. El Salvador requires that rice imports have a USDA certificate stating a shipment is free of a disease that cannot be practically and effectively fumigated (treated). El Salvador requires the laboratory testing of all food products destined for retail sale. Concerns exist about the quality of this local analysis, because some processed foods approved for sale in the United States were rejected after testing in El Salvador, thus barring their sale.

Non-trade barriers (NTBs) also serve as impediments. Guatemala requires that every size or form of food product sold as individual units through retail channels be registered separately, even if the product content is of identical composition. USTR points out that there are not sufficient trained personnel to handle the testing and registration process, that it takes six weeks to complete irrespective of the company or product, and that products are sometimes damaged or pilfered while the process is being completed.

Issues Identified by CAFTA Countries

With about three-quarters of their agricultural exports to the United States already entering duty free under trade preference programs or at MFN zero rates (applied to bananas and raw coffee), the 5 countries are most interested in securing additional and/or unrestricted market access for those commodities now subject to U.S. TRQs: sugar and certain sugar-containing products, beef, dairy products, peanuts, tobacco, and cotton. They are also expected to press for a quick reduction in tariffs on fruits, juices, and vegetables, some of which face high U.S. tariffs: fresh and chilled tomatoes, head lettuce, carrots, cucumbers, peppers, sweet corn, watermelon, cantaloupes, citrus juices, apricots, and peaches.[9]

Central American negotiators continue to express concerns about the adverse impacts they see in opening up their markets to U.S. agricultural commodities (particularly corn, rice, dry beans, and dairy and meat products), most of which benefit from U.S. price and income support programs. This reflects widespread fear that small subsistence farmers will not be able to compete against lower priced imports of "subsidized" commodities from the United States. Though these countries had earlier pressed to include the issue of U.S. farm support on the negotiating agenda, they appear to have accepted the U.S. position that this issue should be addressed

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[8] Measures to protect humans, animals, and plants from diseases, pests, or contaminants.

[9] Dale Hathaway, "The Impacts of U.S. Agricultural and Trade Policy on Trade Liberalization and Integration via a U.S.-Central American Free Trade Agreement," April 2003, p. 38. This paper was prepared for an October 2002 seminar sponsored by the Inter-American Development Bank, and can be accessed at [http://www.iadb.org/INT/Trade/1_english/4_SpecialInfo/Conference/2002/i_Oct202-AgricLiberal/Hathaway.pdf].

multilaterally in the World Trade Organization's (WTO) Doha Round.[10] It remains to be seen if the breakdown of the WTO negotiations in Cancun on September 14, 2003, and a likely delay in reaching any multilateral agriculture agreement that addresses the domestic support issue, will affect the position of the 5 Central American countries. This is in light of the fact that details of the market access offers these countries tabled this summer when CAFTA negotiators met reflected much Central American apprehension about the pace and scope of reducing border protection on their most sensitive agricultural commodities.

The 5 countries, individual commodity groups, and others also have different interests and views on how agriculture should be handled in the CAFTA negotiations. Guatemala in May 2003 tabled a more aggressive proposal to open up its markets to U.S. products, breaking off from the other four. Since then, all 5 countries have sought to work out their differing positions to develop a common front, an objective the U.S. side has supported. Central American rice processors and consumers have competing interests. With milling operations benefitting from the high tariffs imposed on imports of milled rice (considerably more than on raw rice), consumers of this staple could benefit from lower prices paid for imported milled rice from the United States under a trade agreement.

U.S. Agricultural Trade Objectives

Last October, U.S. Trade Representative Robert Zoellick notified Congress of the Bush Administration's intent to negotiate a FTA with 5 Central American countries. In his letter, he stated negotiations would enable the United States to address several "market access impediments in Central America" that affect U.S. agricultural sales to the region. U.S. objectives pertinent to negotiating the FTA's agricultural provisions include:[11]

- eliminating tariffs and other duties and charges on trade between Central America and the United States on the broadest possible basis, subject to reasonable adjustment periods for import-sensitive products.

- eliminating non-tariff barriers in Central America to U.S. exports, including licensing barriers on agricultural products, restrictive administration of tariff-rate quotas, and other trade restrictive measures that U.S. exporters identify.

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[10] This Round's objectives for agriculture are to substantially improve market access for agricultural products, reduce and phase out export subsidies, and substantially reduce trade-distorting domestic support. For additional information, see CRS Report RL32053, *Agriculture in WTO Negotiations*, August 28, 2003, by Charles E. Hanrahan.

[11] USTR Ambassador Zoellick letter to House Speaker J. Dennis Hastert and Senate President pro Tempore Robert C. Byrd, October 1, 2002.

- eliminating Central American government practices that adversely affect U.S. exports of perishable or cyclical agricultural products, while improving U.S. import relief mechanisms as appropriate.
- developing a mechanism with Central America that will support achieving the U.S. objective in the WTO negotiations of eliminating all export subsidies on agricultural products, and in the FTAA [Free Trade Area of the Americas[12]] negotiations of eliminating agricultural export subsidies on trade in the Hemisphere, while maintaining the right to provide *bona fide* food aid and preserving U.S. agricultural market development and export credit programs.
- seeking to have the Central American countries reaffirm their WTO commitments on SPS measures and eliminate any unjustified SPS restrictions.
- incorporating a bilateral safeguard mechanism during the transition period to allow a temporary revocation of tariff preferences if increased imports from one or more Central American countries are a substantial cause of serious injury, or threat of serious injury, to a domestic industry.

U.S. officials have also made repeatedly clear that the issue of U.S. farm support or subsidies, pressed earlier by some Central American countries, will not be part of the CAFTA negotiations, but rather addressed in the WTO context.

U.S. Agricultural and Food Sector Views

Several commodity organizations support the Administration's CAFTA initiative, anticipating that a FTA agreement would further open markets for their producers in the region. For others, support is conditioned upon negotiators addressing specific issues in addition to eliminating tariffs. Some commodity groups have expressed concerns about the negotiations, or have requested that their commodity be excluded from the agreement's scope altogether.[13]

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[12] The 34 countries of the Western Hemisphere (excluding Cuba) in 1998 initiated formal talks to create a regional free trade area by 2005. The FTAA's stated objectives are to reduce and eliminate barriers to trade in goods (including agricultural commodities and food products) and services, facilitate cross-border investment, among others, allowing all countries to trade and invest with each other in the region under the same rules. For additional background, see CRS Report RL30935, *Agricultural Trade in the Free Trade Area of the Americas*, May 23, 2003, by Remy Jurenas, and RS20864, *A Free Trade Area of the Americas: Status of Negotiations and Major Policy Issues*, September 24, 2003, by J.F. Hornbeck.

[13] Stated positions of groups are based on: (1) their submissions to the U.S. International Trade Commission pursuant to its investigation requested by USTR (see footnote 14) into the probable economic effects of CAFTA in the October-November 2002 period (Investigation No. 131-022), and (2) testimony offered at the House Agriculture (continued...)

Supporters of CAFTA

With Central America a net dairy importer, the *National Milk Producers Federation* (NMPF), representing dairy farmers and their marketing cooperatives, sees clear benefits for the U.S. dairy industry in a growing market for milk powder and cheese. It views the elimination of CAFTA tariffs as possibly stimulating additional U.S. dairy exports, by overcoming the advantages of subsidized EU sales and helping to undercut prices of similar products from New Zealand and Australia. NMPF does not foresee much competition from CAFTA dairy products once they receive free access to the U.S. market, as long as such access is restricted to products produced from milk and dairy ingredients that originate in the region. The *National Cotton Council* (NCC), representing cotton farmers, ginners, warehousers, merchants, cottonseed crushers, cooperatives and textile manufacturers, supports the negotiations, expecting increased opportunities for U.S. cotton fiber exports as textile and apparel products produced in the region become more competitive in the U.S. market. NCC is concerned that unless effective rules of origin are incorporated into CAFTA, the U.S. textile sector could experience a negative impact if third country textile products are transhipped through Central America to take advantage of duty-free and quota-free access to the United States. It supports a phase-out of the U.S. cotton fiber TRQ, as long as CAFTA includes tight rules of origin and safeguard provisions.

The *Northwest Horticultural Council* advocates the complete elimination of all Central American tariffs on U.S. apples, pears, and sweet cherries (ranging from 14% to 28%). The Council views the region as a growth market for fresh fruit, particularly Red Delicious apples. It also believes improved access to the region will help its growers and shippers address fierce competition from Chilean fruit growers, whose products now enter some countries duty-free under current free trade agreements. The *Western Growers Association* (representing the California and Arizona fresh fruit, vegetable, and nut sectors) recommends that U.S. negotiators provide these countries with immediate permanent duty free access to the U.S. market, since produce from the 5 countries already enters free under the CBI trade preference program. This association recommends that the CAFTA countries reciprocate by offering immediate tariff elimination on the same products. Western Growers further calls for negotiators not to eliminate or reduce any U.S. safeguard measures that deal with phytosanitary issues, nor to relax or eliminate antidumping or countervailing duties that protect against the dumping of these products in the U.S. market.

The *Grocery Manufacturers of America* (GMA) supports duty-free treatment for all primary commodities and food and beverage products in the shortest time frame possible. It advocates that "under no circumstances should any exceptions be made for U.S. imports of sugar, peanuts or dairy products," arguing that if the TRQs that restrict their entry are not reduced or eliminated, "the opportunities for increased trade will be significantly reduced" and undermine CAFTA's purpose. GMA views Central America as a "potentially strong growth market" for processed food and beverage products, which still face high tariffs. Its other negotiating objectives include ensuring

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[13] (...continued)
Committee's hearing held June18, 2003 on "Multilateral and Bilateral Agricultural Trade Negotiations."

that CAFTA's SPS rules are consistent with WTO rules and are based on sound science, building upon WTO technical barriers to trade provisions to require that technical regulations and standards are not more trade-restrictive than necessary, ensuring trademark protection for branded food products, and securing commitments from Central American countries to eliminate discriminatory taxes on carbonated soft drinks compared to similar beverages.

The *Sweetener Users Association* (industrial users of sugar and other caloric sweeteners and the trade associations which represent them) favors including sugar in bilateral free trade negotiations (including CAFTA), foreseeing that opening up the U.S. market to additional imports would result in lower sugar prices that benefit them and consumers. Liberalizing sugar trade, it argues, would encourage product innovation and stimulate demand, keep food manufacturing jobs in the United States rather than see them move overseas, help maintain a viable cane refining industry with well-paid union jobs, and stimulate competition and thus thwart excessive industry concentration.

Opponents of CAFTA

Some commodity and food product groups oppose their inclusion in the CAFTA, and the reduction and elimination of U.S. tariffs on competitive imports from the region. The *American Sugar Alliance* (ASA) sees dangers in using FTAs to liberalize trade in sugar, arguing that the Administration's piecemeal approach does not address all kinds of distortions in the world sugar market, leaves any "free trade area vulnerable to the harmful effects of subsidies outside the region," and undercuts efforts to remove sugar trade distorting policies in the WTO talks. It points out that the FTAs proposed with Central America and Australia (both major sugar exporters) and Brazil (the world's largest sugar exporter, and also participating in the FTAA) would "force the United States to import more sugar than it needs" and "be a disaster for domestic producers and for foreign suppliers." ASA insists the only way to negotiate global free trade in sugar is in the multilateral WTO context, where all forms of trade-distorting practices (not just tariffs and quotas) used worldwide are made subject to "more far reaching, disciplines." The *National Juice Products Association* (juice and juice beverage processors) opposes any reduction in U.S. tariffs on imports of orange, grapefruit, lemon and grape juices from the 5 Central American countries. It argues that these tariffs have allowed U.S. juice processors "to make use of imported frozen manufacturing concentrate" when U.S. fruit output has not met demand, and also allowed domestic fruit growers "to realize reasonable rates of return during peak production years." Eliminating tariffs, in its view, "would inevitably result in increased imports of juice products" from these countries, and in turn, adversely affect the ability of juice extractors (that supply juice processors) and fruit growers to compete against lower-priced imports and preserve juice quality levels.

The *National Watermelon Association* (producers, handlers and shippers) opposes any tariff reduction on watermelon imports from Central America. It argues that these countries' lower costs would "further handicap efforts to improve economic returns" to domestic watermelon producers, who have worked to achieve a balance in the marketplace using an industry-funded research and promotion marketing order. The *American Dehydrated Onion & Garlic Association* (representing two California firms) opposes any tariff reduction on U.S. imports of dehydrated onion and/or garlic, but if not possible, requests that these import sensitive products be given "an extended tariff phase-out period (of perhaps 15 years or longer)". It argues that eliminating tariffs would devastate the domestic industry and the rural communities dependent upon it. The Association points out that the GSP trade preference program and all U.S. free trade agreements have acknowledged the import sensitivity of these products, determining them not eligible for zero duty treatment and granting them the longest tariff phase-out periods.

Other Groups' Views

Some groups view favorably the Administration's push for bilateral FTAs, seeing the potential for market openings. However, several condition their support for CAFTA on U.S. negotiators addressing specific issues. The *National Chicken Council* and *USA Poultry and Egg Export Council* place poultry, particularly chicken leg quarters, as a priority agricultural issue in CAFTA. While tariffs and quotas on poultry trade may be reduced, these groups see sanitary and veterinary provisions as the "critical hurdle to overcome" in these negotiations. The *National Pork Producers Council* (NPPC) wants U.S. negotiators to persuade the Central American countries to accept the U.S. meat inspection system as sufficient to ensure the food safety of U.S. pork exports in addition to eliminating their pork tariffs. It calls these countries' practice of sending their own inspectors to U.S. pork plants "completely unacceptable" and having the effect of operating as a non-tariff trade barrier. The NPPC points to Chile's last-minute decision to accept meat from any USDA-approved facility before the Administration submitted the U.S.-Chile FTA to Congress as an important precedent to follow to resolve non-tariff barriers alongside tariff negotiations in all ongoing bilateral and regional trade talks.

The *National Cattlemen's Beef Association* (NCBA) views efforts to increase trade relationships with Central America as bolstering "front-line defenses against the introduction of foreign animal diseases" from South America, and developing the potential to export moderate amounts of high quality U.S. beef to the region for tourism and restaurants. With this region filling only 35% of its share of the U.S. beef TRQ in recent years, the NCBA apparently does not expect much competition under a FTA. The U.S. beef industry believes three key aspects must be considered as negotiations near conclusion: (1) CAFTA must not exclude any agricultural product, (2) Central American governments "must begin to understand that congressional ratification will be difficult and improbable without the support of U.S. agriculture on Capitol Hill," and (3) negotiations on tariff rate reductions should start at the current applied tariff rates, not the much higher WTO bound rates that countries recently reverted to, in order to negotiate reductions down from a higher level.

Though U.S. feed grain fills most of the region's import demand, the *National Corn Growers Association* (NCGA) expects to gain additional market access in Central America with free trade under CAFTA. It calls for immediate elimination of corn tariffs in as many of the CAFTA countries as possible, and an end to the use of commodity absorption arrangements by El Salvador, Honduras and Nicaragua. The NCGA also seeks agreement that the 5 countries will evaluate products derived from agricultural biotechnology "solely on the basis of sound science." Wheat producers (represented by the *Wheat Export Trade Education Committee*, *U.S. Wheat Associates*, and the *National Association of Wheat Growers*) view all of the bilateral FTA negotiations as "stepping stones" to address those concerns that are being debated in the WTO and the FTAA, by moving "trade liberalization further than what ... can be achieved multilaterally." Their spokesman notes U.S. wheat exports have posted gains in Central America, accounting for a 70% market share, with sales prospects best in Guatemala and Costa Rica. These three groups, while acknowledging that negotiations must provide a way to address SPS issues, do not support "holding up" trade agreements "until every single scientific issue is resolved."

The *USA Rice Federation* notes that most Central American countries protect their domestic rice millers by prohibiting milled rice imports. U.S. rice exporters further face high bound tariffs, non-trade barriers and SPS restrictions in these markets. The Rice Federation recommends that negotiators seek: immediate low and equal tariffs on all types and forms of rice, to be reduced to zero; substantial disciplines on how TRQs operate, to make more open licensing regimes, and on how SPS rules are enforced; and the elimination of absorption arrangements and price bands. The *American Soybean Association* expects CAFTA will benefit U.S. soybean growers and seeks the elimination of tariffs and price bands and the resolution of outstanding SPS issues in the agreement. The *Distilled Spirits Council* seeks the immediate elimination of Central American duties on imports of U.S. products (which range from 5% to 40%), protections for Bourbon and Tennessee Whiskey as distinctive U.S. products (included in the FTA with Chile), and addressing of technical trade barriers that impede sales to some countries.

Status of CAFTA Negotiations on Agriculture

The details of liberalizing trade in agricultural products between the 5 Central American countries and the United States are being negotiated in the market access group, one of the 5 negotiating committees established for the CAFTA talks. Interest groups and politicians on each side have continually advocated immediate access in the export market for those agricultural products viewed as the most sensitive by the importing country or region. Each side exchanged initial market access offers covering all products (agricultural and manufactured goods) in their May 2003 negotiating round. Subsequent sessions in June and July involved considerable discussion about what time periods (sometimes referred to as "baskets") to use to phase out tariffs and quotas on agricultural products, about each side's views on their "sensitive" commodities, and about different options that might be used to handle those commodities for which each side sought the longest transition period to free trade. Both sides reportedly agreed in June to use four different baskets to phase out border protection. Tariffs on products placed in the first basket would be eliminated immediately. Those falling in the second and third baskets would see their tariffs removed after 5 or 10 years, respectively. Protection on the most sensitive agricultural products (placed in the fourth basket) would be phased out over a longer undefined period. Negotiators at their September session agreed upon a 15-year period for phasing out protection for these sensitive products, and split the fourth basket into two: one ending protection after 12 years, and another after 15 years.[14]

[14] Based on selected articles from issues of *U.S. Inside Trade* and BNA's *Daily Report for Executives*.

Differences remain on which agricultural products are to be placed in the longer-than 10-year transition basket, and reportedly were not settled at the October 20-24 negotiating session. At this session, U.S. negotiators planned to request that sugar, peanuts, and a few other products be placed in the longer than 10-year transition category. Their Central American counterparts reportedly classified beef, pork, corn, rice, poultry, dry beans, and potatoes as their sensitive agricultural commodities, and are seeking the longest tariff phase-out transitions for these. The U.S. proposal did not exclude any agricultural product, but for those subject to a TRQ, market openings are "relatively modest," according to lead negotiator Regina Vargo. She also stated that negotiators had not finalized which products would be covered by a TRQ.[15]

At the October session, U.S. negotiators secured a commitment from the Central American negotiators to provide immediate market access on several U.S. horticultural products. These include apples, pears, grapes, cherries, peaches, sweet corn, and limes.[16] In return, the United States reportedly made permanent the preferential duty free treatment under CBI that Central American horticultural products now receive in selling to the U.S. market.

Even with some progress, observers note that negotiators still must address more difficult issues and settle many details to meet the December 2003 target for concluding a CAFTA agreement. One key issue will be to resolve which sensitive agricultural products fall in the 12-year basket and which benefit from the longest transition period (15 years). Another is determining whether applied or bound tariff levels should be used as the basis from which to reduce tariffs. The Central American countries advocate starting with the much higher bound levels reflecting their WTO commitments (Table 3). To bolster their negotiating position, some governments raised tariffs on key agricultural imports up toward bound levels in 2002 and 2003. The United States favors reducing tariffs from current applied levels, reflecting its stance in the WTO and FTAA trade negotiations, seeking to gain quicker benefits under new market openings. Once these issues are settled, negotiators will wrestle on a tariff line basis on the details of TRQs – setting the size of each quota and its growth rate until phased out, and determining both the within-quota tariff level (low or zero) and the pace at which the much higher over-quota tariff is phased out.

Other provisions applicable to agricultural trade that negotiators will work on include developing rules of origin and special agricultural safeguards. Whether rules of origin for an agricultural product are written to be tight or relaxed can have a bearing on the pace at which negotiators agree to reduce border protection. Safeguards (involving the temporary use of higher tariffs and/or quotas) allow producers of sensitive products additional time to adjust to increased import competition. U.S. negotiators are expected to propose to use automatically-triggered price-based safeguards (modeled after provisions included in the U.S.-Chile FTA) to protect U.S. producers from sudden surges in sensitive agricultural imports from the 5 Central American countries. Similarly, Central American negotiators have

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[15] *Inside U.S. Trade*, "Controversial CAFTA Textiles, Agriculture Work Left for December," October 31, 2003, p. 7.

[16] BNA Inc., *International Trade Reporter*, "International Agreements: CAFTA Negotiators Reach Agreement on Industrial Products, Vargo Says," October 30, 2003, p. 1801.

reportedly raised the concept of tying tariff reductions on imports of their sensitive products to decreases in U.S. farm subsidies provided to such commodities.

Role of Congress

The Bipartisanship Trade Promotion Authority Act (TPA) of 2002 (Section 2102 of P.L. 107-210, Trade Act of 2002) sets out broad objectives for U.S. negotiators to follow in developing agricultural provisions in trade agreements. These are reflected in the specific objectives USTR laid out in notifying Congress of the Bush Administration's intent to negotiate a CAFTA agreement (see pages 7-8). Section 2104(b) requires the President to consult with Congress on specific agricultural issues as negotiations proceed. This interaction during the period of consultation on negotiating positions and strategies is intended to lay the groundwork for subsequent congressional consideration of any CAFTA agreement. In particular, the USTR must follow special consultation procedures with the House and Senate Agriculture, the House Ways and Means, and Senate Finance Committees before engaging in, and during, trade negotiations that affect more than 200 import-sensitive agricultural commodities and food products.[17] Once an agreement is signed, the President and Congress will develop draft implementing legislation that Congress will consider on an expedited basis according to TPA procedures.

Some Members of Congress have signaled concerns with the agricultural market access offers and positions presented by Central American negotiators in recent months. The Chairman and Ranking Member of the Senate Finance Committee have charged that the Central American negotiators are making unrealistic demands on access into their markets of U.S. farm products. These legislators called for the elimination of tariffs and other barriers on products of interest (including beef, pork, corn, wheat and soybeans) "as soon as possible, and preferably immediately. ... Without real market access benefits accruing to U.S. farmers and ranchers through the CAFTA, support for the proposed [agreement] will be subject to question." Both Senators also urged U.S. negotiators to make the acceptance of the U.S. beef and pork inspection system by the Central American countries a top priority and to emphasize the importance that these countries make their SPS policies "science-based, transparent and predictable, and thus WTO compliant" so that U.S. exporters know what is expected when they sell products to that region. The House Agriculture Committee Chairman similarly stated that "countries negotiating with the U.S. must place meaningful offers on the table ... which provide increased access to U.S. agricultural goods, if they hope to secure passage by the U.S. Congress." In a visit to

[17] To assist in its consultations with Congress and prepare for negotiations, USTR in September 2002 requested the U.S. International Trade Commission (ITC) to analyze the probable economic effect of providing duty-free treatment for imports from the 5 Central American countries on U.S. industries that produce like or directly competitive articles and on consumers. USTR's request specifically called for an analysis of the economic effects of eliminating tariffs on imports of these sensitive agricultural products. The ITC was asked to submit its confidential report to USTR by year end 2002.

Costa Rica, he "stressed that U.S. [producers] are becoming wary of trade negotiations for which they see no benefit for their products."[18]

Eight House Members have urged USTR "to proceed with caution" in the CAFTA negotiations, pointing out that U.S. negotiators in this and other regional trade agreements "would immediately confront significant and troubling issues involving sugar trade." Concerned that the recent collapse of the WTO negotiations in Cancun might result in a U.S. policy emphasis to negotiate FTAs that "tend to magnify, rather than reduce, trade distortions," they urged Ambassador Zoellick to reassess the principles underlying this approach to ensure they serve national interests. Their letter urged that ongoing CAFTA negotiations not undermine current U.S. sugar program and policy, and should include strong enforcement tools to deal with labor and environmental standards. Reference was made to Guatemala's sugar industry – "rife with trade-distorting labor and environmental differences that lower production costs."

[18] Letter from Senators Grassley and Baucus to USTR Ambassador Zoellick, August 29, 2003; press release issued by Congressman Goodlatte, August 7, 2003.