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Number 573

MICHIGAN AGRICULTURE: LINKS TO NAFTA

A RESOURCE MANUAL FOR EXTENSION EDUCATORS

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Introduction

During the past two decades, the American farm and food system has become increasingly dependent on world markets. Export markets are an important outlet for U.S. farm and food products, while food imports enrich American diets and imports of inputs reduce production costs in the farm and food system. Increased trade has led to greater income and employment in the farm and food system, and food exports have helped improve the U.S. balance of payments.

As a result of this increased interdependence, markets for U.S. food products are now affected by economic changes and policies throughout the world. Such changes sometimes lead to greater market instability and political conflicts over agricultural trade policy issues. This conflict occurs largely because the domestic policies of individual nations often clash with the policies needed to maintain an effective international trading system. The major question is whether policies can be developed to permit both U.S. consumers and producers to obtain the benefits from international trade without undue market instability or policy conflicts with other nations.

This publication examines the economic and political factors affecting agricultural trade. It is designed to provide a basic understanding of agricultural trade without an excessive use of the technical jargon of trade theory and policy. Data and examples have been included to illustrate the major topics discussed in the text, but many details were omitted in an effort to simplify the presentation.

Chapter I discusses why nations trade, examines the importance of trade to U.S. and Michigan farmers, and identifies our trading partners. Chapter II examines the types of trade protection used by nations, the impact of trade policies on farmers and consumers, and the reasons for extensive protection in international agricultural markets. Chapter III explains the mechanism for developing trade policies and discusses the leadership role the U.S. has played in the formation of trade policy during the past 50 years. Chapter IV examines U.S. trading relations with its North American neighbors — Canada and Mexico — and reviews the North American Free Trade Agreement, including its potential implications for Michigan agriculture. Chapter V examines the impact of the formation of trade blocs on international agricultural markets. Chapter VI provides a summary of the main topics and draws broad conclusions about the future of agricultural trade policy.

In addition to this resource book, the manual includes a glossary of agricultural trade policy terms and a set of camera-ready graphics for use in making presentations. These overheads present the major topics of each chapter and the tables and figures that appear in the text.

CHAPTER I

TRADE AND GLOBAL INTERDEPENDENCE IN THE FARM AND FOOD SYSTEM

ISSUES TO CONSIDER

- Why do nations trade?
- How important is agricultural trade to the United States?
- Who are our trading partners?
- How important is agricultural trade to Michigan?

International trade can be the source of improved living standards and greater economic opportunity. It can also be the source of some of the most complex and divisive policy issues facing national governments today.

International trade can be the source of improved living standards and greater economic opportunity. It can also be the source of some of the most complex and divisive policy issues facing national governments today.

This chapter begins by discussing how economists explain trade in a theoretical manner. Like any theory, trade theory is a simplification of reality. It is based, however, on two fundamental processes — specialization and exchange — that describe many aspects of economic activity. The remainder of this chapter will examine the importance of trade to the farm and food system in the United States and Michigan.

Trade is based on two fundamental processes — specialization and exchange — that describe many aspects of economic activity.

WHY NATIONS TRADE

Trade occurs between individuals, regions and nations. An individual employed in one industry is, in fact, trading his or her labor for wages that can, in turn, be exchanged for goods and services produced by individuals employed in other industries. By permitting individuals to use their abilities and resources in a manner that increases their efficiency, this process of specialization and exchange generates an increase in the economy's total output of goods and services.

The principle of comparative advantage suggests that each region or country will specialize in the production of those commodities for which it has the greatest relative cost advantage.

Trade between regions or between countries arises from this same process of specialization and exchange based on the principle of comparative advantage. Comparative advantage suggests that each region or country will specialize in the production of those commodities for which it has the greatest relative cost advantage. Relative costs differ

among producers because of differences in natural resource endowments, including land, water and minerals; other productive resources such as capital and skilled labor; and technological sophistication and institutional arrangements. Because countries specialize in different products, trade ensures that consumers have access to products from other countries and that producers have access to markets in other countries.

Comparative advantage becomes operational at the farm or firm level when producers select a production program that is expected to generate the greatest net return given their market expectations and their available land, labor, capital and managerial expertise. In other words, given the relative production costs and market conditions, each producer seeks to maximize profits within the constraints imposed by available resources and markets.

Comparative advantage becomes operational at the farm or firm level when producers select a production program that is expected to generate the greatest net return given their market expectations and their available land, labor, capital and managerial expertise.

The concept of comparative advantage can be illustrated with a common example. Farmers in Iowa can produce either corn or wheat, but their net return from a given batch of resources is greater if they grow corn rather than wheat. Farmers in Kansas can also produce corn and wheat, but their net returns, on average, will be greater for wheat than for corn. As a result of these differences in returns, Iowa growers will specialize in corn production and Kansas growers will specialize in wheat production. The total economic output from the states' resources and the profitability of farming in both regions would both be reduced without specialization and trade. A numerical illustration of this example is provided in appendix I-A.

This same principle of comparative advantage operates at the international level. Farmers in each country produce those commodities that are expected to generate the greatest return from their resources and efforts. When these differences operate on a regional and national basis, the principle of comparative advantage explains why the Midwest is the leading producer of grain and soybeans in the United States, while California, Florida and Texas specialize in fruits and vegetables, and the Mississippi Delta states produce cotton and rice. Specialization is also observed among nations, explaining why the United States exports feed grains and soybeans and imports cocoa, coffee and spices from tropical countries. Similarly, this principle explains why Australia specializes in the production of wheat and range-fed livestock, while New Zealand exports dairy products and Thailand exports rice.

The principle of comparative advantage explains why the United States exports feed grains and soybeans while importing cocoa, coffee and spices from tropical countries. Similarly, it explains why Australia specializes in productio of wheat, while New Zealand exports dairy proaucts and Thailand exports rice.

The underlying cause of these national and regional patterns of specialization is the notion that producers, whether in agricultural or non-agricultural pursuits, seek to maximize the profits earned from their talents and resources. This search for profit leads to specialization in production. When a region or nation specializes, it produces more of some commodities than its consumers will purchase but not enough of some other products. Thus, each region must trade its surplus production for those items it does not produce in sufficient quantity. As a result, specialization and trade lead to improved welfare and greater total output than would be available if each nation were self-sufficient in all commodities.

Specialization and trade lead to improved welfare and greater total output than would be available if each nation were self-sufficient in all commodities.

Although specialization among countries is based largely on comparative advantage, government intervention can influence the pattern of agricultural production and trade. This fact raises a number of questions: Should a nation depend on one or a few commodities for income? Is there a connection between trade restrictions and the desire to diversify production or to achieve food security? The principle of comparative advantage is based on the assumption that there are no restrictions on trade flows. That is, it is assumed that there are no market imperfections arising from factors such as the domination of markets by a few buyers or sellers, unequal access to price and market information, or unequal ability to enter and exit certain markets. Consequently, the question continues to be asked: how well does the principle of comparative advantage apply in the real world and what are the consequences of trade barriers that attempt to protect domestic markets from international competition? This publication will examine some of these issues.

Although specialization among countries is based largely on comparative advantage, government intervention can influence the pattern of agricultural production and trade among countries.

The Importance of International Trade to U.S. Agriculture

The growth in international trade has benefited both producers and consumers. The process of specialization and trade provides consumers with lower prices and a wider variety of products. For example, American consumers enjoy tropical products (coffee, bananas, avocados and cocoa) that could be produced only at very high cost in the United States. Similarly, other countries gain access to American wheat and soybeans or Michigan cherries and apples. Trade also provides consumers with year-round access to seasonal products. For example, imports of fruits and vegetables from Latin America during

The growth in international trade has benefited both producers and consumers in the United States. Consumers have gained lower prices and a wider variety of goods, while producers have gained greater export opportunities and increased employment in export-related industries.

the winter months provide a continuing source of some products that are produced only during the summer in the United States.

During the past two decades, U.S. agriculture has become more dependent on international markets. In the 1970s, crop output increased by nearly 47 percent, most of which went to foreign buyers, and the output from two out of every five cultivated acres was exported (Knutson, Penn and Boehm). The United States supplies a wide variety of food, exporting animal products, grains, oilseeds, fruits, nuts, tobacco, cotton and other agricultural products to markets around the world (Table 1). The value of total U.S. agricultural exports was $7.2 billion in 1970, $41.3 billion in 1980, and $39.3 billion in 1990 (Figure 1).

The competitive position of U.S. agriculture in international markets is critically important to the financial success of farmers, agribusinesses and food industries. If export markets were not available, then production of several commodities would have to be reduced or prices of these products would decrease significantly. For example, 26 percent of total U.S. corn production and 39 percent of total wheat production were exported in 1990 (Table 2). The loss of export markets for these products would affect the profitability of farmers, input suppliers and food processing firms.

Exports of food products also generate significant economic activity in other sectors of the economy. Each dollar of U.S. food exports generates $1.52 of additional output in the American economy. Thus, the $40 billion of food products exported during 1989 generated an additional $61 billion of economic activity in the American economy. U.S. food exports generated 1.06 million jobs in 1989, with 580,000 of these jobs being supported in the non-farm sectors of the economy (Lipton and Manchester).

U.S. agriculture has become more dependent o international markets during the past two decades, and the competitive position of agriculture in international markets is critically important to the financial success of farmers, agribusinesses and food industries.

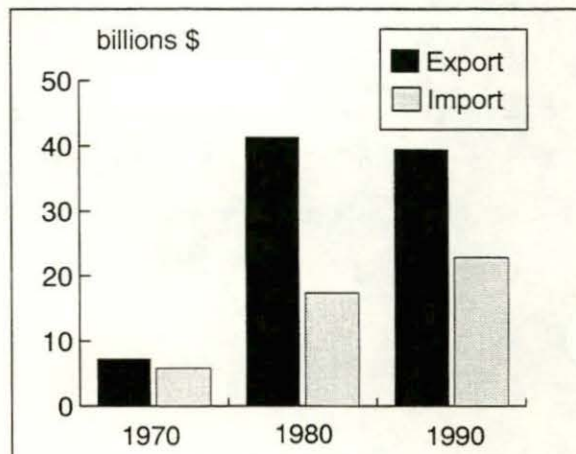
U.S. food exports generated 1.06 million jobs in 1989, with 580,000 of these jobs being supported in the non-farm sectors of the economy.

Table 1. U.S. agricultural exports (million $).

	Fiscal Years		
	1989	1990	1991
Meats and preparations	2,862	3,136	3,511
Other animal products	1,481	1,178	1,257
Hides, skins and furs	1,713	1,844	1,457
Wheat and flour	6,265	4,410	3,058
Feed grains	7,376	8,094	5,789
Other grains & products	3,189	3,194	3,358
Fruit & nuts	2,659	3,117	3,376
Vegetables	1,542	2,079	2,597
Tobacco	1,249	1,359	1,533
Cotton	2,040	2,704	2,605
Oilseeds & products	6,629	6,099	5,609
All other products	2,606	3,059	3,463
TOTAL	39,611	40,271	37,613

Source: USDA, 1992

Figure 1. U.S. agricultural trade, 1970-1990.



Who Are Our Trading Partners?

Many nations depend on U.S. exports for a portion of their food needs. Japan is the largest buyer of U.S. feed grains, while Asian and African countries are the largest markets for U.S. wheat and flour products (appendix I-B and I-C).

The United States also depends on other countries for food imports, including fruits, vegetables, beef, sugar, vegetable oils and tropical agricultural products. Many of these tropical products, such

Table 2. Percentage of U.S. production exported.

	1970	1980	1990
Corn	14%	37%	26%
Soybeans	39%	45%	30%
Wheat	52%	57%	39%
Apples	1%	6%	9%
Beans & pulses	45%	63%	49%

Scource: U.N. Food and Agriculture Organization

The value of Michigan farm exports ranged from $900 million per year in 1980-81 to $500 million during 1984-87 and $800 million in 1989-90.

Trade policy disputes among nations arise because adjustments to the opening of trade do not occur automatically and without cost.

Because the benefits of trade are widely distributed but the costs of trade adjustment usually fall on a smaller number of people, national governments often use trade restrictions to reduce the impact of these costs.

as bananas or spices, do not compete directly with U.S. products. The value of agricultural imports rose from $5.8 billion in 1970 to $17.4 billion in 1980 and $22.8 billion in 1991 (appendix I-D).

The Importance of International Trade to Michigan Agriculture

Agriculture and related food industries are the second largest sector of the Michigan economy, valued at $23 billion annually and employing one-eighth of the total labor force in Michigan's primary industries. The value of Michigan farm exports ranged from $900 million per year in 1980-81 to $500 million during 1984-87, and $800 million in 1989-90 (appendix I-E). Export markets accounted for nearly one-third of cash receipts from farm marketings in 1980-81 but decreased to 20 to 25 percent in recent years. Michigan's major exports are (in order of value) feed grains and products, soybeans and products, wheat and products, vegetables (including dry beans), fruit, live animals and meat (Ferris).

Why are there Disputes over Trade Policy Issues?

Given the benefits that come from international trade, why are trade policy disputes among nations increasing in number and intensity? The primary reason for these disputes is that, unlike the example of trade between Iowa and Kansas discussed earlier, adjustments to the opening of trade do not occur automatically and without cost.

The benefits of increased trade accrue mainly to consumers of imported products and producers of exports. Producers who face increased competition from imports are likely to suffer a loss of income and a depreciation in the value of their productive assets. Thus, though increased trade is likely to benefit the nation as a whole, some individuals are likely to suffer short-term losses. Because the benefits of trade are widely distributed but the costs of trade adjustment may fall on a smaller number of people, national governments often use trade restrictions to reduce the impact of these costs. The use of these restrictions and the process by which the nations of the world attempt to reduce these restrictions will be the subject of the next two chapters.

Appendix I-A.

An illustration of comparative advantage with Iowa and Kansas yields.

A region's or country's comparative advantage is determined by its relative cost of producing goods. A good's relative cost of production is measured by the number of units of another good that must be given up to produce one unit of it. To examine the concept of comparative advantage, assume that Iowa and Kansas have the following average yields of corn and wheat:*

	Corn	Wheat
Iowa	150 bushels per acre	50 bushels per acre
Kansas	100 bushels per acre	40 bushels per acre

Case 1: Assume there is no trade and that each state allocates 50 percent of its land to producing corn and 50 percent to producing wheat. In this case:

Iowa will average 100 bushels of grain per acre ($150 \times 0.5 + 50 \times 0.5 = 100$)
Kansas will average 70 bushels of grain per acre ($100 \times 0.5 + 40 \times 0.5 = 70$)
Total production will average 85 bushels of grain per acre ($100 \times 0.5 + 70 \times 0.5 = 85$)

Case 2: Assume that each state specializes in production and trades with the other. Given the yields shown above, the relative cost of producing corn and wheat in each state can be calculated:

Iowa's ***relative*** cost:
of producing one bushel of corn is 0.3 bushels of wheat ($50/150 = 0.3$)
of producing one bushel of wheat is 3.0 bushels of corn ($150/50 = 3.0$)

Kansas' ***relative*** cost:
of producing one bushel of corn is 0.4 bushels of wheat ($40/100 = 0.4$)
of producing one bushel of wheat is 2.5 bushels of corn ($100/40 = 2.5$)

These results indicate that Iowa must give up 0.3 bushel of wheat to produce each additional bushel of corn, while Kansas must give up 0.4 bushel of wheat to produce each additional bushel of corn. Thus, the relative cost of producing corn in Iowa is less than in Kansas, and Iowa will specialize in corn production. Similarly, Kansas' relative cost of producing wheat (2.5 bushels of corn) is less than Iowa's (3.0 bushels of corn), and Kansas will specialize in wheat production. In this case:

Iowa will average 150 bushels of grain per acre.
Kansas will average 40 bushels of grain per acre.
Total production will average 95 bushels of grain per acre ($150 \times 0.5 + 40 \times 0.5 = 95$).

Many factors can affect comparative advantage, but these simple results demonstrate why economists conclude that specialization and trade permit more efficient use of resources, an increase in total production, and an increase in consumer and producer welfare.

*Other simplifying assumptions include: The prices of corn and wheat are the same, the costs of production per acre are also the same, and there are no transportation costs between Iowa and Kansas.

Appendix I-B. Imports of wheat and feed grains from the United States and total imports by major regions or nations, 1989-1990.

	Annual Average Feed Grain Imports (Million Metric Tons)		Percent from the U.S.	Annual Average Wheat Imports (Million Metric Tons)[1]		Percent from the U.S.
	From U.S.	Total	%	From U.S.	Total	%
Central America	7.8	8.8	89	1.8	3.2	56
South America	1.5	2.1	71	2.0	4.8	42
Europe	5.1	21.7	24	1.0	17.0	6
Africa	3.4	5.9	58	6.4	19.4	33
Mideast	4.4	9.3	47	2.3	12.2	19
CIS	14.4	20.4	71	4.5	14.9	30
China	0.2	6.3	3	5.5	14.7	37
Japan	16.7	21.7	77	2.8	5.5	52
Other Asia	9.8	11.4	86	6.8	15.6	44
Other Nations	0.9	1.6	56	0.1	.9	22
World	64.2	109.2	59	33.2	108.2	32

Source: USDA and United Nations Food and Agriculture Organization

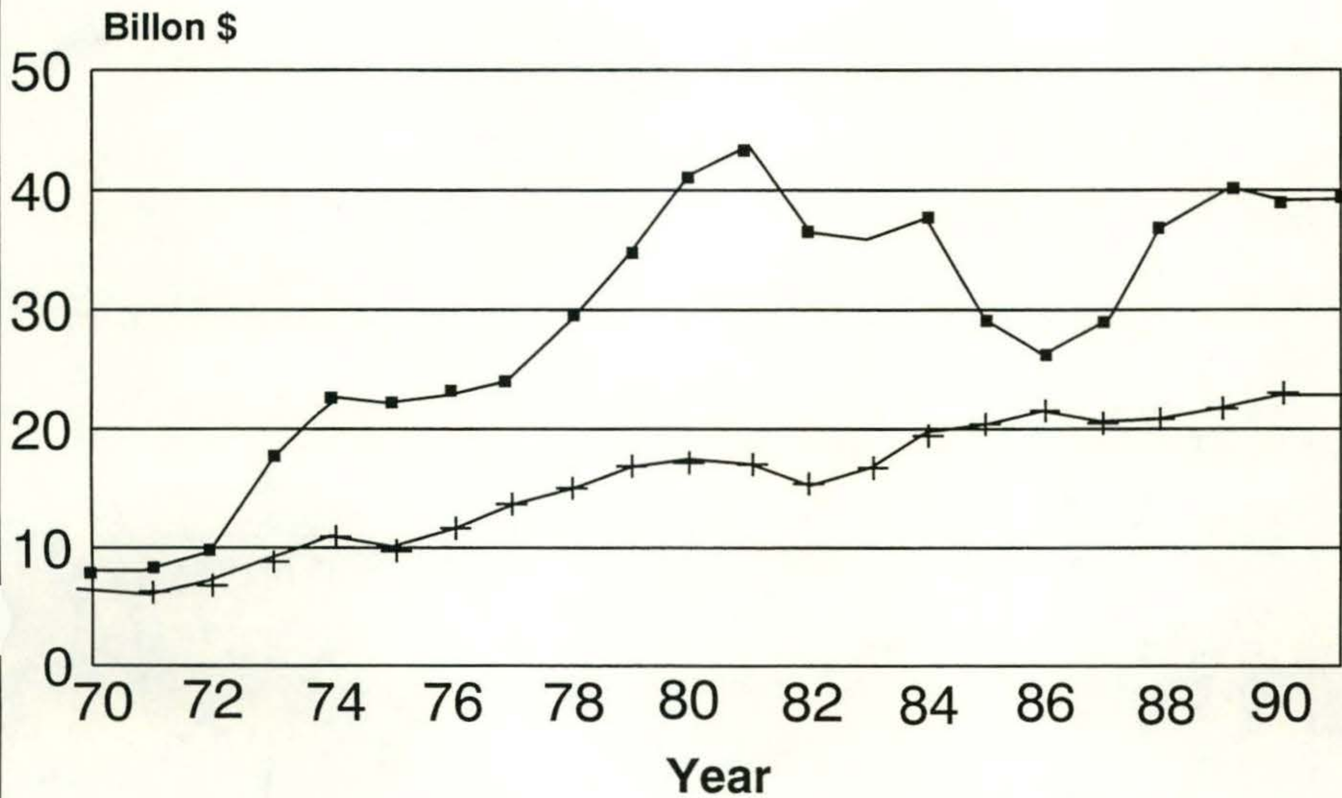
[1] Includes wheat flour (measured as wheat equivalent).

Appendix I-C. Total U.S. agricultural exports by major regions or nations (Million Dollars).

Region or Country	1989	1990	1991
European Community	6,539	6,878	6,779
Other Western Europe	510	493	536
Eastern Europe	422	533	306
USSR	3,229	3,006	1,758
West Asia	2,273	1,996	1,430
China	1,496	909	668
Japan	8,148	8,155	7,738
Taiwan	1,594	1,818	1,738
South Korea	2,453	2,690	2,159
Other Asia	2,710	2,594	2,366
Africa	2,280	2,011	1,883
Mexico	2,757	2,667	2,885
Other Latin America	2,683	2,489	2,614
Canada	2,179	3,715	4,409
Oceania	268	317	346
TOTAL	39,611	40,271	37,613

Source: USDA.

Appendix I-D. U.S. agricultural exports and imports, 1970-1991.



Source: USDA — Exports + Imports

Appendix I-E. Estimated value of Michigan's exports of agricultural products, 1980-81 to 1989-90 (million dollars).

	1980-81	1981-82	1982-83	1983-84	1984-85	1985-86	1986-87	1987-88	1988-89	1989-90
Wheat and products	63	70	32	48	42	112	69	50	125	105
Feed grains and products	389	242	254	347	208	150	136	158	178	255
Soybeans and products	136	123	126	156	91	92	86	141	132	107
Vegetables and preparations (Including dry beans)	168	134	60	56	51	58	51	61	55	87
Live animals and meat (Excluding poultry)	27	29	27	24	22	21	24	37	48	51
Hides and skins	12	14	15	19	19	17	19	22	22	24
Poultry and products	6	5	3	3	3	4	5	5	6	5
Fats, oils and greases	12	12	10	11	10	6	5	7	7	6
Dairy products	6	9	10	11	10	11	11	11	10	7
Feeds and fodders	16	17	18	20	16	19	23	30	36	30
Seeds	7	8	8	8	9	9	9	10	13	14
Others	17	12	12	14	11	14	14	17	27	40
TOTAL	896	709	609	742	517	547	485	597	709	805

Source: USDA.

Chapter II

GOVERNMENT INTERVENTION IN AGRICULTURAL TRADE

Issues to consider

- Do all nations protect their agricultural markets?
- What is the justification for agricultural protection?
- What are the common types of trade barriers?
- What is the impact of trade barriers on producers and consumers?

Despite the economic benefits that can be gained from trade, governments frequently employ policies that restrict the flow of imported goods. These policies affect producers and consumers in both importing and exporting nations. This chapter will discuss those policies that are used most frequently to restrict trade. The impact of these policies on importing and exporting nations will also be examined.

Common Justifications for Agricultural Protection

Nearly every nation employs some form of government restrictions on agricultural trade. Policies that restrict trade are usually referred to as trade barriers or "protectionist" trade policies. Such policies are often adopted to accomplish a domestic policy objective that is in conflict with the free flow of imported goods. When these policies are used, it is often claimed that they will:

Some form of government intervention in agricultural production and trade exists in nearly every country.

- Protect a new (infant) or strategic industry from foreign competition.
- Protect domestic employment.
- Maintain domestic farm programs.
- Provide food security or guarantee an adequate food supply.
- Retaliate against the trade practices of other nations.
- Improve the nation's balance of payments.

Protecting domestic industries, reducing dependence on foreign imports for a staple food commodity or retaliating against other countries' trade policies are all strong motivations for restricting imports.

Nations usually adopt protective measures to shelter an industry from foreign competition. One such use of protection is the use of variable levies by the European Community. Using a combination of high protection and rapid improvements in technology, the EC moved from being a net importer to a net exporter of several commodities, including wheat, beef, dairy products, sugar and canola. Minimizing

the dependence on foreign imports for a staple food commodity is also a strong motivation for restricting imports. For example, Japan often claims that its ban on rice imports is needed to ensure food security and maintain an adequate domestic supply of rice. Claims that other nations are using unfair trade practices have led some countries to retaliate by restricting imports from the offending countries.

Though trade barriers may accomplish some of these objectives, policies that limit trade usually create costs that reduce the welfare of other parties in the importing country. These costs can occur as higher prices for consumers, the loss of product variety and quality provided by imports, or the misallocation of resources within the domestic economy. All such trade barriers result in damage to producers in the exporting country.

Though trade barriers may accomplish some of these objectives, policies that limit trade usually create costs that reduce the welfare of other parties in the importing country.

Types of Trade Barriers

A trade barrier is defined as any policy designed to reduce the flow of trade among nations. Although exporters sometimes impose trade barriers on goods leaving the country, in most cases it is the importing nation that attempts to reduce the entry of goods.

A trade barrier is defined as any policy designed to reduce the flow of trade among nations.

In general, trade barriers are used to protect producers from the adjustments that would be required if lower cost imports were given unrestricted access to the market. The most common types of trade barriers are import tariffs, variable levies, quantitative restrictions (import quotas or licenses), and technical regulations related to food safety or health standards. Other restrictions, such as licensing procedures, administrative barriers, or the control of production and trade by state trading agencies, can also affect international agricultural markets.

The most common types of trade barriers are import tariffs, variable levies, quantitative restrictions (import quotas or licenses), and technical regulations related to food safety or health standards.

Import Tariff: An import tariff is a tax imposed on an imported commodity. A tariff can be based on a fixed rate per unit (a specific tariff), a percentage of the value of the commodity (an ad valorem tariff) or some combination of the two. Because the specific tariff is assessed on the physical units of the product (a specific tariff might be expressed as dollars per ton), the specific tariff does not change as the price of the commodity changes. Consequently, a specific tariff would be less effective at restricting imports if the value of the commodity increases over time and the tariff rate is not adjusted. For example, the U.S. established a fixed tariff on beef of 3 cents per pound during the 1930s.

An import tariff is a tax that increases the price of an imported commodity.

A specific tariff is less effective at restricting imports if the value of the commodity increases over time and the tariff rate is not adjusted.

At a price of 10 cents per pound, this tariff offered a 30 percent level of protection. With wholesale beef prices averaging 70 cents per pound in the 1980s, the same 3 cent tariff provided only a 5 percent level of protection (Robinson). Because the ad valorem tariff is assessed as a percentage of the product's value, the tax remains a fixed percentage of the import price as the price of the product increases.

Tariffs are paid by the individual or company importing the product, with the government of the importing nation collecting the revenue. Consumers in the importing country absorb part of the tariff by paying a higher price for the commodity, while producers in the exporting country absorb the remainder of the tariff in the form of lower prices for exports. Because the prices of both the imported and domestic products have increased, producers in the importing country are the major beneficiaries of an import tariff.

Consumers in the importing country absorb part of the tariff by paying a higher price for the commodity, while producers in the exporting country absorb the remainder of the tariff in the form of lower prices for exports.

VARIABLE LEVY: A variable levy is a tariff equal to the difference between a guaranteed producer price in the importing country and the import price of the commodity on the world market. Variable levies have been used by the European Community to protect various agricultural markets. Because it is designed to maintain the internal price at a fixed level, the tax charged under a variable levy will change to reflect changes in world market conditions.

The variable levy is a tariff equal to the difference between a guaranteed producer price in the importing country and the import price of the commodity on the world market.

For example, if the government sets the internal price for wheat at $150 per ton and the world price is $100 per ton, the variable levy will equal $50 per ton. Importers of the commodity will pay a $50 tax to the government for each ton imported. If the import price decreases to $90 per ton, the variable levy automatically increases to $60 and maintains the internal price at $150. Similarly, if the import price increases to $120, the levy will decrease to $30.

Because the variable levy is adjusted to compensate for any changes in the world market price, it maintains the importer's domestic price at the level established by the government and completely insulates domestic producers from changes in world market prices. Consequently, exporters cannot increase their exports by reducing their price, since the levy will increase by an amount equal to the price reduction. Because the variable levy is automatically adjusted to offset changes in import price, it is a more complete form of protection than a fixed or ad valorem tariff.

Because the variable levy is adjusted to compensate for any changes in the world market price, it maintains the importer's domestic price at the level established by the government and completely insulates domestic producers from changes in world market prices.

As with the other forms of tariffs, the government of the importing country collects the revenue from the variable levy and consumers pay higher prices for both the imported and domestically produced commodities. Producers in the exporting country will receive a lower price for exported products, while producers in the importing country will benefit from an increase in the price they receive.

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Quantitative Restrictions: A quantitative restriction limits the quantity of a commodity that can be imported during a specific period of time. Quantitative import restrictions are used far more extensively in agriculture than in industrial products (Hillman), and it is often more difficult to negotiate reductions in such non-tariff barriers than in tariff barriers. Two common forms of quantitative restrictions are import quotas and import licenses. The United States, for example, establishes a quota on the amount of sugar imported, while Canada uses a quota to restrict imports of poultry products. The government of the importing country generally does not collect revenues from a quota policy as it does from an import tariff. Domestic producers benefit from the higher price, while domestic consumers pay a higher price for the protected product. For example, U.S. sugar producers benefit from the quota policy because import restrictions limit imports of lower priced imported sugar and maintain higher U.S. prices.

Quantitative restrictions such as import quotas or licenses limit the quantity of a commodity that can be imported. The government does not collect revenues from a quota policy as it does from an import tariff. Instead, the recipients of the quota and domestic producers benefit from the higher prices.

With an import licensing regulation, shippers importing a commodity must apply to their government for authorization to import. If issued, an import license will specify the quantity to be imported and the time period in which it may enter the country. By restricting the number of licenses issued, the government can limit the total quantity imported. For example, in 1991 Mexico had import license requirements for nearly 40 percent of the agricultural products it imported from the United States (Shane and Stallings). The importer, not the foreign supplier, receives the additional revenue created by the licensing system (the difference between the import price and the higher internal price). Like other trade barriers, import licenses reduce the quantity imported, increase the price paid by consumers and increase the price received by producers in the importing country.

An import license specifies the quantity to be imported and the time period in which it may enter the country. By restricting the number of licenses issued, the government can limit the total quantity imported.

Technical regulations are standards that products must meet if they are to be admitted into the importing country.

TECHNICAL REGULATIONS: Technical regulations take many forms. Health and sanitary regulations, for example, are designed to prevent the importation of products containing insects, chemical residues, contaminants or diseases that might threaten domestic production or the health of consumers. Administrative regulations can limit imports by slowing the import process or creating high administrative costs for importers. Though such regulations are necessary, they are sometimes used as trade barriers.

Compulsory mixing regulations (also known as domestic content requirements) often reduce the proportion of imports that can be used, thereby preserving a larger market share for the domestically produced commodity. For example, the European Community has sometimes required feed manufacturers to include surplus milk powder produced in the EC as a protein supplement in livestock rations, reducing the use of imported soybean meal (Robinson).

Health and sanitary regulations often are needed to protect animal, plant and human health, but they sometimes are improperly used to reduce imports and increase domestic price.

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STATE TRADING COMPANIES: In some countries, government-sanctioned trading companies or marketing boards are granted a monopoly over the trading and internal distribution of certain commodities. Examples of such agencies include the Canadian and Australian wheat boards and CONASUPO, the Mexican commodity board responsible for marketing corn and dry beans. In many cases, these bodies are responsible for establishing domestic prices and controlling imports. Marketing boards are also used by many developing countries. If these agencies are granted the right to limit imports, they can impose trade barriers that reduce imports and increase domestic prices.

All trade barriers affect both consumers and producers. Import restrictions make consumers pay higher prices for the restricted commodity, while domestic producers gain from the higher prices.

Import barriers increase the price in the importing country, thereby increasing the price received by domestic producers and the price paid by consumers. This higher price stimulates domestic production and reduces consumer demand. The combined effect is a decrease in the quantity imported and a move towards greater self-sufficiency. Several countries use a combination of price support programs and import restrictions to stimulate domestic production.

Export Subsidies

Commodity price support programs are designed to increase the prices of farm products, but these programs can also make domestic commodities more expensive in international markets. To prevent the loss of export markets, countries sometimes combine price support programs with export subsidies to remain competitive in international markets. In this case, a government subsidy is paid to exporters for each unit exported. The exporter can then sell the product at a price below the domestic support level and collect the subsidy payment from the government. Such a program can be used to dispose of surpluses, expand market share or retaliate against subsidies used by other exporters.

Export subsidies are given to exporters for each unit of a product exported. The exporter can sell the product at a price below the domestic price and collect the subsidy payment from the government.

The European Community makes the most extensive use of export subsidies on agricultural commodities. Because its domestic support prices are higher than the world price for most commodities, virtually all EC products require export subsidies (called restitution payments) to compete on world markets. The value of these restitutions often equals or exceeds the world market price of the commodity being exported.

The European Community makes the most extensive use of export subsidies.

The United States maintains various export subsidy programs, including the use of PL-480 (Food for Peace) concessional sales to developing countries and credit guarantees designed to promote exports of U.S. products. Under the Export Enhancement Program (EEP), the United States provides a direct subsidy to foreign buyers in selected markets. This program is frequently used to retaliate against the export subsidies used by the European Community. By reducing the domestic price in the United States, the target price program can also act as an indirect export subsidy.

The United States maintains various export subsidy programs, including the use of PL-480 concessional sales to developing countries, credit guarantees and direct export subsidies under the Export Enhancement Program.

The United States also maintains programs that use traditional market development methods to expand export markets for U.S. agricultural products. The Foreign Agricultural Service (FAS) supports export promotion programs through its agricultural attachés stationed at embassies throughout the world. Their objective is to open new markets for U.S. agricultural products through trade shows and other promotional activities.

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Reducing the Level and Cost of Trade Barriers

Trade barriers exist in nearly every country, and agricultural trade barriers are at the center of some of the most difficult and controversial trade policy disputes that exist among nations today. The following chapters will examine the process used to resolve these disputes, reduce trade barriers and expand the opportunities for increased world trade.

Chapter III

THE U.S. ROLE IN INTERNATIONAL TRADE NEGOTIATIONS

Issues to consider

- What is the General Agreement on Tariffs and Trade (GATT)?
- What trade policy issues are addressed by the GATT?
- Has U.S. agriculture benefited from the GATT process?
- What is the current status of the GATT negotiations?

Agricultural trade issues are at the center of many international trade policy disputes. If these disputes are to be resolved and the gains from trade realized, nations must have a forum in which the rules of the international trading system can be negotiated and enforced. The General Agreement on Tariffs and Trade (GATT) provides such a forum. Though these multinational trade negotiations have had limited success in removing agricultural trade barriers in the past, agricultural issues are increasingly important to the success of these negotiations.

Agricultural trade issues are at the center of many international trade policy disputes.

The Movement Toward Trade Liberalization

During the global depression of the 1930s, most countries attempted to protect domestic industries from international competition. The Agricultural Adjustment Act of 1933 was one such attempt. This legislation established price support programs, provided subsidies for U.S. agricultural exports, and authorized the president to impose tariffs or quotas if imports threatened domestic commodity programs.

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At the same time that these domestic agricultural policy changes were taking place, the United States was also reducing trade barriers in other industries with the passage of the Reciprocal Trade Agreements Act of 1934. By permitting the negotiation of bilateral trade agreements and emphasizing the need to expand international markets for U.S. industrial products, this legislation began a slow process of reversing the trend toward higher tariffs (Ryan and Tontz). As a result of this process, the average tariff on U.S. imports declined

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from 59 percent in 1932 to 25 percent by the end of World War II (Krugman and Obstfeld). Though this framework remained in place until 1945, the difficulties of negotiating trade agreements on a country-by-country basis eventually led to the establishment of an organization capable of negotiating comprehensive trade agreements on a worldwide basis.

The post-World War II period has been marked by the widespread use of trade barriers in international agricultural markets. The increasing use of such policies has led to a high level of political tension over trade-related disputes and intensified efforts to establish greater coordination through negotiated trading arrangements.

What is the GATT?

The primary purpose of the GATT is to promote economic growth by reducing trade barriers. It provides guidelines for trade policy formation, a forum for multilateral trade negotiations and a forum for settling trade disputes among members.

Instituted by 23 signatory nations in 1947, the General Agreement on Tariffs and Trade (GATT) had 103 member nations in 1992. Its primary purpose is to promote economic growth by reducing trade barriers. To accomplish this objective, the agreement provides guidelines for trade policy formation, a forum for multilateral trade negotiations and a forum for settling trade disputes among members.

The General Agreement on Tariffs and Trade is a comprehensive document based on a few fundamental principles. These include:

The GATT requires all tariffs to be applied equally to all members. Tariff reductions are negotiated by requiring each GATT member to reduce tariffs in exchange for tariff reductions by other members.

- Trade policies must be implemented without discrimination, and tariffs negotiated through GATT must apply equally to all GATT members (the "most favored nation" principle).
- Protection must be provided through tariffs rather than quotas, and export subsidies are prohibited. Agriculture is exempt from these provisions.
- Tariff reductions are negotiated by requiring each nation to reduce its tariffs in exchange for tariff reductions by other nations (the "reciprocity" principle).
- Trade disputes are resolved through the GATT resolution process. Any country whose trade policy violates GATT rules must cease the disputed practice or face the use of retaliatory tariffs by the damaged country.

The rules of GATT prohibit the use of import quotas and export subsidies in most industries but permit the use of these policies in agricultural trade.

Though the United States supported greater trade liberalization through the GATT, it also insisted that the GATT provide exemptions to protect U.S. farm price support programs. The use of import quotas and export subsidies is permitted under the rules of the GATT and

these continue to be applied to agriculture. These exemptions applied to commodities for which the United States maintained price support programs or supply controls and which required import protection to protect the viability of these programs.

Eight rounds of GATT negotiations have been conducted since 1947. Agriculture was not included in the first four rounds and was included only peripherally in the fifth round. Efforts were made to include agriculture in the Kennedy round of the 1960s, but no major progress was achieved.

Agriculture was not included in the first four rounds of GATT negotiations. The Tokyo round of the 1970s was the first to include agriculture in the general multilateral framework.

The Tokyo round of the 1970s was the first to include agriculture in the general multilateral framework. The major bargaining issues in this round included the reduction of trade barriers and trade subsidies, the establishment of international commodity agreements for agricultural commodities and the provision of preferential treatment for developing countries.

Problems in Negotiating Agricultural Trade Policy

National trade policies for industrial products have tended to conform to GATT rules, but trade barriers on agricultural products have proven difficult to reduce. Since its inception, the GATT's rules have accommodated national agricultural programs by exempting agriculture from the major principles of the GATT. As a result, many nations have developed agricultural trade policies to fit domestic policy priorities rather than developing domestic farm programs to fit the rules of international trade. This has often created trade policy disputes resulting from divergent national policy objectives.

National trade policies for industrial products have tended to conform to GATT rules, but trade barriers on agricultural products have proven difficult to reduce.

Two problems have plagued most multilateral negotiations on agricultural trade issues. The first problem, which exists for all traded goods, is the difficulty of reaching agreement among the large number of GATT participants, all of whom must be responsive to particular national interests. The greater the number of participants, the more diverse will be the economies of the member nations and the greater will be the number of issues negotiated. As a result, the difficulty of reaching an agreement satisfactory to all members increases rapidly as the number of participants grows. Evidence of this problem is seen in the increasing length of the negotiations as more countries participated in each successive round. The first round of GATT negotiations was completed in less than one year, while the Tokyo round required four years to complete and the Uruguay round, started in 1986, has not yet been completed (Tweeten).

The difficulty of reaching an agreement satisfactory to all members increases rapidly as the number of participants grows.

The second problem is the special nature of agriculture. Food is necessary to sustain life, and governments have historically seen the assurance of adequate food supplies as an important policy objective. Many governments also protect domestic agricultural markets from international competition as a means of maintaining the incomes of farmers. As a result, international agricultural markets have been subject to a wide range of interventions that affect the flow of goods. Conflicts between the national goals of income protection for farmers, food security and food safety for consumers and the international goal of trade liberalization have prevented significant progress in agricultural trade negotiations.

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Despite the exemptions on quotas and trade subsidies that have limited GATT's success in reducing trade barriers on agricultural products, it can still be argued that agriculture has benefited from the GATT trade liberalization process. Just as the protectionism of the 1920s and 1930s may have exacerbated the depression, the liberalization of industrial trade in the postwar era has enhanced economic growth. The reduction of trade barriers for industrial products has led to greater income growth in many nations, increased the demand for agricultural products and fueled the growth in exports of American farm products. In addition, the dispute settlement mechanism provided by the GATT has helped to avert trade wars that could have resulted from disputes over agricultural policies.

The reduction of trade barriers for industrial products has led to greater income growth in many nations, increased the demand for agricultural products and fueled the growth in exports of American farm products.

Trade Disputes Involving the United States

Most industrial countries protect their agricultural sectors with import quotas, export subsidies or other measures that differ from the principles applied by the GATT to other industries. Consequently, there is continuing conflict among GATT nations over agricultural trade issues. Though the GATT provides a mechanism for arbitrating trade disputes, the success of this process has been limited by the GATT's agricultural exemptions.

Most of these disputes have involved the use of export subsidies to dispose of surplus production and to protect market shares in international markets. The frequency of these disputes has also increased since the formation of the European Community. Subsidy cases involving the United States and the European Community included eggs (1957), flour (1958 and 1981), barley (1977), sugar (1958 and 1982),

The frequency of these disputes has also increased since the formation of the European Community. Subsidy cases involving the United States and the European Community included eggs (1957), flour (1958 and 1981), barley (1977), sugar (1958 and 1982), pasta (1982) and oilseeds (1992).

pasta (1982) and oilseeds (1992). In 1982, for example, the United States charged that EC export subsidies on pasta were illegal because pasta is not a primary product covered by the GATT exemptions for agricultural products. In another case, the United States charged that EC production subsidies paid to processors of canned fruit impaired past tariff concessions granted by the EC on imported fruit (Hathaway).

The original GATT provisions did not explicitly prohibit domestic or export subsidies for agricultural products. The agreement does recognize that subsidies may cause undue disturbances to the commercial interests of other countries and admonishes countries to avoid using subsidies. It also states that a country using export subsidies to increase its agricultural exports should not use such subsidies to increase its share of the world market beyond an equitable level (defined as that country's share in a recent comparable period). This is obviously an ambiguous guideline and has not prevented countries from using export subsidies. The United States sought more meaningful restrictions on the use of subsidies during the Tokyo round of the 1970s but could not obtain such an agreement.

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Quantitative restrictions are another area of contention in GATT negotiations. Many developing countries are opposed to the GATT's exemptions that permit developed countries to impose quantitative restrictions on agricultural commodities that developing countries can produce at lower cost. Developing countries believe that the GATT's exemptions protecting agricultural products in industrial countries, combined with its prohibition of the use of quantitative restrictions to protect manufacturing industries in developing countries, have harmed their economies and slowed economic growth among the developing nations of the world.

Many developing countries are opposed to the GATT's exemptions that permit developed countries to impose quantitative restrictions on agricultural commodities that developing countries can produce at lower cost.

The GATT also does not deal effectively with trade restrictions created by state trading agencies. As a result, some governments control imports or exports by creating trading agencies with a monopoly in trade. It is estimated that 90 percent of wheat trade and 70 percent of coarse grain trade passes through state trading agencies (Hathaway). For example, Japanese trade in wheat is controlled by a state trading agency. Canada, Australia and New Zealand have used marketing boards to export commodities and maintain a two-tier pricing policy of high internal prices and low export prices.

The GATT also does not deal effectively with trade restrictions created by state trading agencies.

What is the Current Status of the GATT Negotiations?

Negotiations are continuing on the Uruguay round of GATT negotiations. These negotiations were to focus on agriculture, textiles, intellectual property, service industries and the strengthening of GATT's dispute resolution mechanisms. The original U.S. proposal to the Uruguay round called for the elimination of all trade barriers, export subsidies and domestic programs that significantly distort agricultural trade. The United States was supported in this position by a group of fourteen exporting nations, which met in Cairns, Australia, to develop a joint strategy for eliminating agricultural policies that distort trade.

The original U.S. proposal to the Uruguay round called for the elimination of all trade barriers, export subsidies and domestic programs that significantly distort agricultural trade.

The United States proposed that these changes be made on the basis of an aggregate measure of agricultural protection (the Producer Subsidy Equivalent, or PSE), with each country choosing its own path to the elimination of disruptive domestic programs and trade barriers within a specified time period. This approach proved unacceptable, particularly to the members of the European Community, and was followed by negotiations on specific policy issues, including the conversion of all non-tariff barriers into tariffs, the elimination of export subsidies, and the classification of domestic policies into those that do and those that do not create trade distortions (Buckley). Policies that create trade distortions would then be eliminated over a specified period of time, while non-distorting policies could be retained.

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Prospects for Future Progress in Reducing Trade Barriers in Agriculture

Reductions in agricultural trade barriers have proven difficult to achieve through the multilateral trade negotiation process. In part, this reflects the conviction by some countries that the consequences of any reduction in trade barriers are immediate and, given the inherent problems in agriculture, are not an acceptable means of solving trade policy conflicts. Few countries have been willing to accept these consequences for the high cost components of their agricultural sector.

Given the limited success at negotiating multilateral trade agreements, some nations are now turning to the formation of regional trade agreements, or trading blocs, as an alternative method of gaining the economic benefits from trade. The next chapter will examine U.S. trade relations with Canada and Mexico and the prospects for the formation of a free trade area among the nations of North America.

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Chapter IV

TRADING WITH OUR NEIGHBORS

Issues to consider

- What agricultural products are traded among the United States, Canada and Mexico?
- What is the North American Free Trade Agreement (NAFTA)?
- What is the potential impact of the NAFTA on agricultural trade?

While the GATT is designed to provide multilateral reductions in trade barriers, many nations are also pursuing regional trade agreements designed to reduce trade barriers among a limited number of trading partners. One example of such a regional agreement is the proposed North American Free Trade Agreement negotiated by the United States, Canada and Mexico. This chapter examines the existing agricultural trade patterns among these countries, the provisions of this agreement that could affect agricultural trade, and the potential impact of this agreement on agricultural trade between the United States and its neighbors.

While the GATT is designed to provide multilateral reductions in trade barriers, many nations are also pursuing regional trade agreements designed to reduce trade barriers among a limited number of trading partners.

The Magnitude of U.S. Agricultural Trade with Canada and Mexico

The economies of the United States, Canada and Mexico are interdependent. Canada is the second largest market for U.S. agricultural exports, and Mexico is the third largest buyer of U.S. farm products. During the 1980s, the annual value of U.S. agricultural exports to Mexico averaged $1.9 billion (constituting 80 percent of Mexico's total agricultural imports). The United States shipped an average of $1.8 billion of agricultural exports to Canada during the 1980s, representing 55 to 60 percent of total Canadian agricultural imports.

Canada is the second largest market for U.S. agricultural exports, and Mexico is the third largest buyer of U.S. farm products.

The United States also imports agricultural products from its neighbors. During the 1980s, the annual average value of U.S. imports from Mexico and Canada was $1.7 billion and $1.8 billion, respectively. The United States purchased nearly 36 percent of total Canadian agricultural exports in 1990 and nearly 90 percent of all Mexican agricultural exports. Canada is the largest supplier of U.S. agricultural imports, and Mexico is the second largest source of U.S. imports.

Figure 1. U.S. agricultural trade with Canada and Mexico, 1991.

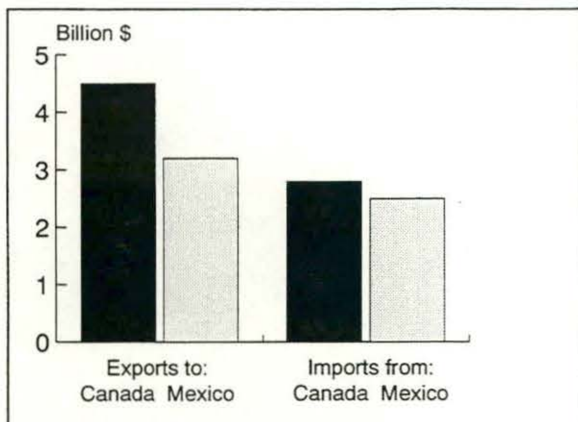


Figure 2. U.S. agricultural exports to Canada, 1985-1991.

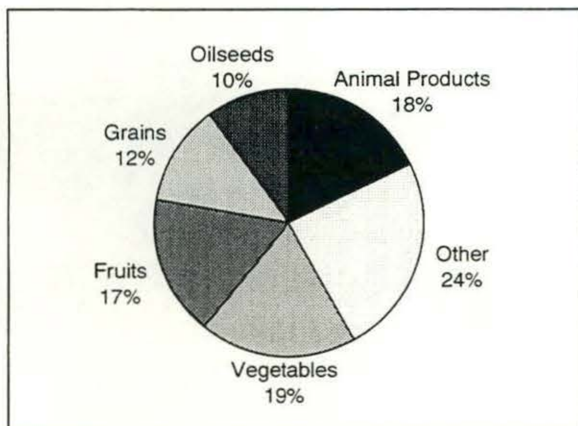
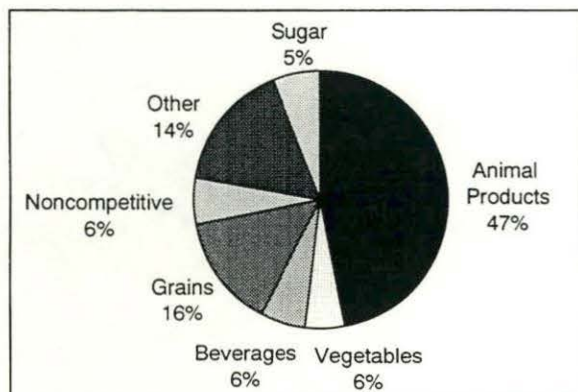


Figure 3. U.S. agricultural imports from Canada, 1985-1991.



U.S. agricultural exports to Canada reached $4.5 billion in 1991, while U.S. imports from Canada totalled $3.2 billion. U.S. agricultural exports to Mexico were nearly $3 billion in 1991, while U.S. imports from Mexico were $2.5 billion (Figure 1). Many of the agricultural commodities traded between the United States and its neighbors are also produced domestically in each country. Consequently, the importation of commodities that compete with domestic production and the impact of trade liberalization in North America are important issues in all three countries.

The Composition of U.S. Agricultural Trade with Canada

Vegetables were the largest category of U.S. exports to Canada (19 percent of total exports), followed by animal products (18 percent), fruits (17 percent), grains (12 percent) and oilseeds (10 percent) (Figure 2). Canadian exports to the United States included animal products (47 percent of total exports), followed by grains (16 percent), vegetables (6 percent), beverages (6 percent), sugar (4 percent) and non-competitive products (6 percent) (Figure 3).

The Canadian government intervenes heavily in agricultural production and trade. Like the United States, Canada provides production subsidies and price supports to its farmers, restricts access to some of its markets and provides export assistance for some products. The Canadian wheat marketing board attempts to stabilize wheat prices and provides rail subsidies for shipments of grains. Canada also has tariffs and quotas on a wide range of agricultural products.

The Composition of U.S. Agricultural Trade with Mexico

Animal products represented the largest share of U.S. agricultural exports to Mexico in recent years (32 percent of total exports), followed by grains (30 percent) and oilseeds (21 percent) (Figure 4). U.S. imports from Mexico consisted of vegetables (34 percent of total imports), coffee and other non-competitive tropical products (22 percent), animal products (15 percent), fruits (10 percent) and sugar (2 percent) (Figure 5).

Both the United States and Mexico limit imports of some commodities through a combination of tariffs, quotas and technical regulations. Fruits and vegetables imported into the United States are limited by seasonal tariffs designed to protect U.S. domestic production. Sugar trade is subject to a quota that limits the quantity of sugar that

Mexico can export to the United States. Mexico limits imports of fruits and vegetables through non-seasonal tariffs (usually of 20 percent) and uses import licenses to limit imports of dry beans, potatoes, corn and some livestock products.

The U.S.-Canada Free Trade Agreement

A free trade agreement between the United States and Canada took effect in 1989. This agreement reduced trade restrictions between the two nations, developed dispute settlement mechanisms to resolve trade policy issues and ensures each country continued access to the other's market. A 10-year transition period removes tariffs gradually for some sensitive commodities, allowing more time for producers to adjust to changes in prices caused by removal of these tariffs. Under certain conditions, a temporary "snapback" tariff can be applied to prevent excessive damage from imports. Key provisions of the agreement are summarized in appendix IV-A. Since the inception of the agreement in 1989, there has been a large and continuing increase in total U.S. agricultural trade with Canada (Figure 6). Other significant changes completed since the beginning of this agreement include:

- A 30 to 60 percent reduction of tariffs for some products and the complete removal of tariffs for others.
- Removal of the Canadian import license requirement on oats, wheat and wheat products.
- Changes in the Canadian Wheat Board's two-price system, with wheat support prices now being comparable to U.S. support prices.
- An increase in Canada's global import quotas on poultry products, giving U.S. producers greater access to the Canadian market.

Trade Liberalization in Mexico

During the 1940s, Mexico established a policy of stringent protection measures for its agricultural and manufacturing industries. This policy sought to promote economic growth and industrialization through development of its internal markets while minimizing dependence on foreign capital and imports. Foreign investment was tightly regulated. Imports were restricted through a combination of import licensing and high import tariffs (up to 100 percent for some com-

Figure 4. U.S. agricultural exports to Mexico, 1985-1991.

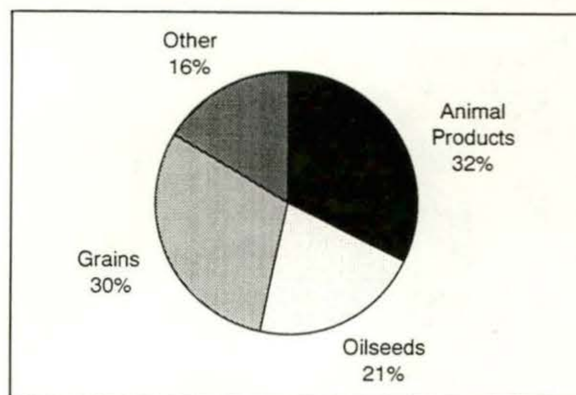


Figure 5. U.S. agricultural imports from Mexico, 1985-1991.

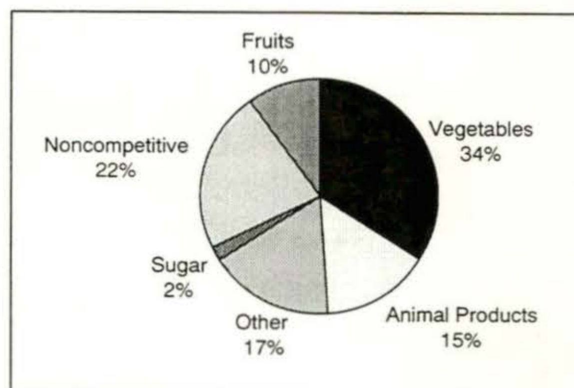
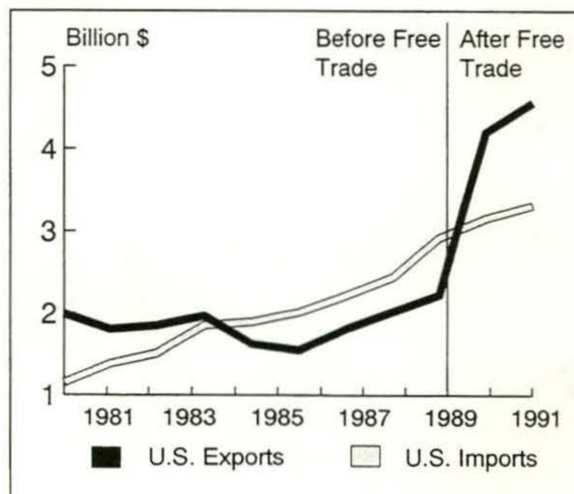


Figure 6. U.S. - Canadian agricultural trade, 1981-1991.



During the 1940s, Mexico established a policy of stringent protection measures for its agricultural and manufacturing industries.

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The NAFTA would create the largest trading bloc in the world, totalling 360 million people with nearly $7 trillion of economic output.

Mexico's interest in the NAFTA includes ensuring access to U.S. markets and attracting international investment.

modities), and domestic commodity markets were regulated by government agencies such as CONASUPO.

The situation changed significantly in 1982 as Mexico faced a foreign exchange crisis created by its inability to meet its foreign debt obligations. In response to this crisis, Mexico began to liberalize its economy and open its markets to international trade and investment. In 1986, the Mexican government reduced most tariff levels to about 20 percent, eliminated the use of import licenses on many products and joined the GATT.

As a result of these changes, the Mexican economy has become more open, and income growth in Mexico has increased significantly in recent years. Before a free trade agreement was conceived, Mexico had begun to liberalize its internal markets and reduce its trade barriers with the United States and other trading partners. These changes in economic policy set the stage for Mexico's participation in the North American Free Trade Agreement.

What is the North American Free Trade Agreement?

In 1990, the U.S. Congress authorized negotiations with Mexico on a free trade agreement. Shortly thereafter, the Canadian government expressed interest in such an agreement, and negotiations began on the North American Free Trade Agreement (NAFTA). The NAFTA would create the largest trading bloc in the world, totalling 360 million people with nearly $7 trillion of economic output.

Mexican Interest in the NAFTA

Mexico's interest in the NAFTA centers around several issues. First, Mexico is seeking greater access to U.S. markets and assurances of continued access. Second, Mexico wants to encourage increased external investment in the Mexican economy. By establishing a more open economy and participating in the NAFTA, the Mexican government would assure investors that the trade liberalization and market reforms of the past decade will not be reversed. Third, the NAFTA is also expected to improve income growth and mitigate inflation in Mexico. Some opposition to the NAFTA exists in Mexico because of concerns that the NAFTA, combined with internal land reform policies in Mexico, would cause displacement of small Mexican ejido farmers who have been guaranteed access to land under Mexican law.

U.S. Interest in the NAFTA

The United States is interested in the NAFTA for several reasons. First, the United States expects to increase its exports to Mexico if trade barriers are reduced. Nearly 65 percent of Mexico's total imports come from the United States. The United States hopes that increased income levels in Mexico, combined with a reduction in Mexico's trade barriers, will increase Mexico's imports of agricultural and industrial products. Second, there is a strong desire to decrease emigration from Mexico into the United States. It is argued that emigration from Mexico to the United States will be reduced if the NAFTA stimulates income and employment growth in Mexico. Third, the United States wants to secure access to investment in Mexico. A key element of a NAFTA is that it would give some U.S. industries greater access to less expensive Mexican labor. This, in turn, would improve some firms' ability to compete in international markets (U.S. International Trade Commission). Opponents of the NAFTA fear job losses in the United States as companies relocate to Mexico in pursuit of lower labor costs or less stringent environmental regulations.

U.S. interests in the NAFTA include increased U.S. exports to Mexico, increased investment in Mexico and the reduction of Mexican emigration to the United States.

Canadian Interest in the NAFTA

Because the volume of trade between Mexico and Canada is very small and the direct impact on Canadian-Mexican trade is expected to be limited, the Canadian interest in the NAFTA is primarily defensive. Canada's largest trading partner is the United States, and Canada's major objective is to maintain gains created by the U.S.-Canada Free Trade Agreement and to assure that its access to the U.S. market is similar to the access granted to Mexico. The inclusion of Canada in the agreement could lead to expanded trade of some agricultural commodities. The NAFTA is expected to expand Canadian exports of grains, oilseeds and red meat to Mexico. Canadian imports of horticultural products from Mexico would likely increase (Cook, et al.).

The Canadian interest in a NAFTA is primarily defensive. Trade between Mexico and Canada is very small.

The Agricultural Provisions of the North American Free Trade Agreement

The North American Free Trade Agreement was signed by the American, Canadian and Mexican heads of state in 1992. This agreement is comprehensive, covering most trade among the three nations. An effort was made to ensure that the provisions of the NAFTA comply with GATT guidelines. The agreement now must be ratified by all

The NAFTA is a comprehensive agreement, covering most trade among the three nations.

three nations. The major agricultural provisions of the agreement are presented in appendix IV-B.

The NAFTA will remove all quotas and import licenses on agricultural products. These non-tariff barriers will be replaced with tariffs or tariff rate quotas. A tariff rate quota specifies the quantity of a commodity that is permitted to enter the importing country on a duty-free basis. Any imports exceeding the quota will be assessed an "overquota" tariff. The quota amount will increase 3 percent per year, and the overquota tariff will be reduced each year, resulting in the removal of both the quota and the tariff at the end of the transition period. Tariff rate quotas will be used only for those commodities facing the greatest adjustment.

A tariff rate quota specifies the quantity of a commodity that is allowed to enter the importing country on a duty-free basis. All additional imports will be assessed a tariff.

Key Factors Determining the Impact of the NAFTA on Agricultural Trade

Because the NAFTA has not yet been implemented, studies can only examine its potential impact on agricultural trade. Such estimates reflect assumptions about the impact of the NAFTA on the growth of Mexican incomes, production costs in each country and the nature of existing trade barriers.

The growth of Mexican income resulting from the NAFTA and Mexico's domestic economic reforms will be a major determinant of U.S. agricultural exports to Mexico.

Demand for U.S. Products: The growth of Mexican income resulting from the NAFTA and Mexico's domestic economic reforms will be a major determinant of U.S. agricultural exports to Mexico. Faster income growth in Mexico will increase demand for U.S. products.

Labor-intensive Products: Wages for unskilled laborers are much lower in Mexico than in the United States. Though the production of some labor-intensive horticultural products may shift to Mexico, much of Mexico's horticultural production is consumed in Mexico. Nearly 80 percent of Mexico's horticultural production is sold to meet its domestic demand, and demand for these products is expected to increase as Mexico's population and income continue to grow (Cook, et al.). Mexico's advantage through low wages is also constrained by limited availability of land suitable for expanded production.

Though the production of some labor-intensive horticultural products may shift to Mexico in response to Mexico's lower wages for unskilled labor, Mexico's demand for these products is expected to increase as its population and income continue to grow.

Infrastructure: Though Mexico may enjoy a cost advantage due to less expensive labor, Mexican transportation systems and other infrastructure elements are not as well developed as those in the United States and Canada. This suggests that even if it is cheaper for Mexican producers to plant and harvest a crop, high marketing costs may make Mexico less competitive with U.S. production.

Though Mexico may enjoy a cost advantage due to less expensive labor, Mexican transportation systems and other infrastructure elements are not as well developed as those in the U.S. and Canada, so Mexican marketing costs are higher.

Technical and Health Standards: As discussed in Chapter II, health and technical standards designed to protect consumers can sometimes act as trade barriers. Maintaining legitimate consumer safety protection while avoiding the creation of trade barriers could prove to be one of the most difficult issues encountered in the implementation of the NAFTA. The United States and Mexico have different standards for pesticide regulation, although there has been increased harmonization of these standards in recent years (Newman). Such harmonization would reduce the uncertainty faced by U.S. exporters, who currently encounter unexpected changes in Mexican regulatory policies. An example of such uncertainty was Mexico's temporary suspension of soybean meal imports during the Mexican soybean harvest, allegedly because inspections were needed for aflatoxin, mycotoxin and pesticide residues in the shipments (U.S. General Accounting Office). The United States and Mexico have developed regulations to limit disease and pest transmission through commodity trade. Some U.S. marketing orders include grade or quality standards. Imports must continue to meet these requirements under the NAFTA.

There has been increased harmonization of U.S. and Mexican standards for pesticide regulation in recent years.

Some U.S. marketing orders include grade or quality standards. Imports must continue to meet these requirements under the NAFTA.

THE POTENTIAL IMPACT OF THE NAFTA ON AGRICULTURAL TRADE

The impact of the NAFTA on specific industries will depend on a number of factors, including the success of Mexico's internal reforms in agriculture, the growth of income in Mexico, improvements in the infrastructure and distribution systems in Mexico, the extent of competition between the United States and Canada, exchange rates among the members of the NAFTA and the outcome of the current Uruguay round of GATT negotiations. The following sections summarize the results of recent studies on the impact of NAFTA on selected agricultural commodities.

Grains and Oilseeds: Mexico uses import licenses to control imports of corn and wheat from the United States. Under the terms of the NAFTA, Mexico would eliminate its import licenses on wheat immediately and would eliminate its 15 percent tariff on wheat over a 10-year period. Mexico would also replace its import licenses for corn with a tariff rate quota. The United States would be permitted to ship 2.5 million tons of corn to Mexico during the first year of the agreement on a duty-free basis. All additional U.S. shipments of corn would be assessed a tariff of 215 percent. This tariff rate quota would

Mexico uses import licenses to control imports of corn and wheat from the United States. Most studies have concluded that U.S. exports of grains and oilseeds to Mexico will increase if the NAFTA is approved.

be eliminated over a 15-year transition period. Mexico would eliminate its 10 percent tariff on soybeans over a 10-year period. Most studies have concluded that U.S. exports of grains and oilseeds to Mexico would increase if the NAFTA is approved.

Mexico uses a combination of import licenses and tariffs to limit imports of U.S. pork and poultry products. Most studies suggest that U.S. exports of pork and poultry products to Mexico will increase if the NAFTA is approved.

Livestock and Meat Products: Mexico uses a combination of import licenses and tariffs to limit imports of U.S. pork and poultry products. Under the terms of the NAFTA, Mexico would eliminate its 10 percent tariff on breeding hogs immediately and would eliminate its tariff rate quota and 20 percent tariff on slaughter hogs over a 10-year period. Mexico would also eliminate its tariff rate quotas on processed pork products over a 10-year period. Mexico would eliminate its import licenses on live chickens and its tariffs on chickens, ranging from 10 to 50 percent, over a 10-year period. Mexico would also eliminate its 15 percent tariff on live cattle and its 20 to 25 percent tariff on processed beef immediately. U.S. tariffs on most live animal and meat products are less than 5 percent and would be eliminated immediately. Most studies suggest that U.S. exports of livestock and meat products to Mexico would increase under the NAFTA. Exports of poultry products to Canada have already increased since the implementation of the U.S.-Canada Free Trade Agreement.

The U.S. will convert its existing import quotas on dairy products into tariff rate quotas. Mexico must also convert its import licenses on dairy products into a tariff rate quota system. Most studies have concluded that U.S. exports of dairy products will increase under the NAFTA.

Dairy: Both Mexico and the United States use quantitative barriers to limit trade in processed dairy products. Under the terms of the NAFTA, the United States would convert its existing import quotas on dairy products into tariff rate quotas. During the first year of the NAFTA, Mexico would be permitted to ship 422 tons of nonfat dry milk to the United States on a duty-free basis. All additional Mexican shipments to the United States will be assessed tariffs ranging from 78 percent to 83 percent. Mexico would also be permitted to ship 5,550 tons of cheese to the United States on a duty-free basis during the first year of the NAFTA, with all additional cheese shipments being assessed a tariff of 69.5 percent. These tariff rate quotas would be eliminated over a 10-year period.

Mexico must also convert its import licenses on dairy products into a tariff rate quota system. The United States would be permitted to ship 40,000 tons of nonfat dry milk to Mexico on a duty-free basis during the first year, with all additional shipments being assessed a tariff of 139 percent. This tariff rate quota would then be eliminated over a 15-year period. Mexico would also eliminate its import licens-

es for cheese and would eliminate its 20 percent tariff on cheese imports over a 10-year period. Most studies have concluded that U.S. exports of dairy products would increase under the NAFTA.

Fruits and Vegetables: Both the United States and Mexico use tariffs to limit imports of fruits and vegetables. Most of these tariffs vary throughout the year, with higher tariffs being applied during the months when Mexican production competes most directly with U.S. production in California, Texas and Florida. U.S. tariffs on fresh vegetables are among the highest charged on any agricultural imports, with tariffs of 8.3 percent on onions, 8.3 to 19.9 percent on cucumbers, 2.5 to 8.5 percent on tomatoes, 5.5 to 12.5 percent on cauliflower and broccoli, and 25 percent on fresh asparagus. Some of the higher tariffs will be eliminated over 15 years; the lower tariffs and those tariffs applied during the off-season will be eliminated in 10 years or less. Mexican tariffs are 8.3 percent on onions, 10 percent on asparagus, 2.5 to 8.5 percent on tomatoes and 10 percent on cucumbers. Most of these tariffs will be eliminated over 10 years or less. The United States would also use tariff rate quotas to limit the quantities of tomatoes and onions that may enter at the reduced tariff.

Most studies suggest that the removal of these tariffs would increase U.S. imports of fresh vegetables from Mexico. The magnitude of this increase and the impact on producer prices in the United States would be determined by the length of the transition period for removal of the tariff and the difference between the cost of production in the United States and Mexico. Potatoes could be an exception to this conclusion. The United States has a 1 percent tariff on potatoes that would be eliminated immediately. Mexico has used import licenses to limit potato imports from the United States and would be required to convert this system into a tariff rate quota. The United States could ship 15,000 tons of potatoes to Mexico on a duty-free basis, and a tariff of 272 percent would be applied to all additional shipments. This tariff rate quota would be eliminated in 15 years.

Most U.S. tariffs on fruits are very low. The U.S. charges no tariffs on imports of apples or cherries, a 0.6 percent tariff on peaches, zero or 0.5 percent on grapes, zero or 0.5 percent on plums and 1.5 percent on strawberries. Tariffs on most types of nuts are 5 percent or less. Mexico applies tariffs of 20 percent on cherries, peaches and apples, 15 percent on plums and pears, and 20 percent on strawberries

Both the United States and Mexico use tariffs to limit imports of fruits and vegetables. Most studies suggest that the removal of these tariffs will increase U.S. imports of fresh vegetables from Mexico.

Most tariffs on vegetables would be eliminated over 10 years or less. The United States would also use tariff rate quotas to limit the quantities of tomatoes and onions that may enter at the reduced tariff.

Mexico has used import licenses to limit potato imports from the United States and would be required to convert this system into a tariff rate quota. The removal of these licenses could increase U.S. exports of potatoes to Mexico.

Most U.S. tariffs on fruits are very low, while Mexico applies tariffs of 15 to 20 percent on most fruits. Several studies suggest that U.S. exports of fruits, particularly tree fruits, will increase if the NAFTA is implemented.

and most tree nuts. Most U.S. tariffs would be eliminated immediately, while most of Mexico's tariffs would be phased out over 5 years or less. Because Mexico has imposed strict limits on apple imports in the past, a tariff rate quota would permit the United States to ship 55,000 tons of apples to Mexico at a reduced tariff. All shipments in excess of this amount would be assessed a tariff of 20 percent. This tariff rate quota would be eliminated over a 10-year period. Most studies suggest that U.S. exports of fruits, particularly tree fruits, will increase if the NAFTA is implemented.

Mexico has used import licenses to limit dry bean imports, while the United States applies tariffs of 4.1 to 8.9 percent on dry beans. Most studies have concluded that U.S. exports of dry beans will increase if the NAFTA is implemented.

Dry Beans: Mexico has used import licenses to limit dry bean imports, and the United States applies tariffs of 4.1 to 8.9 percent on dry beans. Under the terms of the NAFTA, Mexico would convert its import licenses to a tariff rate quota. The U.S. would be permitted to ship 50,000 tons of dry beans to Mexico during the first year of the agreement, with a tariff of 139 percent being applied to all shipments above this amount. This tariff rate quota would be eliminated over a 15-year period. The United States would remove its tariffs on dry beans immediately.

Most studies have concluded that U.S. exports of dry beans will increase if the NAFTA is implemented. Michigan is a leading producer of several types of dry beans, including black turtle beans (a popular variety in Mexico), and a significant share of Michigan's bean exports has been shipped to Mexico in recent years.

Both the United States and Mexico use trade barriers to limit sugar imports. Mexico is now a net importer of sugar, but Mexico's status could be affected by the conversion of the Mexican soft drink industry to corn sweeteners, the privatization of the Mexican sugar processing industry and income growth in Mexico.

Sugar: Both the United States and Mexico use trade barriers to limit sugar imports. Mexico uses a variable levy system to maintain a domestic sugar price of 18.7 cents per pound at the farm level. The United States uses a tariff rate quota to limit imports. Import quotas are assigned to each sugar exporter, and all shipments above this quota are assessed a tariff of 16 cents per pound. Mexico is permitted to ship 7,258 tons of sugar to the United States under this system.

Under the terms of the NAFTA, Mexico would be permitted to ship 25,000 tons of sugar to the United States on a duty-free basis each year during the first 6 years of the agreement. Beginning in year 7, Mexico would be permitted to ship 250,000 tons of sugar to the United States on a duty-free basis, if its sugar production is greater than its consumption.. The U.S. tariff on sugar imports from Mexico would be eliminated by year 15 of the agreement, and Mexico's tariff on sugar imports from the United States would also be phased out by year 15.

The impact of the NAFTA on sugar trade depends on several factors. Mexico is now a net importer of sugar and does not meet the requirements specified by the NAFTA to increase its sugar exports to the United States. Several factors could affect Mexico's export status. First, the Mexican soft drink industry uses only sugar as a sweetener. If this industry should switch to the use of corn sweeteners (a possibility if the NAFTA reduces the price of corn in Mexico in the long run), then approximately 1.2 million tons of sugar now used in soft drinks would be released for other uses. Because the agreement includes corn sweetener in Mexico's sugar consumption, Mexico would not be permitted to ship sugar to the United States if its soft drink industry converts to corn sweeteners.

The Mexican soft drink industry uses only sugar as a sweetener. If this industry should switch to the use of corn sweeteners (a possibility if the NAFTA reduces the price of corn in Mexico in the long run), then approximately 1.2 million tons of sugar now used in soft drinks would be released for other uses.

Second, the Mexican sugar processing industry, a government-owned monopoly for many years, is now being privatized. If privatization improves the efficiency of this industry, Mexico's sugar industry could be more competitive and its export potential would be improved.

Third, growth in the demand for sugar will be a major determinant of U.S.-Mexican sugar trade. If income growth in Mexico continues at a high rate, then the demand for sugar in Mexico could rise faster than the supply, and it is unlikely that Mexico would be a major sugar exporter. If income and demand growth are slower, Mexico is more likely to increase its exports of sugar.

Food Processing Industries: The NAFTA could also affect some food processing industries, particularly if low labor costs in Mexico cause major shifts in the location of production and processing. The impact of the NAFTA on food processors will also depend on several other factors, including packaging regulations, grades and standards, and food safety and health standards for processed products.

The impact of the NAFTA on food processors will depend on several other factors, including packaging regulations, grades and standards, and food safety and health standards for processed products.

Processors of fruits and vegetables often locate close to production. If major shifts in production occur, then processing may also shift. Such changes would be most likely to occur in vegetable production, where Mexico exhibits a comparative advantage in the production of some commodities.

These shifts could affect large firms less than smaller processors if smaller firms have lower profit margins or less modern facilities. Large processors may invest in Mexico to capture increased demand

or cost advantages, but smaller processors would have less flexibility in moving processing facilities to Mexico.

U.S. Trade Policy and the Movement Toward Regional Trade Agreements

Because the United States has led the movement toward multilateral trade liberalization, the establishment of a North American free trade area represents an important shift in U.S. trade policy.

If the NAFTA is approved, some U.S. agricultural producers will gain increased export opportunities while others will face increased import competition. Because the United States has led the movement toward multilateral trade liberalization, the establishment of a North American free trade area would represent an important shift in U.S. trade policy. This change, combined with the formation of free trade areas in other regions of the world, poses new issues in international trade policy. The next chapter will discuss the implications of the emerging trading blocs for U.S. agricultural trade.

Appendix IV-A. Major agricultural provisions of the U.S.-Canadian Free Trade Agreement.

All tariffs on agricultural products will be removed by 1998.

Each country will work to harmonize technical regulations.

Canada's global import quotas on chickens, turkeys, and eggs will be increased.

Each country will be exempted from the other's meat import law.

Canada's rail subsidy on grain and oilseeds shipped to the United States through west coast Canadian ports will be eliminated.

Export subsidies are prohibited on agricultural products shipped to either country.

A special "snapback" provision allows either country to assess a temporary tariff on fruit and vegetable imports if domestic production suffers excessive damage from imports.

Trade disputes will be settled by a bilateral panel whose decisions are binding.

Appendix IV-B. Major agricultural provisions of the North American Free Trade Agreement.

Tariffs and quantitative import barriers are removed among NAFTA members but are unchanged for the rest of the world.

All quotas and import licenses will be eliminated and replaced with tariffs or tariff rate quotas (TRQs).

Mexico will convert all import licenses to TRQs.

The United States will convert Section 22 (dairy, sugar, cotton, peanuts) quotas to TRQs.

TAQs will also be used to ease transition for "sensitive products."

All Tariffs and tariff rate quotas will be phased out by 2009.

Export subsidies will be permitted only to match subsidies from countries outside the NAFTA.

Trade disputes will be settled by a trilateral panel whose decisions are binding.

CHAPTER V

AGRICULTURE IN A CHANGING GLOBAL ECONOMY

ISSUES TO CONSIDER

- Why is there a movement toward trade blocs?
- Will a tripolar world evolve?
- Can agricultural policy survive in a trade bloc?
- What are the implications of the formation of trade blocs?

The preceding chapters examined the underlying economic forces that determine trade patterns, the impact of government policies on international markets, the role of the General Agreement on Tariffs and Trade (GATT) in reducing trade barriers and the potential impact of a North American Free Trade Agreement (NAFTA) on agricultural trade. This chapter discusses the impact of broader changes in economic and political relationships on international agricultural markets and the potential impact of these changes on U.S. and Michigan farmers.

WHY TRADE BLOCS?

A trade bloc is formed when trade barriers are reduced among the members of the bloc while trade barriers remain in force against all other nations. This discrimination creates a fundamentally different trading structure than that sought through multilateral negotiations aimed at reducing trade barriers among all trading partners.

A trade bloc is formed when trade barriers are reduced among the members of the bloc while trade barriers remain in force against all other nations. This discrimination creates a fundamentally different trading structure than that sought through multilateral negotiations aimed at reducing trade barriers among all trading partners.

Leadership in seeking worldwide multilateral reduction in trade barriers has been provided by the United States; the EC has provided leadership in the search for managed trading arrangements.

In recent years, the world has faced a split between those nations seeking multilateral trade liberalization and those pursuing the formation of regional free trade areas, or trade blocs. The United States has traditionally provided leadership in pursuing multilateral reductions in trade barriers, while the European Community — along with some countries with an overriding interest in a specific commodity (Brazil in coffee, for example) — has often provided leadership in the search for managed trading arrangements. Neither of these approaches has succeeded in preventing policy conflicts among nations.

The formation of regional trade agreements is not a new phenomenon — trade blocs existed in Europe as early as the 1950s. Two

major trade blocs — the European Community in western Europe and the Council for Mutual Economic Cooperation in eastern Europe — have existed for most of the postwar period. The other preferential trading arrangements of long standing are those between several European countries and their former colonies. Numerous efforts were also made to establish regional trade agreements among the developing countries of Africa and Latin America. Among the major regions of the world, only Asia has spurned efforts at forming regional trading blocs.

The reasons for developing these preferential trading arrangements have varied. In both eastern and western Europe, the original movement toward integration was designed to facilitate postwar economic recovery and establish stronger economies in support of military objectives. Trade blocs among developing countries were usually formed to expand market size and to provide a broader based economy within which to accelerate economic development.

The formation of regional trade agreements is not a new phenomenon—trade blocs existed in Europe as early as the 1950s.

Among the major regions of the world, only Asia has spurned efforts at forming regional trading blocs during most of the post-World War II era.

U.S. Participation in Trade Blocs

During the past decade, the United States has shown increased interest in the use of bilateral free trade agreements to pursue its trade policy interests. This approach was implemented in the 1980s, after a U.S.-led effort to complete a new round of broadly based GATT negotiations reached a stalemate. Resistance by other countries, particularly the European Community, delayed the completion of multilateral negotiations. This led the United States to pursue a two-track strategy in formulating trade policy. In addition to continued efforts to complete the Uruguay round of multilateral negotiations, the United States also negotiated comprehensive bilateral free trade agreements with Israel in 1985 and Canada in 1988. These were followed by the negotiation of the North American Free Trade Agreement in 1992. The United States has also expressed its willingness to explore bilateral free trade agreements with other countries.

The initial objective of the U.S. bilateral approach was to achieve partial success in reducing trade barriers until broader multilateral agreements could be negotiated. In this context, bilateral agreements were pursued as a complement to the multilateral effort in the GATT. At the same time, the United States has asserted that it would pursue bilateral and multilateral trade agreements with like-minded coun-

The United States has pursued a two-track strategy in formulating trade policy, with bilateral agreements serving as a complement to the mu tilateral negotiating efforts in the GATT.

tries if its objectives for the GATT negotiations are not met. This approach laid the groundwork for U.S. participation in both bilateral and multilateral trade agreements.

The dissolution of the USSR-eastern European trade bloc, the negotiation of the North American Free Trade Agreement and the further integration of European markets under the auspices of the EC 1992 program mark the beginning of a new era.

More and Larger Trade Blocs May Form

The dissolution of the USSR-eastern European trade bloc, the negotiation of the North American Free Trade Agreement and the further integration of European markets under the auspices of the EC 1992 program mark the beginning of a new era. The NAFTA may expand to encompass more Caribbean or Latin American countries, while eastern European countries may seek membership in the European Community. An expanded EC could extend trade preferences to African countries and create a large north-south trading bloc.

The six countries of the Association of Southeast Asian Nations (ASEAN) — Indonesia, Singapore, Thailand, Malaysia, the Philippines and Brunei — have discussed the creation of a free trade area that would include 320 million consumers in one of the world's fastest growing regions.

Will comparable developments occur in Asia? Asian countries have spurned past efforts at economic integration, but the countries of that region are contemplating the formation of a free trade area. The six countries of the Association of Southeast Asian Nations (ASEAN) — Indonesia, Singapore, Thailand, Malaysia, the Philippines and Brunei — have discussed the creation of a free trade area that would include 320 million consumers in one of the world's fastest growing regions. If established, this agreement could begin with a reduction in tariffs in 1993 and create a free market for some industrial products in 15 years.

Interest in an Asian agreement has been heightened by the potential approval of the NAFTA, but these nations' concerns extend beyond the formation of a North American trade bloc. Their broader concern is that, in a world dominated by trade blocs, their interests will be ignored if an Asian bloc does not exist to counter the influence of European or North American blocs. If an Asian trade bloc expands to encompass the industrial countries of Japan, Korea, Taiwan, Hong Kong, Australia and New Zealand, a massive trade bloc encompassing many of the world's fastest growing economies would be formed. A tripolar world consisting of trade blocs in Asia, the Americas and Europe-Africa could emerge in the coming decade.

A tripolar world consisting of trade blocs in Asia, the Americas and Europe-Africa could emerge in the coming decade.

Agricultural Policy in Trade Blocs

How should farm policy be treated among the members of a trade bloc? This difficult question is an important issue that must be resolved during the negotiation of any regional free trade agreement.

Can farm policy treat member countries consistently or at least accommodate the objectives sought by members of a trade bloc?

The European Community's approach to this issue has been to develop its Common Agricultural Policy (CAP). The CAP is based on three principles: common price support policies for agricultural products, community preferences that provide common protection against import competition and common financing of agricultural programs.

Common pricing provides communitywide commodity price support programs designed to facilitate trade among EC members. Community preferences provide domestic products with community-wide protection against imports. The two most common means of achieving this preference are through the use of minimum import prices (maintained by variable levies) and subsidies on domestic products. Common financing requires all members to share the cost of agricultural policies. Implementing this policy requires an extensive decision-making system that recognizes the basic interests of each member country but also develops and implements a consistent communitywide policy. Though often faced with serious differences among member countries, particularly on trade policy issues, the EC has succeeded in developing an effective framework for making and implementing agricultural policy decisions. Movement toward a more integrated system, including proposals to establish a common currency, will further test the resiliency and adaptability of this system.

One approach is to unify the farm policies of member nations through the use of common price support, financial and trade policies.

The European Community has succeeded in developing an effective framework for making and implementing agricultural policy decisions.

Another approach is to fully implement free trade by eliminating all trade-distorting agricultural policies in all member countries. This approach faces some of the same difficulties encountered in multilateral negotiations on agricultural trade issues. Trade barriers are likely to be phased out over time, with adequate recognition of the sectoral, commodity and institutional differences among the member countries. This approach was used to negotiate reductions in most agricultural trade barriers between the United States and Mexico in the NAFTA.

A second approach is to fully implement free trade by eliminating all trade-distorting agricultural policies in all member countries. This approach was used to negotiate reductions in most agricultural trade barriers between the United States and Mexico in the NAFTA.

The problems encountered in reaching agreement on these adjustments, even among a small number of nations, are substantial, and the magnitude of these problems increases as the number of par-

ticipating nations increases. The ultimate goal of this approach — the removal of all trade barriers — can only be achieved gradually in most cases.

Economic Implications of Trade Blocs

The formation of a trade bloc can result in either trade-creating or trade-diverting impacts. Trade creation occurs when removing trade barriers among the members of a bloc increases the total volume of trade. Trade diversion occurs when removing trade barriers among the members of a bloc causes a shift in trade, with greater trade occurring among the members of the bloc but less trade occurring between the bloc and the rest of the world. If trade creation is greater than trade diversion, then the formation of the free trade area will result in a net gain in world welfare (by causing improved resource use). If trade diversion occurs, however, countries outside the trading bloc are discriminated against and may lose export markets that existed before the free trade area was formed.

Both trade-creating and trade-diverting impacts can result from the formation of a trading bloc. If trade creation is greater than trade diversion, then a net gain has been achieved through formation of the free trade area.

The extent of trade creation and trade diversion resulting from the formation of a trade bloc will be determined by two factors. First, the degree of discrimination between the members of the bloc and non-members will be the major determinant of trade creation or diversion. If trade barriers among the members of the bloc were low before the bloc was formed, then the formation of the bloc will discriminate less against non-members and trade diversion is less likely to occur. Second, the competitiveness of producers inside the trade bloc relative to producers in non-member nations will also determine the extent of trade creation and diversion. If the cost of producing a particular good is lower outside the bloc, then the formation of a free trade area is more likely to result in trade diversion.

If trade barriers among the members of the bloc were low before the bloc was formed, then the formation of the bloc will discriminate less against non-members and trade diversion is less likely to occur.

The formation of a trade bloc can also stimulate long-term, dynamic changes beyond those caused by trade creation or diversion. These changes can stimulate economic growth, improve competition and efficiency, create greater economies of scale, and generate desirable structural or economic changes that might not have occurred without the formation of the trade bloc. By generating increases in income, these changes can have a demand effect that will increase the volume of trade within the bloc and between the bloc and non-member countries.

The formation of a trade bloc can also stimulate long-term, dynamic changes beyond those caused by trade creation or diversion.

Because U.S. farmers could be affected by both short-term and long-term changes generated by the formation of trade blocs, there is concern about the trade-offs that might exist. For example, U.S. imports of Canadian livestock products might increase in a free trade area, but U.S. exports of fruits and vegetables to Canada could also increase. Similarly, U.S. imports of horticultural products from Mexico may increase, but the United States is also likely to increase its exports of grains, oilseeds and livestock products. The debate over the gains and losses created by the formation of trade blocs will continue for the coming decade.

Because U.S. farmers could be affected by botl short-term and long-term changes generated by the formation of trade blocs, there is concern about the trade-offs that might exist.

Implications for U.S. Agriculture

The movement toward regional free trade agreements, combined with the outcome of the multilateral GATT negotiations, has the potential to cause major structural changes in international agricultural markets. Although these changes could affect both member and non-member countries, the formation of free trade areas has received the support of many nations. The trade discrimination inherent in these agreements is permissible under the rules of the GATT. Regardless of the outcome of the debate over the NAFTA, there is little evidence that the wider trend toward the formation of free trade areas will be reversed in the near future. Regional economic integration and multilateral changes in trade policy will continue to affect the opportunities available to U.S. farmers in international markets.

Regardless of the outcome of the debate over the NAFTA, there is little evidence that the wider trend toward the formation of free trade areas will be reversed in the near future.

Short-run market shifts that result from trade liberalization are probably less important to the future of agricultural trade than the longer term impact of liberalization on economic growth. As discussed earlier, increased economic growth, leading to increased demand for food, has been the major cause of the growth in agricultural trade during the postwar period. Unfortunately, income growth in many poor countries continues to be limited by inadequate market systems, lack of trained personnel to develop and execute development plans, and conflicts among political leaders.

Short-run impacts through market shifts are less important than the longer term impact that can result if integration stimulates economic growth and hence expanded demand for food, especially in poor nations.

The underlying conditions for increased growth are favorable under the NAFTA. Mexico is a large country with sufficient population to achieve economies of scale in the development of both domestic and export industries. Mexico is also undertaking internal reforms to privatize many industries and attract international investment.

These all suggest that Mexico's economic growth has the potential to remain strong and generate a significant demand effect from the trade liberalization accomplished by the NAFTA. Large numbers of low-income consumers should gain from growth in the Mexican economy. When people at these income levels increase their earnings, they improve their diets and spend more on food. This can generate an important expansion in the export market for U.S. farm products, and Michigan farmers would share in these gains.

Trading blocs are formed for the benefit of member countries, not for the world in general. How these kinds of impacts would play out in a tripolar world is difficult to predict.

Though these conclusions are supported by research, the nature and extent of trade-offs and the impact of economic growth in a broader framework are less clear. Trade blocs are formed for the benefit of member countries, not for the world in general. The impact of the creation of a tripolar world would depend on whether these regions create new trade barriers aimed at countries outside each trade bloc. If the movement toward regional trade agreements results in the formation of trade blocs that develop a fortress mentality and establish protectionist policies, world prosperity and international market growth could decline. If, on the other hand, the GATT negotiations succeed in achieving multilateral reductions in trade barriers, then the formation of regional trade blocs could stimulate flows of capital and technology that will generate more rapid economic growth for all countries. Such an outcome is the best means of achieving an expansion in agricultural trade.

If regionalism results in heavily protected trading blocs that develop a fortress mentality and defensive policies, world prosperity and international market growth could decline. This would not bode well for U.S. and Michigan farmers.

Chapter VI

SUMMARY

The economic and political dimensions of agricultural trade policy are diverse and often contentious. This publication has examined the impact of international trade on U.S. agriculture and the U.S. role in shaping agricultural trade policy.

Several summary observations can be offered about the future of agricultural trade policy and its impact on world markets.

- The U.S. has provided leadership in reducing tariffs on most industrial products. Despite efforts by the United States and some other nations to reduce trade barriers on agricultural products, the same has not occurred in agriculture.
- Agricultural protectionism has increased during much of the post-World War II period and has been brought into multilateral negotiations only in the last two rounds of GATT negotiations (Tokyo and Uruguay).
- In the early 1980s, the United States moved to a two-track approach to trade policy and began to seek bilateral free trade agreements with willing countries.
- Negotiations on a North American Free Trade Agreement are complete. If this agreement is approved, additional Caribbean and South American nations may be included in the future.
- If a tripolar world of European, Asian and North American trade blocs does emerge, the structure of world agricultural markets could change significantly. If such blocs result in the creation of trade barriers that further inhibit trade, then U.S. agriculture could be excluded from some markets.
- If trade blocs are formed in all three regions, internal trade (trade diversion) could increase at the expense of third countries. All major food exporters will continue to seek international markets for their farm products, however, and disputes over agricultural trade policy issues will continue to affect international markets.
- If the formation of trade blocs creates new trade barriers, agricultural trade could be relegated to an increasingly volatile and unstable residual market. The likelihood of such an outcome will be reduced if there is significant progress in achieving multilateral reductions in trade barriers through the Uruguay round of GATT negotiations.

➡ What does the future hold for agricultural trade policy? Though few countries seem willing to accept the complete elimination of agricultural trade barriers, it does seem realistic to expect some reduction in trade barriers and lower levels of protection for agriculture for a number of reasons.

First, government and consumer costs of protection are high and many industrialized countries are attempting to reduce these costs. Second, the impact of these programs on other countries, especially developing countries, are severe — they create barriers to economic growth in these countries that may prevent their becoming major new sources of demand for agricultural exports. Finally, calls for improved use of resources will continue. Throughout the coming decade, governments will continue to ask what level and forms of protection are justified for agriculture and how world trading rules can establish an equitable trading system for all nations.

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A GLOSSARY OF SELECTED AGRICULTURAL TRADE POLICY TERMS

The following is a list of terms that arise in many discussions of agricultural trade policy. Italicized words are defined elsewhere in the list. Definitions were selected from Lipton (1991).

Accession — The process of a country becoming a member of an international agreement, such as the General Agreement on Tariffs and Trade. Negotiations determine the specific obligations a nonmember country must meet before it is entitled to full GATT membership benefits.

Ad valorem tariff — A governmental tax on imports assessed as a percentage of the value of the goods cleared through customs. For example, 10 percent ad valorem means the tariff is 10 percent of the value of the goods.

Antidumping law — A provision (title VII) of the U.S. Tariff Act of 1930 that allows the U.S. Department of Commerce to levy antidumping duties equivalent to the dumping margins under certain conditions. The Commerce Department must determine that an imported product is being sold at less than its fair value and the U.S. International Trade Commission must determine that a U.S. producer is thereby being injured.

Balance of payments — A statement of economic transactions showing the relative difference between the inflow and outflow of goods, services, and capital claims and liabilities between a country and its trading partners. The balance of payments include (1) current accounts, including trade and services; (2) capital accounts, including short- and long-term items; (3) transactions in reserve assets (gold, special drawing rights, and foreign currency holdings); and (4) unilateral transfers of gifts by governments and individuals.

Balance of trade — The difference between the value of goods that a nation exports and the value of the goods it imports. A trade surplus occurs when a country's exports exceed its imports, resulting in a favorable trade balance. Similarly, a trade deficit implies that imports total more than exports for a country, producing an unfavorable trade balance.

Barter — A form of countertrade in which goods of equal value are exchanged under a single contract, within a specified time period, and without any flow of money taking place.

Bilateral trade agreement — A trade agreement between any two nations. The agreement may be either preferential, applying only to the two countries involved, or most-favored-nation, negotiated between the two countries but extending to all or most other countries.

Binding — A commitment made by a government, usually negotiated under the General Agreement on Tariffs and Trade (GATT), that a tariff will not be raised beyond a negotiated level without compensating affected parties. Failure to comply with the commitment gives affected GATT members the right to withdraw bindings of equivalent value.

Blended credit — A form of export subsidy which combines direct Government export credit and credit guarantees to reduce the effective interest rate.

Bound rates — Tariff rates resulting from the General Agreement on Tariffs and Trade (GATT) negotiations or accessions that are incorporated as part of a country's schedule of concessions. Bound rates are enforceable under Article II of GATT. If a GATT contracting party raises a tariff above the bound rate, the affected countries have the right to retaliate against an equivalent value of the offending country's exports or receive compensation, usually in the form of reduced tariffs or other products they export to the offending country.

Cairns Group — A group formed in 1986 at Cairns, Australia. The group seeks the removal of trade barriers and substantial reductions in subsidies affecting agricultural trade in response to depressed commodity prices and reduced export earnings stemming from subsidy wars between the United States and the European Community (EC). The members account for a significant portion of the world's agricultural exports. The group includes major food exporters from both developed and developing countries: Argentina, Australia, Brazil, Canada, Chile, Colombia, Hungary, Indonesia, Malaysia, New Zealand, the Philippines, Thailand, and Uruguay. The Cairns Group is a strong coalition in the Uruguay Round of multilateral trade negotiations held under the auspices of the General Agreement on Tariffs and Trade (GATT).

Capital account — Part of a nation's balance of payments that includes purchases and sales of assets, such as stocks, bonds, and land. A nation has a capital account surplus when receipts from asset sales exceed payments for the country's purchases of foreign assets. The sum of the capital and current accounts is the overall balance of payments.

Cartel — An alliance or arrangement of independent sellers in the same field of business organized in order to function as a monopoly with respect to production or marketing of the commodity.

Common Agricultural Policy (CAP) — A set of regulations by which members of the European Community (EC) seek to merge their individual agricultural programs into a unified effort to promote regional agricultural development, fair and rising standards of living for the farm population, stable agricultural markets, increased agricultural productivity, and methods of dealing with food supply security. The variable levy and export subsidies are two principal elements of the CAP.

Common external tariff — The tariff schedule applied by members of a customs union, such as the European Community (EC), to imports from nonmember countries.

Common market — A regional grouping of countries that levies common external duties on imports from nonmember countries, but which eliminates tariffs, quotas, and other miscellaneous government restrictions on trade among member countries. Also referred to as a tariff union. The European Community (EC) is probably the best known current example of a common market. Others include the Belgium-Luxembourg Economic Union; BENELUX (Belgium, the Netherlands, and Luxembourg); the Central African Customs and Economic Union; the East African Community; the West African Economic Community; and the Central American Common Market. See also customs union.

Compensation — A General Agreement on Tariffs and Trade (GATT) principle which requires a member country that raises a tariff above its bound rate, withdraws a binding, or otherwise violates a trade concession, to lower other tariffs or make other concessions to offset the disadvantage suffered by trading partners. GATT provides that any country that believes its trade interests have been adversely affected by changes in the import regime of another country may request consultations with the offending country. If such government-to-government consultations do not yield results satisfactory to the concerned parties, the complaining country may seek the establishment of an advisory panel which, under the supervision of GATT, will review the facts and recommend compensations or other appropriate action.

Competitive imports — Imported products that are also produced domestically. Examples for the United States are beef or cotton.

Concession — A tariff reduction, tariff binding, or other agreement to reduce import restrictions. In negotiations, a country may offer to reduce its own tariff and nontariff trade barriers to induce other countries to reciprocate. Concession is a key concept of the General Agreement on Tariffs and Trade (GATT) negotiations.

Concessional sales — Credit sales of a commodity in which the buyer is allowed more favorable payment terms than those on the open market. For example, title I of Public Law 480 provides for financing sales of U.S. commodities with low-interest, long-term credit.

Conditional Most-Favored-Nation — The according of most-favored-nation (MFN) treatment subject to compliance with specific terms or conditions. All members of the General Agreement on Tariffs and Trade (GATT), including the United States, accord unconditional MFN treatment to most other GATT members. The United States, however, confers annually renewable MFN treatment to a limited number of countries conditional on their compliance with the terms of Title IV of the Trade Act of 1974.

Contracting party (CP) — A country that has signed the General Agreement on Tariffs and Trade (GATT) and has accepted its specified obligations and benefits. As of January 1991, there were 101 contracting parties to the GATT. About 30 other countries apply GATT rules de facto.

Countervailing duty (CVD) — An additional levy imposed on imported goods to offset subsidies provided to producers or exporters by the government of the exporting country. A wide range of practices are recognized as constituting subsidies that may be offset. Countervailing duties are permitted under Article VI of the General Agreement on Tariffs and Trade (GATT). Under U.S. law, however, countervailing duties can only be imposed after the U.S. International Trade Commission has determined that the imports are causing or threatening to cause material injury to a U.S. industry.

Credit guarantees — USDA programs that protect U.S. exporters or financial institutions against loss due to nonpayment by a foreign buyer. Maximum credit guarantee coverage period is 3 years under the Export Credit Guarantee Program (GSM-102) and up to 10 years under the Intermediate Export Credit Guarantee Program (GSM-103). The programs are operated by USDA's Commodity Credit Corporation. The amount of coverage, including the interest rate and the guarantee fee, is established in the Office of the General Sales Manager and varies by country.

Current account — Part of a nation's balance of payments which includes the value of all goods and services imported and exported, as well as the payment and receipt of dividends and interest. A nation has a current account surplus if exports exceed imports plus net transfer to foreigners. The sum of the current and capital accounts is the overall balance of payments.

Customs union — Similar to a common market except that customs unions do not permit free movement of all factors of production. The European Community (EC) is the best known example of a customs union.

Decoupling — A term used to describe programs which would separate government payments to farmers from the current or future quantity of a commodity produced or marketed, and from the quantity of inputs used in production. Farmers would make production decisions based on market prices but receive government payments independent of production and marketing decisions.

Devaluation — An official reduction of the exchange rate of a nation's currency which lowers the price of domestic currency to foreigners and raises the price of foreign currency. Prices of a

nation's imports rise after devaluation and the cost of exports to foreigners declines. Devaluation is done to address balance of payments problems.

Developing countries — Countries whose economies are mostly dependent on agriculture and primary resources and do not have a strong industrial base. These countries generally have a gross national product below $1,890 per capita (as defined by the World Bank in 1986).

Discrimination — The unequal treatment of internationally traded goods or services according to their source or destination. General Agreement on Tariffs and Trade (GATT) members are generally prohibited from applying discriminatory treatment to either imports or exports.

Dispute settlement — Procedures detailed in the General Agreement on Tariff and Trade (GATT) for legal redress in cases of violation, nullification, or impairment of trade benefits. Article XXII of the GATT obligates contracting parties to consult on GATT matters if any other member makes a request. Article XXIII similarly provides for bilateral consultations, as well as the establishment of a GATT panel to study the matter.

Dumping — Technically, the sale of products on the world market below the cost of production to dispose of surpluses or gain access to a market. Dumping is generally recognized as an unfair trade practice because it can disrupt markets and injure producers of competitive products in an importing country. Article VI of the General Agreement on Tariffs and Trade (GATT) permits special antidumping duties equal to the difference between the price sought in the importing country and the normal value of the product in the exporting country.

Duty — See Tariff.

Embargo — A government-ordered prohibition of trade with another country restricting all trade or only that of selected goods and services.

European Community (EC) — An organization established by the Treaty of Rome in 1957 and also known as the European Economic Community and the Common Market. Originally composed of the six European nations of Belgium, the Federal Republic of Germany, France, Italy, Luxembourg, and the Netherlands, it has expanded to 12 nations. The EC attempts to unify and integrate member economies by establishing a customs union and common economic policies, including the Common Agricultural Policy (CAP). Member nations include the original six nations plus Denmark, Greece, Ireland, Portugal, Spain, and the United Kingdom.

European currency unit (ECU) — A weighted average of all European Community (EC) currencies (except for those of Spain and Portugal). The ECU fluctuates against third country currencies and is used for internal EC accounting purposes. In agriculture, common farm prices, subsidies, and import levies are established in the ECU. Similar to the previously used European unit of account.

European Free Trade Association (EFTA) — A regional free trade area established in 1958 concerned with eliminating tariffs on manufactured goods and agricultural products and originate in and are traded among member countries. Most agricultural products are not subject to EFTA schedule tariffs reductions. Members include Austria, Finland, Iceland, Norway, Sweden and Switzerland.

European monetary system (EMS) — A monetary system established in 1979 to move Europe toward closer economic integration and avoid the disruption in trade that can result from fluctuations in currency exchange rates. The EMS member countries deposit gold and dollar reserves

with the European Monetary Cooperation Fund in exchange for European currency units. The EMS includes all EC members except Greece and the United Kingdom.

Exchange rate — The number of units of one currency that can be exchanged for one unit of another currency at a given time. A decline in the value of the U.S. dollar drops the "price" of U.S. farm products in terms of the currency of many importers. Conversely, an appreciation in the value of the dollar means that foreign importers must spend more of their currency to buy American farm products.

Export allocation or quota — Controls applied by an exporting country to limit the amount of goods leaving that country. Such controls usually are applied in time of war or during some other emergency requiring conservation of domestic supplies.

Export Credit Guarantee Program (GSM-102) — The largest U.S. agricultural export promotion program, functioning since 1982. It guarantees repayment of private, short-term credit for up to 3 years.

Export Enhancement Program (EEP) — A program initiated in May 1985 under a Commodity Credit Corporation (CCC) charter to help U.S. exporters meet competitors' prices in subsidized markets. The program was formally authorized by the Food Security Act of 1985. Under the EEP, exporters are awarded generic commodity certificates which are redeemable for CCC-owned commodities, enabling them to sell certain commodities to specified countries at prices below those of the U.S. market.

Export Incentive Program (EIP) — A program administered by USDA's Foreign Agricultural Service which assists private firms to promote their branded products overseas. An EIP is developed for a specific commodity or product based, in part, on a determination that export markets for the product can be developed most effectively by brand promotion and that there is sufficient U.S. industry interest to support such a program.

Export license — A government document authorizing exports of specific goods in specific quantities to a particular destination. Some countries require an export license only under special circumstances, while others require it for most or all exports.

Export restitutions — Direct export subsidy payments used to promote exports of agricultural goods by the European Community (EC). The "restitution" refunds the difference between the domestic market price and the lower price needed to export.

Export subsidies — Special incentives, such as cash payments, tax exemptions, preferential exchange rates, and special contracts, extended by governments to encourage increased foreign sales. These subsidies are most often used when internal prices exceed export prices. Under Article XVI of the General Agreement on Tariffs and Trade (GATT), export subsidies are considered unfair competition and countervailing duties are allowed on subsidized products. The Tokyo Round produced an agreement on subsidies and countervailing duties that prohibits export subsidies by developed countries on manufactured and semi-manufactured goods.

Exports — Domestically produced goods and services that are sold abroad.

Fair value — The reference against which U.S. purchase prices of imported merchandise are compared with during antidumping investigations. Fair value is generally expressed as the weighted average of the exporter's domestic market prices, or prices to third countries during the period of investigation. However, it may be a constructed value if there are no, or virtually no, home mar-

ket or third country sales, or if there are too few sales made at prices above the cost of production to provide an adequate basis for comparison.

Fast-track negotiating authority — Presidential authority granted by Congress to negotiate trade agreements with the understanding that the negotiated agreement will go before Congress for an "up" or "down" vote without possibility of amendment and within a specified time period.

Fixed exchange rates — Exchange rates established and maintained by government intervention in foreign exchange markets. Also known as controlled exchange rates.

Flexible exchange rate — The market-determined rate of exchange of a nation's currency. The value of a country's currency is determined by the supply and demand for the currencies, which are based on the supply and demand for goods and services produces by the trading nations. Also called a floating exchange rate.

Food and Agriculture Organization (FAO) — An agency of the United Nations concerned with the distribution and production of food and agricultural products around the world. Founded in 1945, FAO is responsible for collecting, analyzing, and disseminating country data on food, agriculture, and rural affairs. The agency also offers technical assistance and operates training projects in many developing countries. Officially known as the United Nations' Food and Agriculture Organization.

Foreign Agricultural Service (FAS) — The export promotion and service agency for USDA. FAS coordinates and directs USDA's activities related to international trade agreement programs and negotiations to improve access for U.S. farm products abroad. The agency is also responsible for gathering and disseminating information on worldwide production, supply, and demand for agricultural commodities; operating statutory programs to facilitate the export of U.S. agricultural products, and representing U.S. agricultural interests abroad.

Free trade area — A cooperative arrangement by a group of nations to eliminate trade barriers among members. Each member may maintain its own trade regime with nonmember nations. The European Free Trade Association is the best known example.

GATT Codes of Conduct — Instruments that prescribe standards of behavior under the General Agreement on Tariffs and Trade (GATT). The codes establish sanctions governing the use of nontariff trade barriers. The sanctions were negotiated during the Tokyo Round. Only signatories to each code are bound by its terms.

GATT Panel — A group composed on neutral representatives that may be established by the GATT Secretariat under the dispute settlement provisions of the General Agreement on Tariffs and Trade. The GATT panel reviews the facts of a dispute and renders findings of GATT law and recommends action.

GATT Rounds — Cycles of multilateral trade negotiations conducted under the General Agreement on Tariffs and Trade (GATT). Eight rounds have been completed since the GATT was established in 1947.

1947:GATT was created during this round.

1949:This round involved negotiations with nations that desired GATT membership. Principal emphasis was on tariff reduction.

1951:This round continued membership and tariff reduction negotiations.

1956:This round proceeded along the same track as earlier rounds.

1960-62: This round, referred to as the Dillon Round, involved further revision of the GATT and the addition of more countries.

1963-67: Known as the Kennedy Round, this round was a hybrid of the earlier product-by-product approach to negotiations and the new formula tariff reduction approach with across-the-board tariff reductions.

1973-79: This round, also called the Tokyo Round, centered on the negotiation of addition tariff cuts and developed a series of agreements governing the use of a number of nontariff measures.

1986 to date: The current round, termed the Uruguay Round, focuses on strengthening the GATT and expanding it disciplines to new areas, including agriculture.

GATT Secretariat — The administrative body of the GATT headed by the Director-General and headquartered in Geneva, Switzerland.

General Agreement on Tariffs and Trade (GATT) — Agreement, originally negotiated in Geneva, Switzerland, in 1947, among 23 Countries including the United States, to increase international trade by reducing tariffs and other trade barriers. This multilateral agreement provides codes of conduct for international commerce. GATT also provides a framework for periodic multilateral trade negotiations on trade liberalization and expansion. The eighth and most recent round of negotiations began in Punta del Este, Uruguay, in 1986. See GATT Rounds.

Generalized System of Preferences (GSP) — A policy that permits tariff reductions or possibly duty free entry of certain imports from designated developing countries. Among other things, the GSP may increase economic growth in developing countries, help maintain favorable foreign relations with free world developing countries, and may serve as a low-cost means of providing aid to these nations. It is part of a coordinated effort of the industrial trading nations to bring developing countries more fully into the international trading system. Under the GSP, the United States provides nonreciprocal tariff preferences for designated developing nations.

Global quota — Limit established by a country on the value or goods which may be imported or exported through its borders during a given period.

Impairment — The partial or total loss of a benefit that was negotiated between the General Agreement on Tariffs and Trade contracting parties, due to an action, policy, or lack of action by one of the parties. Impairment of GATT rights and obligations is subject to formal action under GATT dispute settlement procedures.

Import barriers — Quotas, tariffs, and embargoes used by a country to restrict the quantity or value of a good that may enter that country.

Import licensing — Procedures that require documentation (other than that required for customs purposes) to be submitted to the relevant administrative body for approval before importing is allowed.

Import quota — The maximum quantity or value of a commodity allowed to enter a country during a specified time period. A quota may apply to amounts of a commodity from specific countries

Import substitution — A strategy which emphasizes replacing imports with domestically produced goods.

Imports — The quantity or value of goods legally entering a nation.

Intellectual Property Rights (IPR's) — Ownership of the right to possess or otherwise use or dispose of products created by human ingenuity. Examples of IPR's include trademarks, patents, and copyrights. Increased protection of intellectual property rights is an issue of discussion in the Uruguay Round of General Agreement on Tariffs and Trade (GATT) talks.

International Monetary Fund (IMF) — Established in 1946 to assist in expansion of stable world trade and monitor exchange rate policies of member countries. The IMF also acts as a banker of last resort for countries experiencing foreign exchange deficiencies.

International trade barriers — Regulations imposed by governments to restrict imports from and exports to other countries. Tariffs, embargoes, import quotas, and unnecessary sanitary regulations are examples of such barriers.

International Trade Commission (ITC) — An independent agency of the U.S. Government established in 1916 to monitor trade, provide economic analyses, and make recommendations to the President in cases of unfair trade practices. Interest groups, such as growers or trade associations, can petition the ITC to investigate the trade practices of other countries to determine whether "material Harm" has been done to U.S. producers.

Internal trade-distorting subsidies — Payments to farmers which do not affect productions and thereby distort trade. Included would be the subsidies in calculating the "aggregate measure of support." Payments to farmers for conservation practices, disaster relief strictly income transfers "decoupled" from production etc. would not be considered trade distorting.

Market access — The extent to which a country permits imports. A variety of tariff and nontariff trade barriers can be used to limit the entry of foreign imports.

Market Promotion Program (MPP) — An export promotion program authorized by the Food, Agriculture, Conservation, and Trade Act of 1990 that replaces the Targeted Export Assistance (TEA) Program, authorized by the Food Security Act of 1985. The MPP is designed to encourage development, maintenance, and expansion of commercial farm export markets. Unlike TEA, the MPP does not restrict assistance to U.S. producer groups or regional organizations whose exports have been adversely affected by a foreign government's policies, although these cases receive highest priority. The program promotes exports of specific American commodities or products in specific markets. Under the program, eligible participants receive generic commodity certificates in payment for promotional activities approved by the Secretary of Agriculture.

Marketing board — A major form of government involvement in commodity marketing by some countries, such as Canada and Australia. These boards generally handle all export sales for the commodity. They may administer provisions to guarantee farmers a minimum price each year based on the cost of production or provide an initial minimum price with supplemental payments based on export sales. Boards may oversee a two-price plan in which domestic prices differ from the export price. Canada and Australia use marketing boards for selected grains, and Australia operates a wool marketing board. Many developing countries also use marketing boards for all import purchases.

Meat Import Law — A U.S. law, enacted in 1964 and amended in 1979, which provides for the imposition of import quotas if imports of certain meat products exceed the trigger level. This limit is calculated from a formula based on domestic quota meat production and cow beef production. The law applies to fresh, chilled, and frozen meat of cattle, sheep (except lamb), and goats, as well as certain prepared and preserved beef and veal products.

Most-favored-nation (MFN) — An agreement between countries to extend the same trading privileges to each other that they extend to any other country. Under a most-favored-nation agreement, for example, a country will extend to another country the lowest tariff rates it applies to any third country. A country is under no obligation to extend MFN treatment to another country, unless they are both contracting parties to the General Agreement on Tariffs and Trade (GATT), or unless MFN is specified in an agreement between them.

Multilateral Trade Negotiations (MTN) — In general, discussions of trade issues involving three or more countries. An example is the General Agreement on Tariffs and Trade (GATT) which serves as a forum for international tariff negotiations. This term is also applied to any of the eight rounds of GATT negotiations since 1947.

Noncompetitive imports — Agricultural products purchased from foreign countries because they cannot be grown profitably on a large scale in the importing country. For the United States, these imports include coffee, cocoa, rubber, and bananas.

Nontariff trade barriers — Regulations, other than traditional tariffs, used by governments to restrict imports from, and exports to, other countries. Embargoes, import quotas, import licensing, variable levies, state trading, and unnecessary or excessive labeling, health, and sanitary standards are examples of the types of nontariff trade barriers that have increased since the end of World War II, while tariff rates have declined significantly.

Organization for Economic Cooperation and Development (OECD) — An organization founded in 1961 to promote economic growth, employment, a rising standard of living, and financial stability; to assist the economic expansion of member and nonmember developing countries; and to further expand world trade. The member countries are Australia, Austria, Belgium, Canada, Denmark, Finland, France, the Federal Republic of Germany, Greece, Iceland, Ireland, Italy, Japan, Luxembourg, the Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, Switzerland, Turkey, the United Kingdom, and the United States.

Phytosanitary certificate — A document issued by a government to an exporter which certifies that the commodity is free from pests or disease. in accordance with the importing country's standards.

Preferential trade agreement — See Bilateral trade agreement.

Principal supplier — The country that is the most important source of a particular product imported by another country. In negotiations conducted under the General Agreement on Tariffs and Trade (GATT), a country offering to reduce import duties or other barriers on a particular item generally expects the principal supplier of the imported item to offer, in exchange, to reduce restrictions on another item. Both countries then automatically grant the same concession to all other countries to which they have agreed to accord most-favored-nation treatment.

Producer subsidy equivalents (PSE's) — An economic concept used to estimate the effect of government policy by measuring the amount of the cash subsidy or tax needed to hold farmers' incomes at current levels if all government agricultural programs were removed. PSE's are used to compare different policy tools and their effects on farmer revenue and consumer costs across countries. As a result, most General Agreement on Tariffs and Trade (GATT) trade liberalization proposals hinge on the use of measures such as PSE's and CSE's in negotiating lower protection levels.

Protectionism — A tariff, subsidy, or nontariff trade barrier, for example, imposed by a country in response to foreign competition, in order to protect domestic producers. This distorts the

world trading system by impairing the operation of comparative advantage and provides incentive for inefficient domestic production.

Public Law 480 (P.L. 480) — Common name for the Agricultural Trade Development and Assistance Act of 1954, which seeks to expand foreign markets for U.S. agricultural products, combat hunger, and encourage economic development in developing countries. Title I, also called the Food for Peace Program, makes U.S. agricultural commodities available through long-term dollar credit sales at low interest rates for up to 30 years. Donations for emergency food relief and nonemergency assistance are provided under Title II. Title III authorizes "food for development" projects. The Food, Agriculture, Conservation, and Trade Act of 1990 made fundamental changes in the U.S. food aid program, including shortening the maximum repayment term of Title I loans form 40 to 30 years and expanding Title II to include nonemergency assistance. The 1990 legislation also authorized a new Title III Food for Development Program that provides government-to-government grant food assistance to least developed countries.

Quantitative restriction (QR) — Explicit limits on the quantity or value of a product permitted to enter or leave a country. Examples include quotas, embargoes, restrictive licensing, and other means of limiting imports.

Quarantine. sanitary, and health laws and regulations — Government measures to protect human, plant, and animal health, such as restricting the use of potentially injurious preservatives and other additives in food products or denying entry of plants or animals from countries where specific diseases are present. While largely imposed for health reasons, in some cases these laws and regulations may be used to restrict foreign competition.

Reciprocity — A traditional principle of General Agreement on Tariffs and Trade (GATT) negotiations that implies an approximate equality of concessions accorded and trade benefits received among or between participants in a negotiation. Under GATT, developing countries have not been obliged to offer fully reciprocal concessions.

Reference price — The minimum import price for certain farm commodities under the European Community's Common Agricultural Policy. The reference price is normally based on an average of EC market or producer prices over a given period.

Residual supplier — A country that furnishes supplies to another country only after the latter has obtained all it can from other preferred sources.

Restitutions — A term used by the European Community to describe export subsidies on agricultural products. Specifically, restitutions are subsidies calculated to offset the difference between EC prices and world prices. In contrast, subventions are subsidies given without regard to market prices.

Retaliation — An action taken by one country against another for imposing a tariff or other trade barrier. Forms of retaliation include imposing a higher tariff, import restrictions, or withdrawal of previously agreed upon concessions. Under the General Agreement on Tariffs and Trade, restrictive trade action by one country entitles the harmed nation to take counteraction.

Section 22 — A section of the Agricultural Adjustment Act of 1933 (P.L. 73-10) that authorizes the President to restrict imports by imposing quotas or fees if the imports interfere with Federal price-support programs or substantially reduce U.S. production of products processed from farm commodities.

Section 32 — A section of the Agricultural Adjustment Act Amendment of 1935 (P.L. 74-320) which authorizes use of customs receipts funds to encourage increased consumption of agricultural commodities by means of purchase, export, and diversion programs. Section 32 is funded by a continuing appropriation of 30 percent of the import duties imposed on all commodities, both agricultural and nonagricultural. Domestic acquisition and donations constitute the major use of section 32.

Section 201 — Part of the U.S. Trade Act of 1974 (P.L. 93-618) that allows the President to provide relief to industries hurt by competing imports. Growers or trade associations must petition the International Trade Commission to investigate complaints of trade practices.

Section 301 — A provision of the U.S. Trade Act of 1974 (P.L. 93-618) that allows the President to take appropriate action to persuade a foreign government to remove any act, policy, or practice that violates an international agreement. The provision also applies to practices of a foreign government which are unjustified, unreasonable, or discriminatory, and which burden or restrict U.S. commerce.

Snap-back provision — A provision in an agreement that allows a signatory to withdraw concessions under specific circumstances, such as a surge of imports or balance of payments disequilibria.

Specific tariff — A tariff expressed as a fixed amount per unit. See also ad valorem tariff.

State marketing boards or state trading agencies — See marketing boards.

Tariff — A tax imposed on commodity imports by a government. A tariff may be either a fixed charge per unit of product imported (specific tariff) or a fixed percentage of value (ad valorem tariff).

Tariffication — The conversion of nontariff import barriers (such as variable levies import quotas, discretionary licensing, import bans and restrictive state trading practices) to tariffs. The resulting tariff equivalents would be based in observable differences between domestic and world prices for a specific period such as in 1986-88. See also Tariff rate quota system.

Tariff quota — Application of a higher tariff rate to imported goods after a certain quantitative limit (quota) has been reached during a specified period. The usual tariff rate applies to any imports below the quota amount. Tariff quotas do not limit the quantity of goods that may be imported.

Tariff rate quota system (TRQ) — A tariff system for sugar imports authorized by a Presidential proclamation on September 14, 1990. The TRQ replaces the restrictive quota system which had regulated the amount of sugar entering the United States since 1982. The U.S. quota was found to be in violation of GATT rules, following a complaint by Australia. The TRQ imposes a nominal or zero duty for import quantities up to a certain level, and a very high duty on imports above the first-tier level.

Technical barrier to trade — A specification which sets forth characteristics a product must meet in order to be imported. These characteristics include levels of quality, performance, or safety.

Terms of trade — The relationship over time between the price of a country's exports to the price of its imports. Terms of trade become more favorable as export prices received rise compared with import prices.

Threshold price — A term applied under the European Community's (EC) Common Agricultural Policy to a price fixed at the level that will bring the selling price of imported grains up to the level of the target price in the EC region with the least adequate supplies. The threshold price is equivalent to the target price minus transportation costs and is used to calculate the variable import levy on non-EC grains.

Trade barriers — Regulations used by governments to restrict imports from, and exports to, other countries. Examples include tariffs, nontariff barriers, embargoes, and import quotas.

Trade block — See free trade area.

Trade liberalization — A term which describes the complete or partial elimination of government policies or subsidies that adversely affect trade. The removal of trade-distorting policies may be done by one country (unilaterally) or by many (multilaterally). Proposals for agricultural trade liberalization submitted to the General Agreement on Tariffs and Trade in 1987 and 1988 varied in the policies included and the length of time for implementation. The initial U.S. proposal, for example, called for complete liberalization of agricultural trade by eliminating all policies affecting production, consumption, and trade in all counties over a 10-year period. The Cairns Group, in contrast, included only trade-distorting policies and provided for short-term trade reform measures, as well as intermediate and long-term actions.

Trade negotiations — See Multilateral trade negotiations.

Unfair trade practices — Actions by a government of firms that result in competitive advantages in international trade. Such actions include export subsidies, dumping, boycotts, or discriminatory shipping arrangements. Under Section 301, the President is required to take appropriate action, including retaliation, to obtain removal of policies or actions by a foreign government that violate an international agreement or are unjustifiable, unreasonable, or discriminatory and that burden or restrict U.S. commerce.

Uruguay Round — The most recent round of multilateral trade negotiations conducted under the General Agreement on Tariffs and Trade (GATT). The talks were launched in September 1986. Agriculture was included and negotiators focused on reducing the use of agricultural domestic and export subsidies, providing for greater market access, harmonizing sanitary and phytosanitary barriers, and strengthening the role of GATT in agricultural trade.

U.S. International Trade Commission (USITC) — An independent U.S. Government agency responsible for reviewing and making recommendations concern countervailing duty and antidumping petitions submitted by U.S. industries seeking relief from imports that benefit from unfair trade practices. The USITC was known as the U.S. Tariff Commission before its mandate was broadened by the Trade Act of 1974.

U.S. Trade Representative (USTR) — Cabinet-level head of the Office of the U.S. Trade Representative, the principal trade policy agency of the U.S. Government. The U.S. Trade Representative is also the chief U.S. delegate and negotiator at all major trade talks and negotiations.

Variable levies —The difference between the price of a foreign product at the port and the official price at which competitive imports can be sold. Such levies are effectively a variable tax on imports or a variable export subsidy. Variable levies are used by the European Community (EC), Austria, Sweden, and Switzerland.

Voluntary export agreement — An agreement between trading partners in which the exporting nation, in order to reduce trade friction, agrees to limit its `exports of a particular good. These agreements are generally undertaken to avoid action by the importing country against imports that may injure or in some way threaten the positions of domestic firms in the industry in question. Also called voluntary restraint agreement.