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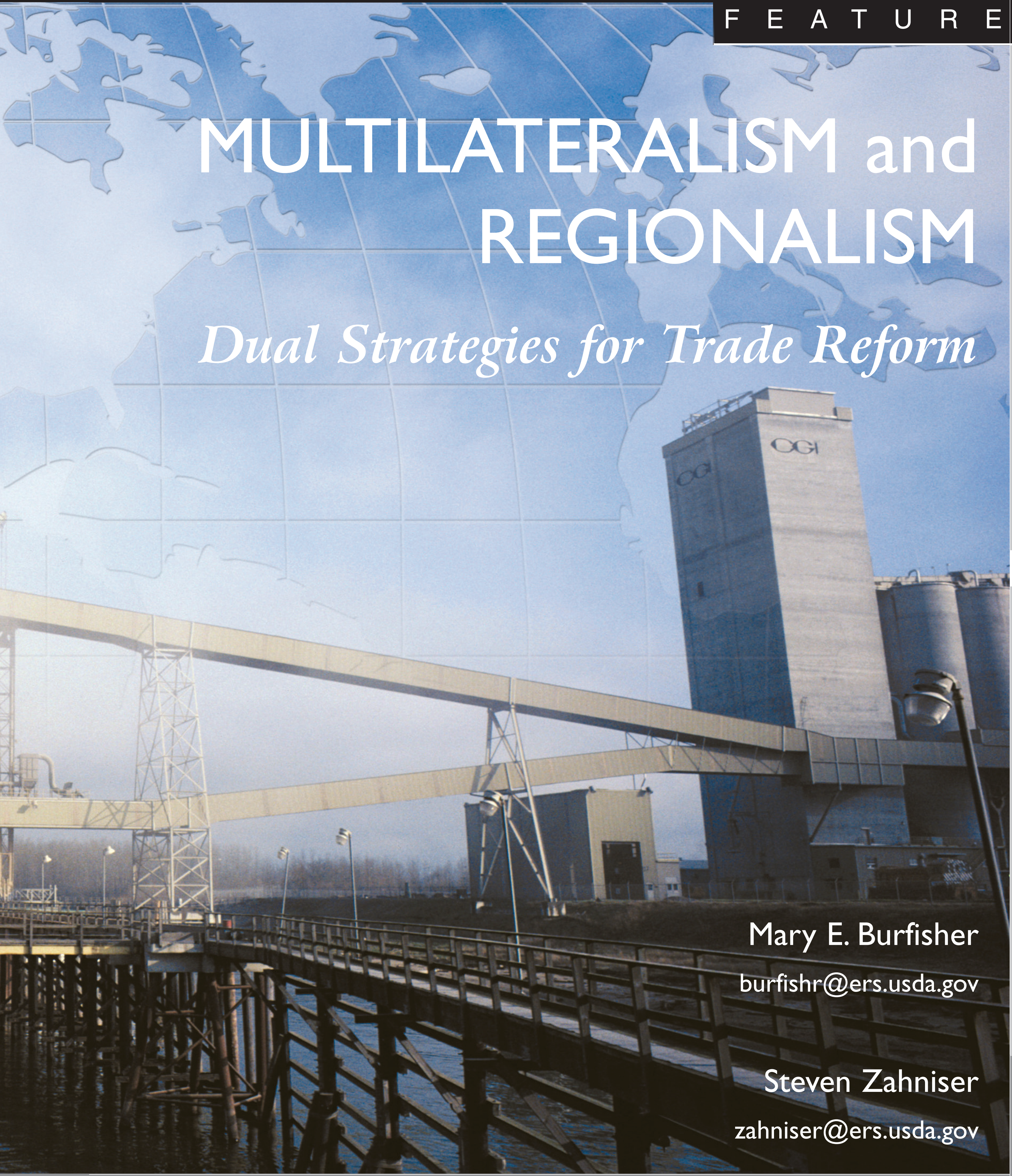

MULTILATERALISM and REGIONALISM

Dual Strategies for Trade Reform

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The United States is engaged in agricultural trade liberalization in two different types of venues. At the multilateral level, the U.S. is an active participant in the current round of world trade negotiations, called the Doha Development Agenda or Doha Round, at the World Trade Organization (WTO). The Doha Round opened in 2001 and is scheduled to conclude in 2005 (see box, "U.S. Proposal for Agricultural Reform in the Doha Round," p.29). At the regional level, the U.S. hopes to build upon the North American Free Trade Agreement (NAFTA) with Canada and Mexico by creating a Free Trade Area of the Americas (FTAA) that will include 34 countries in the Western Hemisphere. In addition, the U.S. has concluded free-trade negotiations with Chile and Singapore; is pursuing similar agreements with Morocco, Australia, Bahrain, and countries in Central America and Southern Africa; and has proposed an agreement with the countries of the Middle East (see box, "U.S. Engagement in Regional Trade Agreements").

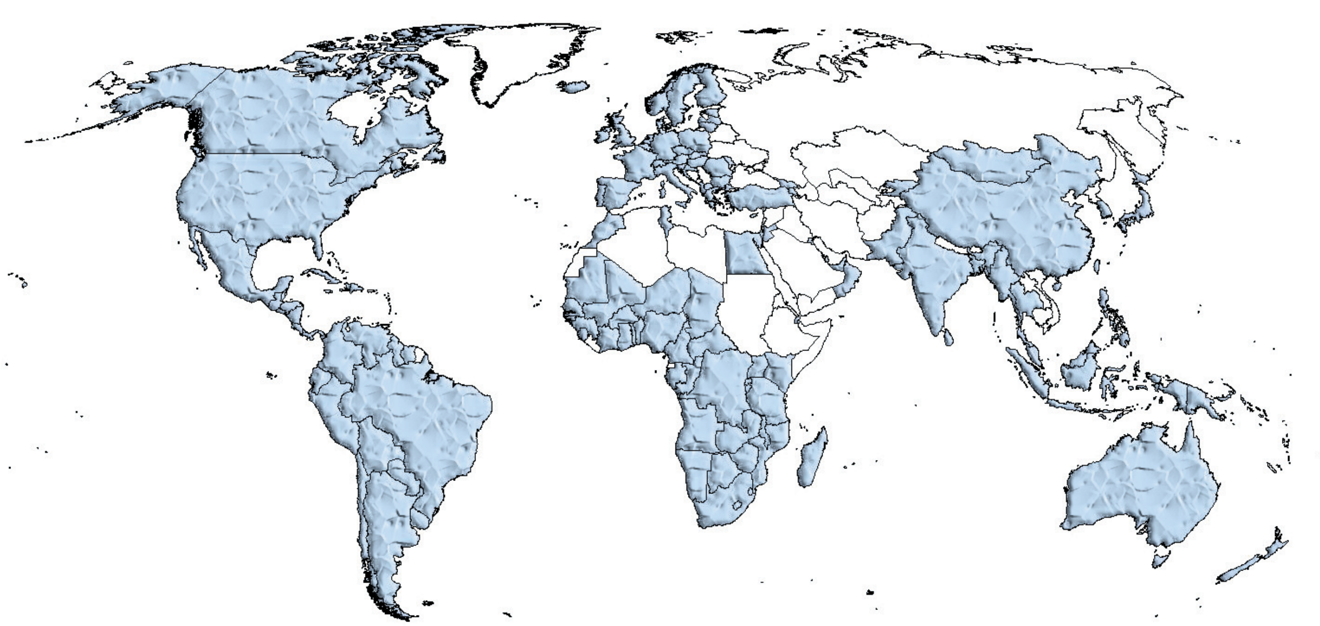
Why does the United States pursue both multilateralism and regionalism? This dual trade strategy is grounded in two fundamental ideas: (1) trade reform at either level is beneficial to the U.S. economy, and (2) each venue for trade liberalization offers unique opportunities. Multilateralism is clearly beneficial in that it engages virtually every country in the world in a mutual process of trade reform. In contrast, regional trade agreements (RTAs) are exclusive and discriminatory, but they are capable of much deeper trade reforms since their adherents are fewer, more like-minded and committed, and often linked geographically.

Importance of Trade Reform to U.S. Food and Agriculture

Roughly a quarter of the cash receipts of U.S. agricultural producers are derived from exports. Since expansion of the domestic market is largely constrained by the growth rate of the U.S. population, the international market has absorbed much of the growth in U.S. agricultural production over the past decade. From 1994 to 2001 (the latest year for which data are available), the value of exports consistently grew faster than total farm cash receipts. Imports now constitute about 9 percent of U.S. food consumption (versus 7 percent in the late 1980s), although this proportion varies greatly by product. Imports have enabled U.S. consumers to enjoy more varied food at a lower cost. U.S. food processors also benefit from international trade, since it enables them to access the most useful and cost-effective inputs available, further lowering the cost of food.

Because of trade's growing importance to U.S. agriculture, trade policy is becoming an increasingly critical part of a comprehensive U.S. farm policy. U.S. trade policy is directed toward trade liberalization. Whether through multilateralism or regionalism, the basic rationale for trade liberalization is essentially the same: Free markets allow countries to specialize in the production of goods in which they hold a comparative advantage. Moreover,

Members of the World Trade Organization (WTO)



Countries belonging to the WTO

U.S. Engagement in Regional Trade Agreements

Agreements and/or Members (in addition to the U.S.)	Status
Israel	Entered into force, 1985. Agricultural provisions subject to further negotiation.
Canada-U.S. Free Trade Agreement (CUSTA)	Entered into force, 1989.
Canada	Incorporated into NAFTA, 1994.
	Fully implemented, 1998.
North American Free Trade Agreement (NAFTA)	Entered into force, 1994.
Canada, Mexico	Full implementation scheduled, 2008.
Jordan	Entered into force, 2001.
Chile	Signed, 2003.
Singapore	Negotiations concluded.
Free Trade Area of the Americas (FTAA)	Negotiations underway.
Antigua and Barbuda, Argentina, Bahamas, Barbados, Belize, Bolivia, Brazil, Canada, Chile, Colombia, Costa Rica, Dominica, Dominican Republic, Ecuador, El Salvador, Grenada, Guatemala, Guyana, Haiti, Honduras, Jamaica, Mexico, Nicaragua, Panama, Paraguay, Peru, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Suriname, Trinidad and Tobago, Uruguay, and Venezuela	
Central American Free Trade Agreement (CAFTA)	Negotiations underway.
Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua	
Morocco	Negotiations underway.
Australia	Negotiations underway.
South Africa Free Trade Agreement (SACU)	Negotiations underway.
Botswana, Lesotho, Namibia, South Africa, and Swaziland	
Middle East region	Proposed.
Countries not yet specified	
Bahrain	Proposed.

by allowing firms to serve customers across several countries, trade liberalization can enable greater economies of scale and other efficiencies. The resulting production efficiencies lower costs and thereby increase the welfare, or purchasing power, of consumers.

Multilateralism: Broad Reforms With a Global Reach

The U.S. has backed multilateral trade reform since 1947, when it became one of 23 signatories to the General Agreement on Tariffs and Trade (GATT). Eight successive rounds of multilateral trade negotiations brought member countries together to negotiate the mutual reduction of tariffs and other trade barriers. Today, the GATT's successor organization, the WTO—which came into existence in 1995—boasts 146 members (as of April 2003). An additional 29 countries currently enjoy observer status, which obligates them to seek membership within 5 years.

Trade rounds under the GATT gradually lowered the average global tariff on manufactured goods to just 4 percent and helped to establish a rules-based global trading system. Trade rules that ensure predictability and fairness in trade relationships and contain a credible enforcement mechanism spur investment, promote the efficient conduct of business, and facilitate the expansion of trade and economic growth. While the first seven rounds of GATT negotiations did very little in the way of liberalizing agricultural trade, the Uruguay Round (1986-94) made three major contributions. It: (1) established upper limits on agricultural tariffs and converted nontariff barriers such as quotas to tariffs, capped at specified levels; (2) placed limits on the quantity and value of export subsidies; and (3) limited expenditures on the most distorting types of domestic agricultural subsidies, such as price supports and input subsidies.

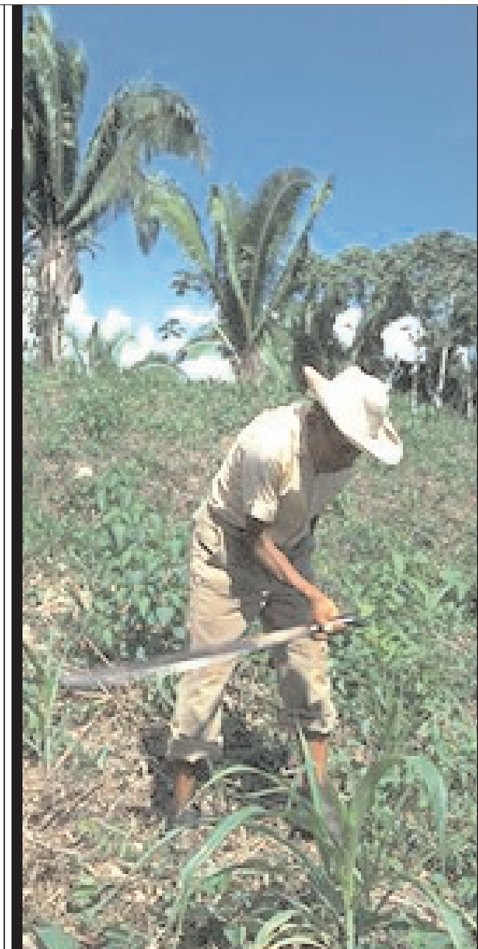


Photo by Franco Mattioli, IFAD

Despite this progress, significant distortions in agricultural policy persist in virtually all parts of the world. Economic modeling conducted by ERS indicates that present levels of global agricultural tariffs and subsidies depress world agricultural prices by about 12 percent and lower the volume of world agricultural trade by 15 percent. Further reductions in the amounts of agricultural tariffs and subsidies that are allowable under the WTO form one of the key challenges facing the Doha Round.

U.S. producers and consumers alike have much to gain from further multilateral trade liberalization. If the agricultural tariffs and subsidies in effect today were completely eliminated, the annual volume of U.S. agricultural exports would increase by about 20 percent, U.S. agricultural imports would rise by about 9 percent, and the U.S. agricultural terms of trade (the price of agricultural exports relative to agricultural imports) would improve. U.S. exports would account for much of the resulting expansion in world trade, mostly due to the fact that U.S. producers face high agricultural tariffs in foreign markets, with a global average of 60 percent. Consumers would benefit from the removal of U.S. agricultural tariffs, which average about 10 percent, as well as the effects of global tariff reform, which would increase agricultural production efficiencies around the world and lead to lower prices. Full agricultural policy reform would increase the purchasing power of U.S. consumers by about $13 billion annually.

Given the many benefits of multilateralism, why not pursue this trade strategy alone? The main strength of multilateral reform—its global reach—is also its primary weakness. Multilateralism requires reaching a consensus among a diverse, global membership that includes countries with different priorities and interests, as well as countries at different stages of development. This diversity of perspective and circumstance is particularly true of the multilateral agricultural negotiations, and it helps to account for the slow progress of these efforts. For many developing countries, the agricultural sector has a unique social and economic role as an engine for development and a source of income, employment, and security for a large share of their populations, including their most vulnerable citizens. To accommodate these special circumstances, developing countries have so far been allowed by the WTO to follow a more gradual schedule for agricultural policy reform than developed countries.

Regionalism: Deeper Reforms With Key Trade Partners

In an RTA, a relatively small number of countries agree to mutually reduce their barriers on each other's exports. At one time, RTAs were mostly established by geographic neighbors. Today, many RTAs encompass geographically distant countries, such as the U.S.-Jordan and EU-Mexico agreements, but the term "regionalism" is still commonly used. Over the past decade, there has been a rapid increase in the formation of RTAs. As of May 2003, over 180 such agreements were in force worldwide, over four times the level of a decade earlier, and at least 30 more are planned or under negotiation. Almost every country in the world has joined at least 1 RTA, and some have entered 20 or more.

Countries pursue regionalism for a number of reasons. Foremost, regionalism is a strategy to achieve comprehensive reforms with key trade partners. In the RTAs of the past decade, members have sought to implement deep economic and institutional integration by crafting agreements that address more than tariff reform. Many RTAs now deal with the reform or harmonization of regulatory practices, investment protection, labor issues, trade dispute resolution, and the development of common positions in other trade negotiation venues. Increasingly, RTAs are also viewed as a way to link developing and developed countries in a common project of economic development. By encouraging investment and locking in unilateral economic reforms, RTAs can facilitate productivity gains in participating developing countries and accelerate their economic growth.

Many developed countries offer nonreciprocal preferences as another way to foster exports by developing countries. Nonreciprocal preferences are arrangements between developed and developing countries that reduce tariffs or even allow duty-free access for selected products from developing countries. However, these arrangements often exclude products that are of the greatest importance to developing countries. In addition, nonreciprocal preferences do not require participating developing countries to adopt their own market access reforms. For these reasons, nonreciprocal preferences are now viewed by many as a less effective development tool, compared with RTAs.

Most of the RTAs that involve the United States have been successful in liberalizing agricultural trade. By 2008, NAFTA will have eliminated nearly all tariffs—agricultural and nonagricultural—among Canada, Mexico, and the United States. Although the U.S. free-trade agreement with Israel largely left agriculture as a subject to be negotiated later, the yet-to-be-ratified agreements with Chile and Singapore contain extensive agricultural provisions. In the Free Trade Area of the Americas (FTAA), now under negotiation, the United States has made an aggressive proposal for mutual agricultural trade liberalization. Every agricultural commodity would be included in trade reform, with tariffs to be eliminated immediately or within a specified transition period, depending on the state of development of the exporter.

Because the RTAs that involve the U.S. generally include agriculture, they have generated important benefits for U.S. farmers, ranchers, and consumers. Through extensive policy and economic analysis, ERS has identified NAFTA's impact in isolation from other factors. NAFTA has had a large proportionate impact on several U.S. agricultural exports, as measured by an estimated increase in trade of 15 percent or more, relative to what would have occurred without the agreement. These exports include beef and processed tomatoes destined for Canada, as well as cattle, dairy products, apples, and pears destined for Mexico. NAFTA has spurred a similarly large proportionate increase in several U.S. imports, including Canadian beef and Mexican sugar and peanuts.

NAFTA will be consolidated with the Western Hemisphere's other RTAs, resulting in a single, comprehensive trade pact, the FTAA. As a result, U.S. products will no longer have to compete against the trade preferences given by agreements in which the U.S. is not a member, such as the Common Market of the South (MERCOSUR). Also, the FTAA countries outside NAFTA will no longer have to compete against the preferences that Canada, Mexico, and the U.S. currently give to each other. U.S. exports of processed foods, dairy products, oils and fats, and rice are expected to benefit particularly, while horticultural products and processed foods (including sugar) are likely to see increased U.S. imports.

Despite regionalism's many benefits, there are many critics of this trade


Photo by Bill Tarpenning, USDA

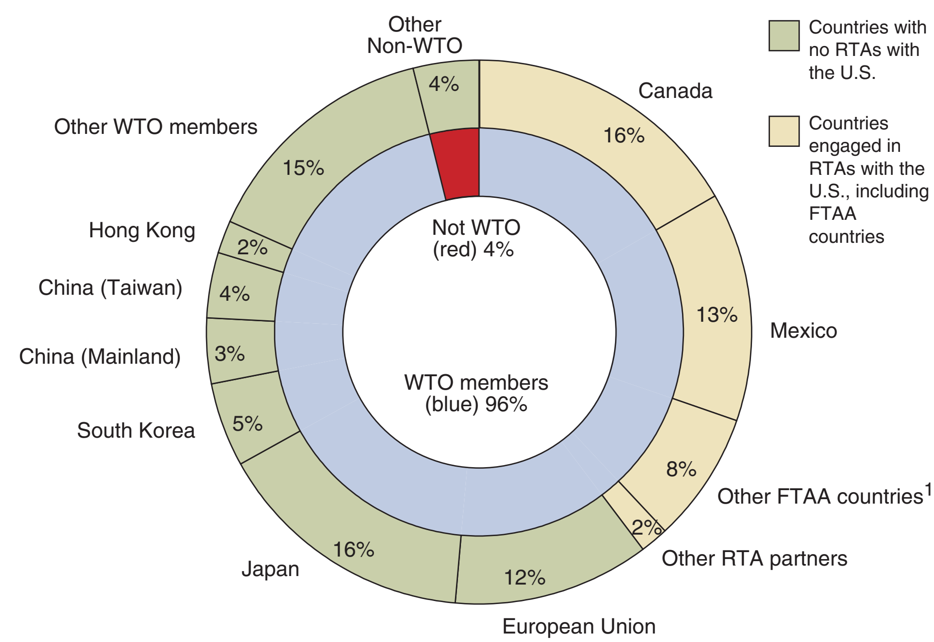
strategy. Perhaps the main reason for this criticism is the discriminatory nature of RTAs. By offering trade preferences to selected partners, they undermine a key principle of the GATT/WTO. Under the WTO's most-favored-nation principle, a country may not offer trade advantages to one country that it does not offer to all countries. Global trade rules grant an exception for the discriminatory preferences of RTAs, but only for those agreements that are on the whole trade-liberalizing.

RTAs can also be trade-diverting, as they can shift trade away from the lowest cost sources of imports and toward preferred trading partners. Trade diversion harms consumers in the importing country, and it can create or entrench special-interest groups that benefit from trade preferences and trade diversion. Trade diversion is more likely to occur when the RTA provides for selective, rather than comprehensive, liberalization or when the tariffs imposed by members on the rest of the world are very high.

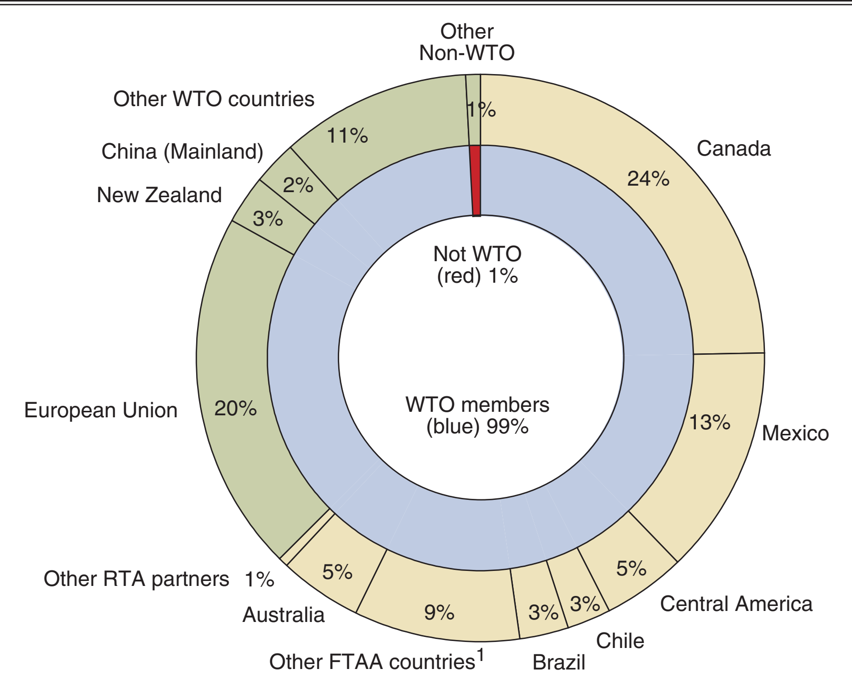
In addition, regionalism has a more limited geographical reach than multilateralism. For countries like the U.S., with widespread export markets, relatively modest reforms on a global basis can have larger trade impacts than deep reforms with a few trade partners. For example, the WTO signatories accounted for 96 percent of U.S. agricultural exports in 2002, while the countries that have either a current or proposed RTA with the U.S. accounted for just 39 percent. (Almost all the RTA partners of the U.S. are also WTO members.) Meanwhile, the WTO signatories supplied 99 percent of U.S. agricultural imports in 2002, compared with over 60 percent from RTA partners. For both exports and imports, Canada and Mexico were the two most important RTA partners in terms of their share of U.S. agricultural trade.

Finally, some types of agricultural policies have global dimensions that are

U.S. agricultural exports by destination, 2002 ($53.3 billion)



U.S. agricultural imports by origin, 2002 ($41.0 billion)



The outer circles classify all U.S. trading partners in terms of whether they are engaged in RTAs with the U.S. or not. The yellow portions of the outer circles include all the countries listed in the box on p. 25 ("U.S. Engagement in Regional Trade Agreements"), except for the Middle East region and Bahrain, as these agreements have not yet been defined clearly.

The inner circles classify those trading partners in terms of whether they are members of the WTO or not.

[1] The Bahamas is a member of the FTAA, but not a member of the WTO, although it has submitted a formal request for accession. It accounted for less than half a percent of U.S. agricultural exports and imports in 2002.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U.S. Proposal for Agricultural Reform in the Doha Round

The U.S. proposal to the Doha Development Agenda contains three key elements:

- To enhance export competition, the United States has proposed that export subsidies be phased out over a 5-year period, that export taxes on agricultural products be prohibited (with some exceptions for developing countries), and that rules be established to govern export credits and state-trading enterprises.
- To foster improvements in market access, the United States has proposed comprehensive and harmonizing tariff reductions, with a tariff-cutting formula that lowers high tariffs the most. Additionally, the United States has proposed a 20-percent expansion in tariff-rate quotas–the quantity of imports subject to lower, within-quota tariff rates–and that within-quota tariffs be eliminated altogether over a 5-year period.
- To reduce trade-distorting domestic support, the United States has proposed the adoption of a single category of trade-distorting support, with expenditures capped at no more than 5 percent of a country's total value of agricultural production, and agreement on a specific date for the elimination of all trade-distorting support. Examples of trade-distorting domestic support include price supports like marketing loan benefits and subsidies for fertilizer, seed, and other inputs. The U.S. proposal allows countries to pursue domestic policy objectives, including environmental protection and support for rural communities, as long as they do so in a manner that does not distort production or trade. It also offers special consideration to developing countries so that they may use supports essential to development.

not easily addressed at the regional level. For example, domestic agricultural subsidies are difficult to include in an RTA unless the signatories are willing to adopt a common agricultural policy, as in the EU example. Production subsidies influence a country's total trade, not just its trade with its RTA partners, and their negotiation in a regional forum is likely to reduce the leverage of RTA members in multilateral negotiations. Likewise, it is difficult for an RTA to address export subsidies. Although the use of subsidies by members among themselves could be limited, it would be hard to monitor subsidies offered to RTA members by outside countries, and it would be difficult to design compensatory measures to protect regional exporters.

Regionalism and Multilateralism: Mutually Reinforcing Strategies

Why then continue with RTAs? The current U.S. trade strategy for regionalism, called "competitive liberalization," treats regionalism and multilateralism as complementary and mutually reinforcing approaches to trade reform. By partnering with countries that are ready to liberalize their markets through an RTA, the U.S. hopes to motivate other countries to seek additional trade reforms at both the regional and multilateral levels. Moreover, RTAs have been linked to increased investment and productivity gains in developing economies. These favorable developments contribute over the long term to the economic growth and stability of our trade partners and directly support growth in the demand for U.S. exports.

Multilateralism, in which the entire membership of the WTO engages in a sustained process of mutual trade liberalization, remains the ultimate goal for trade reform because no member country is excluded from the process or confronted with discriminatory regional trade preferences and because some policies—such as domestic agricultural supports and export subsidies—are more effectively addressed in a global forum. While more elusive and gradual, continued progress in multilateral trade negotiations is critical to the world trading system. As regionalism becomes a larger and more embedded aspect of the international trading system, a sustained commitment to multilateralism can help to contain the potential divisiveness of regionalism while harnessing its energy for deeper and more rapid reforms. W

This article is drawn from. . .

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Effects of the North American Free Trade Agreement on U.S. Agriculture and the Rural Economy, edited by Steven Zahniser and John Link, USDA/ERS, WRS-0201, July 2002, available at: www.ers.usda.gov/publications/wrs0201