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AGRICULTURE

Tim Josling

The linkages between regional integration and agricultural trade strategy are of increasing interest to developing countries as they confront the challenge of opening up their economies to competition while mitigating the associated adjustment costs. Countries around the world have stepped up their efforts to establish regional preferential trade agreements (PTAs) and to coordinate trade relations with other regions. Agricultural trade is a core component of many of these trade initiatives, and a large part of the gains from regional integration depends on the inclusion of agricultural and food products in PTAs. Agricultural trade policy and regional integration agreements can together serve as instruments for accelerating growth and contributing to poverty alleviation.

Although the motivation for PTAs is often political, these agreements have significant implications for agriculture and other sectors of the economy. Many North-South agreements were concluded after a country gained independence, in order to maintain trading links developed in the colonial era—typically, for trade in raw materials and agricultural products. Other PTAs were instituted as part of the development of alliances and to bolster regimes that were under threat. Agricultural products often provided trade opportunities that reinforced such alliances. PTAs have long been used by developed countries to pursue overseas developmental objectives through the provision of preferential market access, often for primary products. Such access, however, has frequently been constrained when sensitive domestic agricultural products were involved.

More recent thinking has cast doubt on the longer-term benefits of PTAs, on the grounds that they tend to lock exporting countries into a particular pattern of exports, often of unprocessed raw materials and farm products, while competitors develop other markets and diversify their range of export products. A further problem, from the viewpoint of developing countries, has been that the terms of the PTAs are largely at the discretion of the preference-granting country, with little guarantee that the agreements will not be changed if they lose domestic political backing. This asymmetry also implies that the granting country can continue to extract from the preference-receiving partner political benefits such as support for economic and political positions.

The role of PTAs in agricultural development varies greatly, from strategic and deliberate to largely passive and reactive. Countries can choose to plan their agricultural strategies on a regional basis to take advantage of scale economies and overcome some of the constraints facing small national markets. Often, however, agriculture is brought into regional agreements through extraneous circumstances rather than careful planning; agriculture becomes one element in a broader set of complex trade-offs. PTAs often have an underlying rationale of contributing to increased regional cohesion and political integration, and the treatment of the agriculture sector becomes of interest, beyond strictly commercial considerations. Food security and the coordination of food policies and marketing infrastructure may be important reasons for the inclusion of a strong agricultural component in regional policies. Thus, the key issues in addressing agricultural trade in PTAs are whether regional integration promotes or hinders the development of a sustainable, competitive agriculture sector and whether agricultural trade considerations contribute to or detract from the benefits of regional integration.

This chapter attempts to put into perspective what we know and do not know about the economic impact of PTAs on agricultural development. The next section surveys the arguments for and against preferential trade integration as a development strategy for agriculture. These arguments relate, in general, to the effects of opening up

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trade among selected trade partners, as opposed to relying on either unilateral or multilateral actions. The rationales also cite possible economies in the joint production of public goods that benefit agriculture, ranging from research and extension to food security reserves. The second section then reviews what is known empirically about the impact of PTAs on agricultural trade. The third discusses some ways in which PTAs have dealt in practice with a set of problems that are commonly encountered when agriculture is included in PTA provisions. Both regional and bilateral PTAs are considered, as the agricultural problems differ somewhat in the two types of agreement.

Economics of Agricultural Trade in PTAs

In most respects, the economics of agricultural trade in PTAs is no different from the economics of nonagricultural trade. As with trade in nonfarm goods, agricultural trade in PTAs benefits from static gains related to expanded market access and from more dynamic gains related to the spread of ideas, innovations, and know-how (see Baldwin, ch. 3 in this volume).

Two important initial questions frame any agricultural trade strategy in PTAs: (a) how high are domestic (tariffs and nontariff) barriers relative to those of regional partners and other countries, and (b) how efficient are the export sectors within the region? If the region includes suppliers of agricultural products whose costs are lower than those of more distant exporters, then the regional strategy carries benefits similar to the unilateral or multilateral lowering of tariff barriers. Regional supplies can be integrated into a country's food policy, and ensuring access to those supplies will be an element in food security policy. The higher the existing tariffs (and other trade barriers) that restrict regional trade in these products, the greater will be the benefits of preferential liberalization to consumers. But this also implies greater disruption to domestic producers, who presumably have not had to face regional competition. When there are other products that could gain from the export opportunities that would open up with regional trade, a beneficial transfer of resources from the import-competing to the exporting agriculture sector may be possible. But if the agriculture sector in the regional partner is not efficient, the reduction in trade barriers may merely substitute a high-cost partner product for a more efficient third-country supply. Under these conditions, the advantages are likely to be small and the costs high.

These considerations need to be seen in a dynamic context. Inefficient agricultural suppliers could become low cost if their inefficiencies had been the consequence of limited markets and diseconomies of scale. The extent to which regional integration can provide the scale needed for such cost reductions depends on specific circumstances, but, in principle, the achievement of economies of scale can be a positive argument for regional integration. If the partner with the inefficient agriculture sector can make use of scale economies to become efficient, costs will decrease. But to treat PTAs as a nursery for potentially competitive sectors is controversial at best: the infant may become dependent on the protected market within the PTA and may not have an incentive to become competitive outside the area. Moreover, import-competing sectors will tend to shrink with regional integration and may lose some benefits of scale. Thus, the larger question is whether there is a possibility of a broad restructuring of the agriculture sectors of each of the PTA partners so that economies of scale can be exploited and resources redeployed to take advantage of regional (as opposed to national) cost advantages.

Fluctuations in output often mark agricultural markets, and trade is a vital means for offsetting the impact on available consumer supplies. The easier trade is, the less is the cost of market disruption to consumers. Greater regional food security is thus another plausible argument for integration of the regional partners' food supply network. All parties to a PTA that includes an open internal agricultural market will enjoy the advantages of more secure access to regional supplies. Even where weather and other related determinants of yield variations are regionally correlated, there can still be benefits from pooling risks. Storage facilities can be collectively operated, and regionally coherent transportation systems can improve distribution. There may, however, be a political cost because of loss of the ability to control domestic markets.

Agricultural trade in PTAs can benefit from some of the considerations of spatial or economic geography that apply to trade in goods. Some of these have to do with the provision of public goods, where the good concerned is valued (and underprovided) across local jurisdictions. More generally, both public and private sector actions can be expanded to a regional scale with advantage. Greater coordination of export strategies, more reliable supply chains for buyers, shared control over the quality and safety of exports, a better bargaining position with importers in other countries, and the possibilities for branding and labeling of regional products are all likely to result in expansion of export markets.

Preferential Agricultural Trade and Multilateral Commitments

As noted by Baldwin and Freund (ch. 6 in this volume), a key tension between bilateral or regional trade rules and

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multilateral trade rules arises from the latter's requirement that PTAs eliminate tariffs and other trade measures on "substantially all trade" and that the level of preference be 100 percent. (The multilateral rules in question are those of the General Agreement on Tariffs and Trade, or GATT, as now embodied in the World Trade Organization, or WTO.)[1] Although there has as yet been no agreement on the interpretation of "substantially all trade," agriculture is the sector most often excluded or treated differently; manufactures are far more likely to benefit from tariff reductions in PTAs than are agricultural goods (Fiorentino 2005). The prospect that competing exporters will challenge the exceptional treatment of agriculture in PTAs is remote, however, because these competitors tend to benefit from it. Exporters within the PTA have implicitly agreed to the exclusion and would be reluctant to challenge a partner with respect to mutually agreed decisions.

The requirement for movement toward full internal free trade (100 percent preference) has also been problematic. In some PTAs, partners gain an advantage from preferential tariffs but still face nonzero rates. Despite the inconsistency with GATT Article XXIV, several of these preferential tariff schemes have been permitted. As noted, there would be little outside interest in challenging such schemes, given that the lack of 100 percent preference works to the advantage of the excluded supplier.[2] The WTO requirement that the free trade area encompass "substantially all trade" (which, for most developing countries, includes agriculture) imposes costs on PTAs that include high-cost agriculture sectors. It may be therefore better in economic terms for such PTAs to exclude highly protected sectors, including agriculture.

The complementarity of preferential tariff reduction with multilateral trade developments can be part of a positive strategy for agriculture: the multilateral system could work to lower most favored nation (MFN) tariffs and reduce trade-distorting subsidies, making it easier and less costly to negotiate PTAs. The coordination of multilateral strategy among the regional partners also offers other possibilities for regional negotiating strategies and negotiating groups and opens an opportunity to develop strategies that combine regional and multilateral integration.[3]

There are indications that PTAs may be more successful than multilateral agreements in opening markets for agricultural goods. It often seems easier to fine-tune market access within discriminatory agreements, through selective inclusions. The European Union (EU) provides limited access for sensitive agricultural products to the many countries that have signed such agreements, including the Mediterranean countries, the African, Caribbean, and Pacific (ACP) countries, South Africa, and Mexico.[4] Within the North American Free Trade Agreement (NAFTA), the United States is moving toward a free internal agricultural market with Mexico and Canada, with few exceptions. More recently, the United States has negotiated agreements with Chile, Central America, the Dominican Republic, and Australia giving those countries preferred, although not free, access to U.S. markets. Less sensitive food products are also included in generalized system of preferences (GSP) schemes. Substantial amounts of agricultural trade thus do face barriers less restrictive than MFN tariffs. Presumably, much of this trade is diverted from lower-cost suppliers.

Yet the short-term market access gains from a PTA have to be weighed against the possible adverse effects on the multilateral trading system. Many of the problems that make the incorporation of agriculture in a PTA regime difficult also prevail in a multilateral context. A prominent issue in this regard is the extent to which disciplines on domestic farm subsidies can be included in PTAs. It is often assumed that the conduct of domestic policy is outside the realm of PTAs, but this is not always the case. The movement toward "decoupled" policies, encouraged by the WTO Agreement on Agriculture, has the advantage of making it easier to have free trade in a commodity and still maintain domestic support policies (box 7.1). Nevertheless, the existence of an active domestic support policy, involving subsidies and market management, complicates the negotiation of free trade in those products. If agricultural trade can be omitted from PTA provisions, the question of domestic support does not arise. Conversely, if agriculture cannot be excluded without violating WTO provisions, the potentially problematic issue of domestic support policies cannot be avoided.

The treatment of export subsidies in PTAs is similarly problematic. Various trade agreements include provisions that countries may not employ export subsidies in mutual trade. Although this sounds like a logical stipulation, it is not easy in practice to ban subsidies paid on internal trade without creating an incentive to import from outside and a disincentive to export within the PTA. In effect, export subsidies also have to be controlled at the WTO level.

The current Doha Round of WTO negotiations would, if successfully completed, make a significant difference to the ease with which agricultural trade could be opened up within PTAs. Under the provisions of the 2008 draft modalities, tariff levels for developed countries would decline by more than 50 percent for agricultural products, and tariff-rate quotas (TRQs) for sensitive commodities would be expanded. This would reduce both the degree of preference for partner suppliers (and hence the risk of trade diversion) and the adjustment for import-competing sectors. Given an agreed schedule of WTO tariff reductions,

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Box 7.1. The WTO Agreement on Agriculture

The Agreement on Agriculture entered into force with the establishment of the World Trade Organization (WTO) on January 1, 1995. The preamble to the document cites the agreed long-term objective of the Uruguay Round reform program: to establish a fair, market-oriented agricultural trading system. The program includes specific commitments to reduce support and protection in the areas of domestic and export subsidies and market access and through the establishment of strengthened and more operationally effective General Agreement on Tariffs and Trade (GATT) rules and disciplines. The Agreement on Agriculture also takes into account nontrade concerns, such as food security and the need to protect the environment, and it provides for special and differential treatment for developing countries, including an improvement in the opportunities and terms of access for agricultural products of particular export interest to these members.

In principle, all WTO agreements and understandings on trade in goods apply to agriculture. These include GATT (incorporated into the WTO agreements as GATT 1994) and WTO agreements on such matters as customs valuation, import licensing procedures, preshipment inspection, emergency safeguard measures, subsidies, and technical barriers to trade. Where there is any conflict between these agreements and the Agreement on Agriculture, the provisions of the latter prevail. The WTO General Agreement on Trade in Services (GATS) and the Trade-Related Aspects of Intellectual Property Rights (TRIPS) Agreement are also applicable to agriculture.

Source: WTO Agreements series: Agriculture.

the marginal impact of quicker reductions for regional or bilateral partners may be more tolerable. In addition, export subsidies would finally be eliminated—a step that has proved difficult to accomplish within PTAs. But the main contribution that the WTO negotiations on agriculture can make to the process of regional and bilateral trade liberalization may be to push countries to abandon price supports in domestic markets and embrace direct payments for public goods or for income relief. Such policies will be more compatible with PTAs, as well as beneficial for the multilateral trading system.

Because of the slow pace of the Doha Round negotiations on agriculture, regional negotiations may have to bear the brunt of attempts to further liberalize agricultural trade and to open access to new markets for agricultural exports. Thus, in agriculture there is a strong degree of complementarity in trade negotiations. Plurilateral agreements can erode market access barriers, but they can also foster less advantageous trade flows by discrimination among suppliers. Multilateral talks can reduce the scope for such trade diversion. The multilateral process can handle subsidy reduction, which, in turn, makes it easier for countries to agree to opening up regional or bilateral trade. This complementarity, however, depends on progress at the multilateral level. Currently, that is the stumbling block.

Economic Integration as an Agricultural Strategy

Is regionalism a better approach to agricultural trade policy than reliance on improved market access though the multilateral system? PTAs may be better than tariff reductions through the WTO at improving market access for the preferred partner with less threat to domestic agriculture sectors. Regional and bilateral PTAs, however, cannot deal effectively with agricultural export subsidies and domestic farm support, and so it is likely that the WTO will continue to be needed as a complement (Josling 2009). Meanwhile, regionalism poses problems for the multilateral system. PTAs may pick the easiest agriculture sectors to liberalize, leaving the most difficult products to the WTO. PTAs can also lead to investment in the "wrong" countries, just to get access to their agricultural markets. Moreover, too many simultaneous negotiations can overstretch resources. Some PTAs can be "strategic": an example is the efforts of the Southern Cone Common Market (Mercosur, or Mercado Común del Sur) to get the rest of South America into its camp before dealing with the United States and NAFTA. Some can be competitive, as when the EU and the United States compete for the Mercosur market. Such activities are likely to distract from the WTO, or they might distort the multilateral nature of the Doha Round.

These issues have been discussed in the literature of trade strategy. Analyses by Zissimos and Vines (2000) and by Andriamananjara (2002) suggest that joining a PTA can be the best "safe-haven" strategy when other countries are also doing so. But this does not imply that the end result is one large free trade area, given that PTA membership confers a terms-of-trade gain on members at the expense of nonmembers. Some members, at least, will be better off limiting PTA membership than allowing expansion to cover the world as a whole. The effect is similar to that suggested by the domino theory of the dynamics of regional trade blocs (see Baldwin, ch. 3 in this volume). As PTAs expand, the attraction of being within the bloc (or the cost of being outside) increases, but the marginal gain to existing members

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of adding one more (small) market to the bloc, and the extra administrative and political cost of a large membership, will act as a brake. The implication is that each such agreement will tend to find its equilibrium size, where the costs and benefits of enlargement are in balance.[5]

So, is the pursuit of PTAs a short-term or a long-term strategy in agricultural liberalization? Pursuing bilateral North-South PTA arrangements at the regional level may lead to short-term benefits of access to agricultural markets for participating developing countries. But developing countries should be aware that preferential access is likely to be eroded as more countries sign such deals, reducing the value of preferences (García-Alvarez-Coque 2002). For PTAs to be beneficial in the longer term, governments and stakeholders should implement a set of reforms to help sustain the growth of domestic agriculture and reduce the poverty of the agricultural population.

As noted, this type of discriminatory trade agreement has both positive and negative aspects. On the positive side is the ease of reaching an agreement among a small group of adjacent countries. Often, the countries involved will share historical and social perspectives on trade and agriculture. But this ease of reaching agreement comes at a cost. PTAs tend to "cherry-pick" the easiest trade areas in which to conclude a deal, leaving the more difficult ones to the WTO. The ease of reaching an agreement may reflect the willingness of the parties to avoid hard decisions by excluding sensitive sectors such as agriculture from the deal.

Those PTAs that have been most effective in opening up agricultural markets have tended to include as members major agricultural exporters that see the advantages of expanding markets. Countries that are mainly importers of farm products are less likely to agree to open up markets, and hence the benefits to the sector may be small.

In PTAs among members in different regions, the temptation to exclude sensitive sectors of agriculture is even greater, as there is less probability that the deal will include provisions of benefit to agricultural export interests. Given that bilateral PTAs often involve countries which are not geographically close, there is often an opportunity to negotiate with a country with a complementary agricultural pattern, to take advantage of trade opportunities. In practice, this often works in reverse, as countries cherry-pick partners so as to avoid conflicts over agriculture. The existence of political tensions in trade agreements usually indicates potential economic benefits that could be realized from changes in trade patterns.

The positive and negative aspects of PTAs are compounded by the apparent advantage that nonreciprocal preferences give to the recipient country relative to others. But overall, the limiting factors mentioned above, together with the restrictive rules of origin for many processed products, have severely limited the role of trade preferences in encouraging agricultural diversification in developing countries.

Tariffs introduce a wedge between the world price of a product and the price on the domestic market. Trade preferences allow products from the beneficiary country to enter the partner country with lower import duties than are applied to other countries' products under the partner country's MFN tariffs and hence capture some of the wedge. They give suppliers in beneficiary developing countries access to part or all of the price premium that normally accrues to the importing country government as tariff revenue. The acquisition of these rents raises returns in the developing country and, depending on the nature of competition in domestic product and factor markets, stimulates expansion of the activity concerned, with implications for wages and employment.

Developing countries, especially the least developed countries (LDCs), face much higher trade-related costs than other countries in getting their products into international markets. Some of these costs may reflect institutional problems within the countries themselves, such as inefficient practices and corruption, and these require a domestic policy response. But some reflect weak transportation infrastructure and firms' lack of access to standard trade-facilitating measures such as insurance and trade finance.

Empirical Evidence on Agricultural Trade and PTAs

What might a theoretical approach to the issue of agricultural trade and regional agreements suggest? Would one expect the proliferation of PTAs to have brought about trade expansion in agricultural products? In his analysis of the economic impact of regional integration on agricultural trade, Goto (1997) concludes that the higher the level of preintegration protection, and the lower the degree of product differentiation, the greater the impact of regional integration. He hypothesizes that "regionalism has more [of an impact] on agricultural trade than on manufacturing [trade], because the initial level of protection is higher and the degree of product differentiation is lower for agricultural products." On the basis of this theoretical conclusion, PTAs could be expected to have a significant role in agricultural liberalization, and this hypothesis will be explored in the brief review of the empirical literature that follows.

The literature on agricultural trade issues in PTAs is thin and scattered, and there is very little by way of detailed

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and comparative analyses of the arrangements made for agriculture in regional PTAs. Bilateral PTAs are somewhat better documented, as they tend to be focused on a more limited number of products, and the trade flows and conditions of market access are watched closely by the domestic sectors concerned. Unilateral preferences are again the subject of study, in part because of their dependence on periodic renewal and in part because of their direct impact on competing suppliers. An example of a case for which there is adequate information and several empirical analyses would be the EU's regime for bananas, where the WTO case has brought much transparency to the way in which the ACP countries sell their bananas to Europe and to the marketing choices of the excluded suppliers. Sugar sales to the United States and the EU under PTAs have also been closely analyzed, and adequate data exist for calculating the effects of such trade arrangements.

Absent such comprehensive and detailed studies dealing with the amount and type of agricultural products traded within PTAs, the assessment of the costs and benefits of agricultural trade in PTAs has tended to rely on more conceptual studies. These studies can be grouped by their focus on one of three questions:

- Has regional trade increased faster than trade with third countries?
- Does the existence of PTAs explain trade flows among the partners in such agreements?
- What are the gains and losses from participation in regional or bilateral PTAs?

The first group of studies essentially consists of explorations of the extent to which world trade is becoming more or less regionalized. It is difficult to derive direct implications from the outcome of such studies because regional trade could well increase rapidly even in the absence of regional agreements. The nature of agricultural and food trade itself is changing over time, and the goods and services that are traded across continents may vary with the regional composition of trade. But it is still useful to have these studies as a way of putting the regionalization of agricultural trade policy in context.

The second group of studies generally involves ex post explanations of trade flows. The most commonly used technique is a gravity model. By inserting dummy variables for the existence of PTAs in regression equations, this method aims to determine the significance of such trade policies in the explanation of trade flows. Agricultural trade flows can be isolated in these studies, and the importance of the trade policy for agriculture can be determined. One application has been to look at the implications of health and safety regulations for regional trade. These models do not evaluate the trade policies themselves and cannot indicate whether a particular trade strategy is desirable.

The third group of studies consists of ex ante evaluations of prospective agreements. These studies often use computable general equilibrium (CGE) models to calculate trade flows and the welfare implications of policies. Most of the few studies that focus on agriculture take a similar approach, analyzing the significance of trade agreements for agricultural trade.

Each of the three sets of studies has strengths and weaknesses. The study findings are reviewed below, and issues of relevance to the specific question of the empirical evaluation of trade preferences are then addressed.

Regional Trade Flows

The steady growth in world trade in relation to world output is seen as an indicator of the success of the multilateral trade rules put in place by the GATT and reinforced by the WTO. The assumption has been that the elimination of trade barriers and the extension of trade rules have stimulated trade flows. But has trade tended to be concentrated among regions? The literature (e.g., Lloyd 1992; Anderson and Blackhurst 1993) tentatively concludes that the trading system has not developed into a series of intensively trading blocs, with decreased interbloc trade.[6] Trade among blocs remained resilient, despite the burst of "regionalism" in trade policy that characterized the decade from 1985 to 1995. Nevertheless, evidence of increased intrabloc trade has been a widespread, if not a dominant, feature of the trading system.

Several studies find that intraregional trade in agricultural and food products grew during the 1980s and 1990s (Vollrath 1998; dell'Aquila and Kuiper 2003). With regard to the effects of particular trade blocs, Diao, Roe, and Somwaru (1999) find that, on average, agricultural trade under NAFTA, the European Union (then consisting of 15 countries), Mercosur, and Asia-Pacific Economic Cooperation (APEC) grew more rapidly than did total world agricultural trade.[7] In particular, growth in intraregional agricultural trade exceeded the growth in extraregional agricultural trade for these PTAs.

Trade Flows and Preferences

A PTA increases trade among members through preferential treatment. The question is whether that growth comes at the expense of the rest of the world. Despite a number of theoretical and empirical contributions in recent years, the

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effects of PTAs on trade in agrifood products have not been evident from the literature because most of the studies have dealt with merchandise trade. It remained for some time an open empirical question, to what extent agrifood trade among PTA partners has increased and how much of the increase could be attributed to trade diversion.

Recently researchers have tried to answer this question but have come to mixed conclusions. Jayasinghe and Sarker (2008) analyzed NAFTA's trade creation and trade diversion effects on trade in six selected agrifood products from 1985 to 2000. The results show that the share of intraregional trade within NAFTA is growing and that NAFTA has displaced trade with the rest of the world. Countries participating in NAFTA have moved toward a diminished degree of relative openness in their agrifood trade with the rest of the world. Grant and Hertel (2005), however, find, with only a few commodity exceptions, that PTAs have increased trade with nonmembers even as members have increased trade among themselves. As these examples show, the impact of PTAs on agriculture varies among regions and among agricultural products.

Evaluating Trade Preferences

A major problem with the standard databases on tariff levels is that they rarely incorporate preferential tariffs. Given the amount of world trade that enters countries under preferential (or zero) tariffs, the picture of market access presented in these databases is misleading. This omission is gradually being rectified; one notable advance has been the development by the French research organization Centre d'Études Prospectives et d'Informations Internationales (CEPII) of a database that includes full information on the preferential tariffs accorded developing countries. Analysis of the extent to which PTAs promote the development of agriculture by opening up markets remains difficult but is now subject to empirical exploration.

Trade preferences, both reciprocal and nonreciprocal, can provide the premium over the normal rate of return that is required to encourage investment in developing economies. The increase in agricultural trade attributable to preferences leads to more output and, if there are scale economies, to lower costs, stimulating further trade. Thus, the search for preferential access to foreign markets is naturally a component of national trade policy. The degree of preference, however, can be fleeting if others are also negotiating market access. The benefits may be those of the first mover and can be eroded steadily over time.

The granting of trade preferences is also a policy decision subject to evaluation. The key question is whether the partner receiving the preference is able or likely to be able to meet import requirements at a reasonable cost. Lowering tariffs against third countries, even if done unilaterally, is a strategy that would minimize the cost of giving preference to high-cost imports. Making exceptions for tariff-free access for high-cost partner supplies would seem less desirable. Too stringent rules of origin will also add to the possibility of trade diversion because it will discourage processing of third-country raw materials in the partner country.

The main drawback to relying on preferences for export products for agricultural development is the effect on the pattern of domestic agricultural production. A few export commodities will benefit from preferences, but this will set the economic context for other products that have to compete for land and labor. In addition, the guarantee of access under unilateral preference schemes may be a Faustian bargain, as the supplying economy becomes more dependent over time on the continuation of the preference margin. Preferences can create a degree of dependence that constrains flexibility and diversification and results in high-cost production of preferred products (Topp 2001). Moreover, other countries will have an interest in reducing those preference margins over time. The most highly protected products have the highest potential margins of preference, but these are also the products that are likely to lose the most protection through WTO negotiations.

Many preferences are, in any case, quantity constrained. When preferences are granted on products for which domestic prices in industrial countries are much higher than world prices, such as sugar in the EU and the United States, quantities are limited, to avoid undermining the distortionary policies that generate the large divergence between domestic and world prices. In these instances, preferential access can lead to substantial gains for preferred suppliers but little hope of market expansion, and high probability that the gains will be eroded.

In addition, some of the preference rents may not be available for development. How much of the available rent is actually obtained by suppliers in developing countries depends on the nature of competition in the industry and the regulations governing the granting of preferential access, among other factors. If there is little effective competition among buyers, exporters may be unable to capture much of the price premium. Olarreaga and Özden (2005) find that only a third of the available rents for African exports of clothing to the United States under the African Growth and Opportunity Act (AGOA) actually accrue to exporters. Furthermore, satisfying the rules governing preferences raises costs and reduces the extent to which the preferences increase actual returns. The costs of satisfying the rules of origin (ROOs) in preference schemes have

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been cited as a major reason for low rates of utilization of preferential access in some cases (UNCTAD 2001; Brenton and Ikezuki 2005).

Tariff preferences can lead to other adverse effects that need to be taken into account. Negotiations in the Doha Round have shown that existing preferences can lead to support for highly protectionist policies in industrial countries and can weaken proposals that would substantially reduce such levels of protection. This not only causes a rift among developing-country negotiating positions but also perpetuates policies that depress world markets and reinforce dependence on preferences for export revenue.

Differences and inconsistencies between preference schemes can prevent developing-country suppliers from evolving global market strategies. Furthermore, the preference schemes may not be directly consistent with poverty reduction objectives: beneficiaries of trade preferences are not always the poorest constituents in developing countries. Although rents do accrue to the developing country, they will tend to benefit the owners of the most intensively used and the most limiting factors.

Relatively few studies have directly measured the value of preferences. The value depends on the difference in returns in different markets. The rents accrue to the holder of the preference, but those rents are usually subject to the trade policy of the preference-giving country. A recent example of this view of preferences is given in Paggi, Yamazaki, and Josling (2005): the value of improved access to Central American markets by U.S. exporters as a result of the Central America Free Trade Agreement (CAFTA) and its extension to the Dominican Republic (CAFTA–DR) depends on who else has such preferences in those markets and how long any advantage over other competitors will last. The United States competes with the Mercosur countries and with the EU in Central American agricultural markets, and evaluation of the value of CAFTA for U.S. exporters is as much a function of the state of trade relations among these other countries as of the details of CAFTA as such.[8]

One problem with calculating the value of regional and bilateral preferences in agriculture is that the models traditionally used do not adapt well to such questions. The study of trade flows and the impact of regionalism may not capture the strategic and dynamic aspects of PTAs. A country contemplating joining a PTA does not need to know whether that PTA has been trade creating or trade diverting; the issue is whether acceding to the agreement creates beneficial trade flows, either from better market access or from reliable low-cost imports. In the case of a customs union, the height of the common tariff holds the key—for some countries, accession will lead toward liberalization, whereas for others, it will be a move toward greater protection.

Gravity models and other models that seek to "explain" trade flows are of limited use in evaluating the value of preferences. Ex post analysis of why trade has taken place does not answer the fundamental question of whether differentiating one's own tariff schedule in exchange for similar differentiation by others is beneficial. If the gravity model identifies "natural" trade partners, then the question is, why is that natural trade, based on proximity and income, not taking place already? The answer could be that the trade policy of the partner country precludes such trade, but many other explanations could intrude. And the "best" trade partners may well be on other continents. So, gravity models are an interesting way of looking at trade patterns, but a shaky guide to policy action.

CGE models also have drawbacks for the evaluation of preferences, although they do address the key issue of the economic benefits and costs. The difficulties stem from whether the situation to be analyzed can be specified in enough detail. The trade policy question may require knowledge of particular market conditions, such as quality and production cost. The device of assuming that each country produces a somewhat different version of traded products masks the question of whether and how such differentiation can be created and exploited. An exporter will ask, "What are the regional markets that can open up for my product, and how can I adjust to meet the market requirements?" The CGE model will reply that the relevant substitution elasticity is already in the model and is not a part of the policy space.

This, then, is the dilemma facing analysts in this area. Every PTA is different, in its coverage and treatment of products. Moreover, members' motivations and interests can differ widely, making the overall analysis of the agreement of limited use to individual countries. And within each country, the calculation of costs and benefits will be specific to conditions in particular sectors. In brief, the task of analyzing any particular decision for a country on the basis of the benefits to be gained from a trade agreement is heavily data intensive, context specific, and time related. It is not surprising that the models do not produce satisfying answers to such questions.

Does this mean that the study of PTAs and their variations is pointless? Clearly, one needs to continue to evaluate the overall impact of a fragmentation of the rule system in world trade and the ways in which regional and multilateral trade can coexist and become more complementary. But in addition to that work, there is considerable scope for focusing on the practical issues of decision making in the area of trade policy. Such work would help countries—in

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particular, those with limited internal analytical capacity—face the challenges of the day.

The Practice of Agricultural Trade in PTAs

Regional PTAs have the capacity to develop strong regional agricultural systems, but the path may be politically difficult. Bilateral PTAs are free of the problem of regional competition but often have issues with the liberalization of trade in particular products, where there may be links between the two economies concerned. Regional PTAs are considered first because most of the difficult questions surrounding the incorporation of agriculture arise in these cases. The EU, the European Free Trade Association (EFTA), NAFTA, and Mercosur provide rich examples of the ways in which the issues have been tackled. The recent growth of bilateral PTAs across regions offers many other cases of the treatment of agriculture. In particular, the bilateral PTAs negotiated with the EU and with the United States represent (different) standards for the way in which developing countries can seek to gain secure market access in major developed-country markets. These bilateral agreements tend to be "lighter" in the area of agricultural policy, avoiding the problems that accompany the development of regional agricultural and food markets (Josling 2009).

Agricultural Provisions in Regional PTAs

The inclusion of agricultural trade in a regional PTA is a challenge for negotiators. Relatively high levels of protection in agricultural markets, combined with a heightened sensitivity to issues bearing on the maintenance of a domestic production base for staple foods, makes for tensions. Countries in the same region are likely to have similar production patterns. Where there has been a history of agricultural trade among the countries, the tensions may be a minor political problem, but in many cases, trade with neighbors in a regional group may raise major concerns.

Some PTAs have chosen to omit agriculture from their provisions. EFTA was created in 1960 by seven countries that had opted out of the European Economic Community (EEC, the precursor of the EU). Several members (Austria, Finland, Sweden, and Switzerland) had high-cost farming sectors because of climate or topography and did not wish to compete directly with the United Kingdom or Denmark. EFTA accordingly chose to exclude agriculture (and fisheries) from the free trade provisions. Each country was able to maintain its own agricultural policy through tariff provisions and domestic support.[9]

The decision to leave agriculture and fisheries out of the EFTA agreement led to the exclusion of the sector from the terms of the European Economic Area (EEA), the set of bilateral PTAs that the EU negotiated with EFTA members as a way of keeping them close to the EU in terms of economic regulation and price levels. The EEA allowed for free trade in manufactured goods and cooperation in regulatory issues. In effect, it extended the previous bilateral PTAs to several aspects of trade that had been incorporated into the 1992 Single Market of the EU. Although some quotas on agricultural goods were expanded, there was no progress toward incorporation of the rural sector into economic integration, as would be stimulated by enlargement. Later, EFTA countries found themselves unable to include agriculture in bilateral agreements that they negotiated with countries such as Canada and had to settle again for small bilateral trade deals.

At the other extreme, the countries that formed the EEC (later, the European Union) made a conscious decision to include all trade, including agriculture, in their trade liberalization. As integration progressed, more internal agricultural trade took place, some of it displacing lower-cost imports. In addition, the agricultural market became more integrated as firms were able to locate in other member states, and a European food industry began to emerge. The development of a Common Agricultural Policy (CAP), with common financing and uniform support mechanisms, advanced farther in the EU than in other PTAs. More recently, harmonized regulations on food safety and quality controls have reinforced the development of a regional industry.

The polar cases of EFTA and the EU bracket the degree of incorporation of agriculture in PTAs. Almost all other PTAs have included agricultural trade in the liberalization process, to varying degrees. The agricultural content of the PTAs can be explored by identifying some issues that arise in most cases. These categories are not confined to agricultural trade, but they do form a set of negotiating issues that frame the agricultural agenda. They include the schedule for cutting tariffs and the use of TRQs as a way of increasing access; safeguards against import surges; subsidies to domestic firms and to firms dependent on exports; the provision of public goods, both environmental and related to food security; and market structures and institutions.

Tariff cutting. Elimination of tariffs among partners is the defining feature of a PTA, and the inclusion of agricultural tariff lines in the reduction schedules is a key decision. For some products, the tariff cuts are made at the time the PTA enters into force; for others, a schedule of reductions is agreed. Agricultural tariff cuts, at least for sensitive

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products, are usually introduced over time. The timetable for liberalization in NAFTA provides an example.

NAFTA set in process the removal of all trade barriers to goods moving between countries in North America. The detailed market access provisions were embedded in three bilateral agreements, of which the one between the United States and Canada essentially continued a previous bilateral agreement. For the U.S.–Mexico bilateral agreement, the time period for most sectors to achieve market integration was 10 years, but markets for some sensitive agricultural products (beans and corn for Mexico, and tomatoes and citrus products for the United States) were given 15 years to adjust. The adjustment period has ended, and the U.S.–Mexico agricultural market is now effectively open.[10]

Another success in removing tariff barriers on trade in farm products has been in the Australia–New Zealand regional market.[11] The Australia–New Zealand Closer Economic Relations Trade Agreement (ANZCERTA) takes the two countries farther toward effective market integration than does NAFTA in North America, although by no means as far as the EU. Both countries are major agricultural exporters. The product mix of exports is somewhat similar, reducing the scope for trans-Tasman trade, but there are natural trade flows based on climatic differences, such as sales of Australian wheat to New Zealand and exports of New Zealand dairy goods to Australia. These flows were hampered by tight restrictions on trade within domestic marketing legislation. It took bold political decisions, coupled with a significant reduction in the power of the marketing agencies, to allow trade in agricultural products to flow freely.

In most respects, tariff cutting in agricultural markets has been successful in Latin American PTAs. Among Mercosur countries, agricultural trade is nominally free; indeed, agricultural products are widely traded among the member states, notably from Argentina to the others. Mercosur has relatively few provisions that apply specifically to agriculture. There are two likely reasons for this relatively liberal treatment of the sector. First, Mercosur includes major exporters of temperate agricultural products, each of which would like to strengthen its agriculture industry and promote regional exports. Second, as a result of sweeping structural reforms, the countries concerned have eliminated many of the state marketing monopolies that previously controlled trade.[12] This, together with the reduction of subsidies and support prices, has allowed a fuller incorporation of agriculture within Mercosur than in many other PTAs.

Safeguards. As a complement to tariff cutting, PTAs frequently include safeguards that allow temporary increases in tariffs should imports surge. Agricultural products in PTAs are often subject to specific safeguard provisions to help guard against sudden shifts in trade patterns. The nature of the safeguards for agriculture is usually in the form of a "snapback" to a previous tariff, no higher than the MFN tariff rate, for a limited period of time. Similar provisions in NAFTA were used on several occasions during the transition period to react to trade surges. Countries generally reserve the right to take action under WTO safeguard provisions, although not in addition to regional safeguards. The EU is again an exception; its regulations prohibit safeguard action against trade from another member state.

Domestic and export subsidies. The thorny issue of domestic subsidies in PTAs has been dealt with in two different ways. Generally, the decision is made in negotiations not to attempt any constraints on subsidies. Indeed, it is usually assumed that PTAs could not regulate domestic subsidies because to do so on inter-PTA trade but not on extra-PTA sales would be impractical at best and self-defeating at worst. The emphasis in several PTAs is, accordingly, on acknowledging the multilateral process as the location of decisions on subsidy reduction. Hence, NAFTA contains the injunction to "endeavor to work towards domestic support measures" that have minimal trade-distorting effects or that would be exempt under a future GATT agreement (the so-called "green box" policy instruments). It recognizes, however, the right of parties to change domestic support measures subject to GATT obligations. This light treatment of a contentious area enabled negotiators to say that they were not altering domestic policy.

The EU took a different tack. All subsidies by member states are constrained by the competition regulations of the EU, and farm subsidies are not excluded from this provision. The CAP became (in principle) the only vehicle for granting agricultural subsidies, although some exceptions have survived the attempts by the European Commission to enforce this regulation. One result of the common nature of the CAP has been that the EU can negotiate reductions in domestic support as a single WTO member, which individual members of other PTAs are not in a position to do.

Export subsidies for agricultural products pose similar issues. Several PTAs have contemplated banning export subsidies on intrabloc trade, but this is easier said than done. The NAFTA provisions again give a good example of the dilemma facing PTA negotiators. The text states that parties "share the objective of the multilateral elimination of export subsidies for agricultural goods" and promises cooperation in the GATT to this end. The zeal for multilateral elimination of such policies does not, however, extend

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to their internal use. Article 705.2 of NAFTA merely holds it "inappropriate" for a party to grant export subsidies on sales to another party unless the importing country is benefiting from export subsidies paid by other countries.[13] In other words, matching of EU export subsidies in Mexico is allowable by the United States and Canada until such practices are stopped multilaterally. Indeed, if the exporting and importing parties agree to an export subsidy on intra-NAFTA trade, that subsidy is allowed. This provision, no doubt, was included to take account of the considerable importance to the United States of retaining the means to stay competitive with EU export subsidies in the Mexican market.

PTA discussions about the impact of different marketing structures and institutions raise some interesting issues. This is particularly true for state marketing institutions in agricultural products, where historical differences in policies can lead to problems for integration. An early example was the difficulty posed for the EU at the time of U.K. accession (1973) by the existence in England and Wales of the Milk Marketing Board (MMB), which held a monopoly on milk sales and on imports of milk products. This situation was clearly inconsistent with the competition regulations of the EU, and so the MMB had to change its policies and give up its control over the milk market. A more recent example appears in the 1986 U.S.–Canada free trade agreement. Canada was able to exclude from the free trade provisions the products of its supply-managed sectors, primarily dairy and poultry, which were managed largely by provincial marketing boards. Neither the United States nor Canada wished to face the task of harmonizing marketing systems for these products, and it was felt that the operation of the boards required control of all imports, including those from the United States. As a result, the integration of these sectors was delayed indefinitely.

Public goods. It is widely recognized that agriculture provides certain public goods (as well as negative externalities in the way of water and soil pollution). In rich countries, these public goods are often identified as the stewardship of the landscape and the provision of locally grown healthy foods; in less affluent societies, the benefits are food security, rural development, and poverty alleviation. Whether society is adequately compensating the farm sector for the provision of these public goods is a subject of debate in many countries. The collective provision of a public good within a PTA can sometimes be advantageous, in particular where agricultural and environmental conditions are defined more by geography and climate than by political boundaries. Similarly, coordination of rural infrastructure within a regional PTA could form the basis for improvement of the economic capacity of an agricultural area.

One particular public good associated with agriculture deserves separate mention. Food security refers to the ability of a country to provide the conditions under which food is available to (and relatively affordable by) the population. Economic, social, and political imperatives converge here. The contribution of PTAs to the attainment of this objective is generally positive, as discussed above, but the issue does pose some challenges for negotiators. A balance has to be struck between the benefits of open trade for the regionwide sharing of risk and the ultimate national responsibility for ensuring food supplies. The issue that may cause regional friction is whether a partner in a PTA may restrict supplies to another partner when its own supplies are scarce. The stronger PTAs, with regional food markets and coordinated policy reactions, will tend to restrain the ability of one country to impose an export ban on a partner, whereas the weaker agreements tend to leave this possibility open.

Many PTAs include provisions that relate to the health and safety aspects of agricultural and food trade, such as the harmonization (or the mutual recognition of) health and safety regulations. (See, in this volume, Maur and Shepherd, ch. 10, and Stoler, ch. 11, on standards in PTAs.) Most such provisions are based on the WTO Sanitary and Phytosanitary (SPS) Agreement and do not require members to go far beyond those standards. In some cases, however, such as ANZCERTA, the establishment of joint agencies to oversee such regulations acts as a guard against trade frictions (Almeida, Gutierrez, and Shearer 2009).

Institutions. Institutional innovations are also common, although some of the bodies set up seem to have little role in policy decisions. The NAFTA trilateral agricultural agreement, for instance, set up a Committee on Agricultural Trade to administer the arrangements and an Advisory Committee on Private Commercial Disputes regarding Agricultural Goods to deal with private disputes. But there is little evidence that these bodies have had any significant impact on agricultural trade policy over the 15 years of their existence.

Agricultural Provisions in Bilateral PTAs

The treatment of agriculture in bilateral PTAs is often markedly different from that in regional agreements.[14] The motivation for such PTAs ranges from strategic to practical, but most often it is the exchange of preferential access for goods and services, with little regard for the longer-run economic relationship. No regional integration of the agriculture sectors is envisaged, and many of

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the tensions around farm policies that occur in regional pacts are absent. The main characteristics of bilateral PTAs are usually determined by the dominant partner, often a developed country, and the discussion of these PTAs is therefore conveniently organized according to the dominant partner—in these examples, the EU and the United States.

EU agreements. In the network of agreements involving the EU and nonmembers, agriculture is still treated as being largely outside the realm of unrestricted free trade. The Euro-Mediterranean agreements now being finalized between the EU and the countries of North Africa and the Middle East have so far avoided including unrestricted access for sensitive agricultural products, and the same is true for the customs union that was negotiated with Turkey. The negotiation of a free trade agreement between the EU and South Africa was held up by the reluctance of the EU to grant improved access to goods that would have directly competed with those covered by the CAP. The agreement between the EU and Mexico was also difficult to negotiate until Mexico abandoned its attempt to win easy access to the EU market for a full range of agricultural products.

Similarly, Mercosur and the EU are finding it difficult to overcome the problems that improved access to the EU market would seem to pose for European agriculture. The Cotonou Agreement between the EU and ACP countries, which mandated the negotiation of a transformation of the existing nonreciprocal agreements into full free trade areas after eight years, attempted to address agricultural trade issues, but these negotiations were hampered by inconsistency with the CAP. The unilateral PTA between the EU and the least developed countries (the Everything But Arms agreement) broke significant new ground in this respect by providing duty-free and quota-free access for agricultural goods, with only temporary derogations for the most sensitive commodities—rice, sugar, and bananas.

Traditionally, the EU has used the policy of trade preferences as a strategy of cooperation for development and has unilaterally granted trade concessions to other countries. Now, Euro-Med agreements are taking further steps toward trade liberalization on a bilateral and reciprocal basis. Since the first Euro-Mediterranean Conference in November 1995, the EU and 12 Mediterranean countries have been engaged in negotiating association agreements (the Barcelona process). The overall objective is to form, eventually, a single Euro-Mediterranean free trade area from the separate agreements in place. Yet trade in agriculture is subjected to weak liberalization, within the present framework of the association agreements. No explicit liberalization road map has been defined for the agriculture sector as a whole; only for certain products have specific concessions for liberalization been determined. A concern for the non-EU Mediterranean countries is that, with the conclusion of PTAs between the EU and other countries in Asia and Latin America, the competitive advantage that they themselves used to enjoy in EU markets may be eroded, and they may become marginalized.

The deferral of substantive negotiations on liberalization of trade in agricultural products has been a constant feature of the Euro-Mediterranean partnership (Asbil 2005). The principal reason has been the reluctance on the part of European farmers to compete with Mediterranean countries that are not EU members. The southern enlargement of the EU in the 1980s redefined its relation with the Mediterranean partners. Greece, Portugal, and Spain compete directly in agricultural products with the countries of North Africa, and these members' political influence largely explains the limits on trade concessions through tariff quotas and reference quantities (García-Alvarez-Coque 2002). Agriculture has become a key sector in the debate between the EU and its Mediterranean trade partners because it is seen as a necessary element in the establishment of a balance of commercial opportunities through increases in both industrial and agricultural exports from the region.

The other problem that Mediterranean countries need to consider is the shortcomings in the diversification and competitiveness of their production structures. Several Mediterranean countries have very similar product compositions of exports. Algeria, Cyprus, Israel, Morocco, and Spain all have agriculture sectors oriented toward specialty products—mainly, fresh fruit and nuts, olive oil, and wine. The similarity of agricultural products means that, especially since the enlargement of the EU to include Cyprus, Greece, Malta, Portugal, and Spain, EU members find it easy to replace supplies from nonmember Mediterranean countries with supplies from EU members.

The current negotiations between the EU and the ACP countries (the signatories to the Lomé and Cotonou Agreements) have advanced through six regional talks. The EU has succeeded in agreeing on a comprehensive economic partnership agreement (EPA) with Caribbean ACP countries through CARIFORUM and the Caribbean Community (CARICOM) Regional Negotiating Mechanism.[15] In the case of the African countries, negotiations are being channeled through four of the main regional agreements. The Economic Community of West African States (ECOWAS), in collaboration with the West African Economic and Monetary Union (WAEMU; in French, Union Économique et Monétaire Ouest-Africaine, UEMOA), is the negotiating partner for 16 West African states. Eight

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Central African states have been negotiating through the Economic and Monetary Community of Central Africa (CEMAC, Communauté Économique et Monétaire de l'Afrique Centrale) in conjunction with the Economic Community of Central African States (ECCAS), with which CEMAC has plans to merge. Seven Southern African states are negotiating through the Southern African Development Community (SADC), although some of those states are not SADC members. Another 15 are represented by the Common Market for Eastern and Southern Africa (COMESA), even though some of them do not participate in other COMESA activities. With the exception of the agreement with the Caribbean, the EPAs are still not fully in operation. Some countries have signed partial ("goods only") agreements, but more than half of the ACP countries failed to reach an agreement before the January 1, 2008, deadline, when the WTO waiver that allowed the EU to negotiate these agreements expired. Renewal of the waiver would encounter some opposition. Countries that have shown opposition to the EPAs include South Africa, which already has a free trade agreement with the EU, and Nigeria, with its oil-based economy. A bold move by China to develop trade and investment links with African countries appears to be causing a rethink of the desirability of continuing close ties with the EU if these come with political constraints.

U.S. agreements. U.S. policy toward regional and bilateral PTAs changed dramatically in the mid-1980s. Long a champion of the multilateral system and of nondiscrimination, the United States has now become an active supporter of bilateral PTAs as a complement to its commitment to the WTO and its membership in NAFTA. The United States has completed, or is currently in the midst of, trade negotiations with 27 countries aimed at creating about 20 separate PTAs.[16] The United States has economic and geopolitical reasons for expanding its commercial ties; the attraction for other countries is to secure preferred access to the large U.S. market.[17]

The first of these recent PTAs was signed with Israel in 1985, as an expression of political and economic support for that country. The free trade agreement with Canada followed in 1986, largely at Canada's request. It was designed to consolidate existing sector agreements, encourage U.S. investment north of the border, and give Canadian firms some protection from aggressive use of trade remedy provisions (i.e., antidumping and countervailing duty measures). In 1990 Mexico requested similar conditions, to ensure overseas investors' access to the large U.S. market. Canada opted to join the United States and Mexico in NAFTA, which incorporated the earlier bilateral agreement with Canada. A free trade agreement with Jordan was concluded in 2001, again as a show of political support and economic assistance.

The United States began to negotiate additional bilateral PTAs in 2002, as an expression of a policy of "competitive liberalization" articulated by the U.S. trade representative. This policy consisted of offering swift negotiations to any country that was willing to conform to terms consistent with the mandate of the U.S. administration, as specified in the Trade Promotion Authority Act. The list of willing trade partners with which PTAs were concluded includes Bahrain, Morocco, Oman, Peru, and Singapore. Among other completed bilateral PTAs with a more significant agricultural component were those with Chile and Australia. Talks with Bolivia, Ecuador, Peru, the Southern African Customs Union (SACU), and the United Arab Emirates (UAE) are currently suspended.[18] Agreements with Colombia, the Republic of Korea, and Panama await ratification. A new front has been opened up in the Asia-Pacific region, as the United States has begun to explore the possibility of a Trans-Pacific Partnership (TPP) agreement, to include Australia, Brunei Darussalam, Chile, New Zealand, Singapore, and possibly Malaysia and Thailand. Recent agreements have often been designed as "templates" for future PTAs within a region. Thus, the PTAs with Bahrain, Oman, and the UAE are seen as building blocks toward a Middle East free trade area, and the negotiations with Malaysia and Thailand (along with the one already in place with Singapore) were originally supposed to pave the way for other bilateral PTAs with ASEAN countries—although this prospect has been overtaken by the TPP. The PTAs themselves usually follow from trade and investment framework agreements (TIFAs) and bilateral investment treaties (BITs). The United States has a considerable number of TIFAs and BITS in place that would form the basis for bilateral PTAs.

Although all the PTAs have provisions for tariff reductions that affect many food and agricultural goods, the agreements, with few exceptions, control trade in a range of products considered politically sensitive in one or both partners. For the United States, these sensitivities include sugar, citrus fruits, peanuts, and dairy products; for the partners, the list includes corn, beans, and rice.

Three current agreements have the greatest actual or potential impact on U.S. agricultural markets and hence on the environment in which policy is formed: the recent PTAs with Chile and Australia, and the CAFTA–DR agreement. Table 7.1 summarizes the main characteristics of each agreement.

The United States and five Central American countries—Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua—began negotiations on CAFTA in 2003, and the agreement took effect in 2006. Negotiations with the

Table 7.1. Summary of Provisions Affecting Agriculture in NAFTA, U.S.–Chile, U.S.–Australia, and CAFTA Agreements

Provision	NAFTA	Chile FTA	Australia FTA	CAFTA
Tariff cuts	Some tariffs eliminated, others staged over 5, 10, and 15 years	Some tariffs eliminated, others staged over 4, 8, 10, and 12 years; some cuts delayed for 2 and 4 years	Most tariffs eliminated, others staged over 4, 10, and 18 years	Some tariffs eliminated, others staged over 5, 10, and 15 years; other cuts delayed for 6 or 10 years; duty-free after 15 or 20 years
TRQs	Introduced during transition period for sensitive products	No use of TRQs introduced	TRQs for imports of avocados, cotton, peanuts, tobacco, beef, and dairy products into the United States expanded; above-quota duties for beef phased out over 18-year period; current sugar TRQs not increased: no cuts in above-quota tariff	TRQs for sensitive products in Annex 3.3; rules on administration of TRQs (in addition to GATT Article XIII)
Agricultural safeguards	TRQs allowed as special safeguard for horticultural crops (Annex 703.3)	Additional duties linked to price trigger (Article 3.18) for goods listed in Annex 3.18; total duties not to exceed MFN rate; safeguard not operative after 12 years, or when zero-duty stage reached	Additional customs duties linked to price trigger for horticultural products (Annex 3-A, section A) and to quantity triggers for beef (Annex 3-A, section B); price triggers used for beef in 19th year of agreement (Annex 3-A, section C); safeguard not operative when zero-duty stage reached	Additional duties linked to trigger quantities (Article 3.14) for products listed in Annex 3.14; total duties not to exceed MFN rate; safeguard not operative when zero-duty stage reached
Other safeguards	Safeguards (Chapter 8A): snapback to previous year's tariff on bilateral trade or MFN tariff	Trade remedies (Chapter 8); GATT 1994 Article XIX safeguards	Safeguards (Chapter 9); GATT 1994 Article XIX safeguards	Trade remedies (Chapter 8); GATT 1994 Article XIX safeguards
Export subsidies	Agreement to avoid use of export subsidies on bilateral trade unless third countries subsidized exports to NAFTA markets; agreement to work together for elimination in the GATT	Agreement to avoid use of export subsidies on bilateral trade unless third countries subsidized exports to Chile or the United States; agreement to work together for elimination in the WTO	Agreement to avoid use of export subsidies on bilateral trade unless third countries subsidized exports to Australia; agreement to work together for elimination in the WTO	Agreement to avoid use of export subsidies on bilateral trade unless third countries subsidized exports to CAFTA markets; agreement to work together for elimination in the WTO
Domestic support	Agreement to work together in GATT for reduction of domestic support levels and shift to less trade distorting instruments	Agreement to work together in WTO for reduction of domestic support levels and shift to less trade distorting instruments	Agreement to work together in WTO for reduction of domestic support levels and shift to less trade distorting instruments	Agreement to work together in WTO for reduction of domestic support levels and shift to less trade distorting instruments
SPS measures	Precursor of WTO SPS agreement (Chapter 7B)	Affirm commitment to SPS agreement	Work to resolve trade conflicts over SPS barriers	Affirm commitment to SPS agreement
Dispute settlement	Dispute settlement mechanism for matters arising from agreement (Chapter 20); separate procedures for review of antidumping and countervailing actions (Chapter 19)	Dispute settlement mechanism for matters arising from agreement (Chapter 22)	Dispute settlement mechanism for matters arising from agreement (Chapter 21); provision for monetary penalties	Dispute settlement mechanism for matters arising from agreement
Institutions	Committee on Agricultural Trade; Working Group on Agricultural Subsidies; Advisory Committee on Private Commerce Disputes Regarding Agricultural Goods	Working Group on Agricultural Trade; Committee on Sanitary and Phytosanitary Matters	Committee on Agriculture; Standing Technical Working Group on Animal and Plant Health Measures	Committee on Agricultural Trade; Agricultural Review Commission; Committee on Sanitary and Phytosanitary Matters

Source: Author's compilation from texts of agreements.
Notes: CAFTA, Central America Free Trade Agreement; FTA, free trade agreement; GATT, General Agreement on Tariffs and Trade; MFN, most favored nation; NAFTA, North American Free Trade Association; SPS, sanitary and phytosanitary; TRQ, tariff-rate quota; WTO, World Trade Organization. Citations of specific provisions refer to the respective agreement.

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Dominican Republic that would fully integrate that country into CAFTA were concluded in 2004. In addition, ratification of the pending agreement with Panama, if successful, would round off the establishment of free trade agreements between the United States and almost all of the countries of Central America (see Paggi, Yamazaki, and Josling 2005).

CAFTA is intended to help foster economic growth and improve living standards in the Central American region by reducing and eliminating barriers to trade and investment. It essentially converts the nonreciprocal and discretionary benefits that these countries derive from the Caribbean Basin Initiative (CBI) into permanent and reciprocal access to the U.S. market. CAFTA covers all trade, but the agricultural component is one of its most important aspects (see table 7.1). The key to the agricultural agreement is market access; the arrangement contains relatively few provisions in the areas of export subsidies and sanitary and phytosanitary regulations, and it does not cover domestic subsidies.

Agricultural trade barriers in the Central American countries are higher than those for manufactured goods, and CAFTA will create improved market opportunities for U.S. agricultural products and for related goods and services. CAFTA locks in the applied duty rates for many products and ensures that permanent U.S. access to the market is preserved. Its short-term impact on U.S. exports may, however, be modest because the terms of the agreement delay the full benefits of increased access to the countries of the region for U.S. agricultural products of interest. The lengthy phase-in period for increased market access and the back-loading of commitment levels suggest that the benefits of the agreement may only be realized many years in the future.

Increased access to the U.S. market for Central American goods will also be a consequence of CAFTA. Here, however, the effect is likely to be even more limited because most CAFTA countries have had permanent duty-free access to the U.S. market since the late 1960s under the GSP and since 1990 under the provisions of the Caribbean Basin Initiative (CBI) and the Caribbean Basin Economic Recovery Act (CBERA), which implements the CBI. The CBI was enhanced in 2000 under the terms of the Caribbean Basin Trade Partnership Act (CBTPA) to grant access more equivalent to that enjoyed by Mexico under NAFTA. In fact, approximately 99 percent of CAFTA exports already enter the U.S. market duty-free. Duties are paid only on over-quota imports, as part of the U.S. tariff-rate quota regimes for sugar, dairy products, cotton, meats, and peanuts.[19]

The bilateral PTA with Chile was easier to negotiate than either NAFTA or CAFTA. Chile is an important exporter of agricultural products, particularly fruits, vegetables, and wine, but the different seasonality makes the produce complementary to rather than competitive with U.S. production. The beneficiaries were supermarkets, which gained the assurance of year-round supplies. Chile is one of the more liberal Latin American countries, even on agricultural products, so that opening up to U.S. exporters was not such a big move for its farmers. Aside from some controversy over wine labels, the talks went smoothly. It may have helped that Chile is not a significant sugar exporter.

The U.S. agreement with Australia also involved a Southern Hemisphere country and thus offered some advantages of complementary production. Australia, however, is a major exporter of meats, dairy products, cereals, and sugar, and so tight rules had to be built in to the agreement to protect U.S. farmers from competition from imports. Reluctantly, Australia accepted long transition periods for dairy products and beef, and an exclusion altogether of any relaxation of protection for the U.S. sugar sector. This decision may have an effect on the politics of future bilateral PTAs.

The most ambitious bilateral agreement to have been negotiated since NAFTA is still awaiting approval by Congress at present. The Korea–U.S. Free Trade Agreement (KORUS) would establish a free trade area between the United States and a major economy in East Asia. There was no doubt from the beginning of the talks that agriculture would be a stumbling block, with the Korean government, in particular, not wishing to open up its highly protected rice market to U.S. exports. The U.S. position had been to include rice, even if access for U.S. rice were to be introduced slowly over a transition period. In the end, the rice sector was essentially excluded from the agreement. This establishes a precedent in case KORUS were to act as a template for an agreement with Japan.

Summary

Agricultural trade is becoming increasingly governed by conditions negotiated in preferential trade agreements (PTAs), whether regional or bilateral. Regional integration of agricultural markets through open trade can have a positive effect on the development of a competitive and sustainable agriculture sector, although complementary policies at the multilateral level are needed to prevent trade diversion. PTAs can yield benefits in the area of food security and the provision of public goods, but the empirical analyses required to quantify these benefits are scarce, in part because of the very diverse treatment of agriculture in PTAs. If concluded with the right partner countries, PTAs

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can avoid the disadvantages of trade diversion. If the terms of the agreements are appropriate, such PTAs can further full integration into the global economy and stimulate needed investment and the transfer of technology.

Notes

1. A full account of the interpretation of GATT Article XXIV is provided in Hudec and Southwick (1999). Srinivasan (1998) presents a critique of the systemic issues posed by PTAs. A type of agreement not considered in this chapter is the partial-scope agreement, which covers only a subset of goods. These agreements are not generally notified under Article XXIV.

2. It is perhaps ironic that the insistence on both the inclusion of substantially all trade and 100 percent preference increases the likelihood of trade diversion. Exclusion of those sectors where protection is high, and the partial liberalization of internal trade in those high-cost sectors that are covered, would reduce trade diversion, although it would also limit trade creation. The strict rules were presumably inserted to discourage trade agreements that merely "picked low-hanging fruit" by confining themselves to nonsensitive sectors or small reductions in tariffs.

3. For a discussion of the benefits of coordinating trade strategies for small countries see Schiff (1997, 2002); Andriamananjara and Schiff (1998).

4. Adjustment of market access provisions is made easier by the negotiation in the Uruguay Round of tariff-rate quotas (TRQs) that ensure continued access for those countries with negotiated quotas. Allocation to preferred partners of TRQs allowed in WTO schedules is a principal link between the multilateral and preferential trade regimes. These allocations appear contrary to the spirit of Article XIII of the GATT, which provides that the distribution of quotas should be nondiscriminatory and should reflect market conditions.

5. Analytical devices such as that applied here are sometimes difficult to reconcile with a world of actual countries and diverse trade strategies. In fact, some new members may be willing to pay the price for entry, and some old members may have strong reasons for excluding newcomers.

6. The "completion" of the European Community's (EC's) internal market reform, which was incorporated in the 1992 program, was the product of an attempt to remove remaining barriers between EC members in goods, services, labor markets, and capital markets. The success of the European Commission in pushing through this program caused a stir of interest in other regions.

7. The inclusion of APEC in this list is of interest, as no preferential tariff reductions were specified in that agreement. APEC's modus operandi was and is a loosely coordinated process of unilateral liberalization among its members, with no discrimination against outsiders.

8. This analysis also points up the importance of timing in trade agreements. The advantage of being first to reach a deal may be considerable. And the negotiation of long transition periods may be of little value in easing adjustments if other countries can enter into agreements with a shorter time horizon.

9. A side agreement guaranteed access for Denmark to the British market for pigmeat products and for limited quantities of dairy goods.

10. Canada declined to join the open market between Mexico and the United States because that would have required liberalization of the supply-managed sectors (dairy products and poultry), as well as sharply increased prices for sugar in Canada.

11. The original ANZCERTA suffered from a lack of ambition and political support (Lloyd 1991). A 1988 review of its operations led to an acceleration of the process of liberalization, with July 1990 set as the date for the removal of remaining tariff and nontariff barriers. In addition, export subsidies on intrabloc trade were to be removed.

12. In 1991 Argentina eliminated export taxes on agricultural goods, which had long been a source of government revenue. A small tax on oilseed exports remained, together with a fee to pay for research. Argentina has essentially liberalized imports of agricultural goods, although some export taxes have reappeared in recent years.

13. The language about and treatment of export subsidies is much softer in NAFTA than in the U.S.-Canada Free Trade Agreement, which banned the use of export subsidies between the two countries.

14. Bilateral PTAs involving Singapore do not face the same political problems in including agriculture and food products as do most other agreements. Singapore has no significant agricultural production and no import barriers. Other countries, however, may be concerned about the possibility of trade deflection through Singapore. Japan, for instance, has not agreed to open its agricultural market to imports from Singapore in their bilateral free trade agreement.

15. CARIFORUM includes the Dominican Republic, as well as the CARICOM countries.

16. It is worth recalling that in the late 1930s, U.S. trade policy took a similar direction. The Reciprocal Trade Agreements (RTA) Act of 1934 was an open-ended mandate to negotiate bilateral trade agreements with other countries, and about 30 such agreements were signed.

17. In many cases, access is already covered by existing agreements, but the negotiation of a formal PTA reduces uncertainty as to whether these preferences will continue.

18. SACU is made up of Botswana, Lesotho, Namibia, South Africa, and Swaziland.

19. For more details on CAFTA and its potential impact on U.S. agriculture, see Paggi, Yamazaki, and Josling (2005).

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