

Regional Trade Agreements and U.S. Agriculture. Mary E. Burfisher and Elizabeth A. Jones, editors. Market and Trade Economics Division, Economic Research Service, U.S. Department of Agriculture. Agricultural Economic Report No. 771.

Abstract

Regional trade agreements (RTA's) have become a fixture in the global trade arena. Their advocates contend that RTA's can serve as building blocks for multilateral trade liberalization. Their opponents argue that these trade pacts will divert trade from more efficient nonmember producing countries. U.S. agriculture can benefit from participating in RTA's and may lose when it does not. Agriculture is an important source of potential U.S. gains from RTA's. While the United States, as a global trader with diverse trade partners, can gain potentially more from global free trade than from RTA's, many recent RTA's have been more comprehensive in their liberalization of agricultural trade liberalization than the Uruguay Round. A strong multilateral process can help ensure that RTA's are trade creating, rather than protectionist.

Acknowledgments

The authors wish to thank Sophia Huang, our economics editor. Thanks also to Deana Kussman, Thomas McDonald, and Dale Simms, our technical editors, and Wynnic Pointer-Napper and Victor Phillips, Jr., our graphics editors.

Appreciation is extended to Cheryl Christensen, Steven Haley, and David Skully for their role in the oversight and review of the project's development. Verna Blake and Lilia George provided technical support. The authors gratefully acknowledge the reviews of Abraham Avidor, Mary Bohman, Britta Bjornland, Jaime Casteneda, Larry Deaton, Praveen Dixit, Carol Goodloe, Munisamy Gopinath, David Harrington, Timothy Josling, Maureen Kilkenny, William Kost, Jeffrey D. Lewis, Wolfgang Muench, Robert Paarlberg, Emilio Pagoulatos, Sherman Robinson, Terry Roe, G. Edward Schuh, Renee Schwartz, Robert Spitzer, Ron Trostle, Silvia Weyerbrock, Alan Winters, and Fumiko Yamazaki.

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Regional trade agreements (RTA's) have become an increasingly important part of the global trading system. The United States has become an active participant in RTA's, with memberships in the North American Free Trade Agreement (NAFTA), the Asia Pacific Economic Cooperation (APEC) forum, and the U.S.-Israel Free Trade Agreement. The United States also has trade initiatives in the Caribbean Basin. An important new regional trade agreement is the proposed Free Trade Area of the Americas (FTAA), which would encompass most countries of the Western Hemisphere, and help reconcile the proliferation of trade agreements in the Hemisphere into one comprehensive trade pact.

Regional trade agreements have generated intense debate. Advocates for RTA's emphasize their *trade-creating* effects. By providing for freer trade among members, RTA's can increase welfare by shifting regional production toward the most efficient producers, enabling consumers to purchase goods at lower prices. Opponents of RTA's argue that because most agreements introduce some degree of trade discrimination, they are likely to divert trade from more efficient producers in the rest of the world. A second issue raised by RTA's is their effect on multilateral trade negotiations. Whether RTA's will reinforce or accelerate global trade talks, or act to slow down or derail them is under debate.

This report analyzes the implications of regional trade agreements for U.S. agriculture. Key findings include:

—*U.S. agriculture can gain from participating in RTA's.* By lowering trade barriers among members, the major RTA's in which the United States participates—NAFTA, APEC and, potentially, the FTAA—are expected to benefit U.S. agriculture. In the long term, their trade-creating effects—increased agricultural trade and specialization among RTA partners—will increase the efficiency of U.S. agricultural producers and reduce prices for consumers. These RTA's are expected to improve the U.S. international terms of trade in agriculture, with an increase in U.S. farm export prices relative to import prices.

—*U.S. agriculture can lose when not a member of RTA's.* Expansion of the European Union (EU) is likely to divert agricultural trade and reduce U.S. agricultural exports to the EU and to third markets. But, the current CAP program is probably unsustainable with EU expansion, and potential EU farm program reforms would reduce these negative impacts on the United States. A U.S. decision to remain outside the FTAA would divert trade from U.S. agriculture. However, many expect RTA's to induce economic growth in the Western Hemisphere. If this trade-linked growth occurs, the United States is expected to benefit from the FTAA, even as a nonmember.

—*Agriculture is an important source of U.S. gains from RTA's.* Gains from trade liberalization are roughly proportional to the size of the trade barrier. Because U.S. agricultural exports still face relatively high trade barriers in world markets, the inclusion of agriculture in trade agreements accounts for much of the U.S. gains from RTA's. Over the past decade, RTA's have become more compre-

hensive in their treatment of agriculture, in contrast to earlier RTA's, many of which excluded agriculture.

—*RTA's interact with domestic farm programs.* RTA's limit the ability of member countries to maintain independent farm programs. Market arbitrage within a free trade area will tend to unify prices, making members' efforts to use farm support programs to maintain different price levels either ineffective or costly. The conversion of most U.S. farm support into decoupled contract payments is compatible with free trade pacts. At the same time, the reduction in farm support and greater market orientation of many countries' farm sectors over the past decade has made RTA's more likely to include agriculture, increasing the gains from RTA's.

—*In agriculture, RTA's have both trade-creating and trade-diverting impacts, but trade creation dominates in most RTA's.* To date, the empirical evidence shows that the Australia-New Zealand Closer Economic Relations, the Canada-U.S. Trade Agreement, and MERCOSUR (the Common Market of the South, among South American countries) have led to increased agricultural trade with both partners and nonmembers, supporting the view that RTA's can unleash growth in trade that benefits members and nonmembers alike. When fully implemented, NAFTA, APEC, and the FTAA are expected to be net trade creating in agriculture. Only the EU has resulted so far in net agricultural trade diversion. Its expansion to include Central and East European countries is also expected to be trade diverting.

—*Regionalism and multilateralism are likely to be mutually reinforcing in agriculture.* A strong multilateral process can help minimize the negative aspects of RTA's and make it more likely that RTA's will take shape as trade-creating, rather than protectionist, agreements. In turn, the freer agricultural trade already achieved in the Western Hemisphere and committed to in APEC is likely to strengthen efforts to achieve freer trade at the upcoming mini-round of the General Agreement on Tariffs and Trade.

—*The United States can potentially gain more from multilateralism than from RTA's.* Because the United States is a global trader with diverse trade partners, it can potentially gain more from global free trade than from regional trade agreements. So far, however, multilateral talks have fallen far short of achieving free trade, and the gains to the United States from the deeper commitments made by RTA's are expected to exceed those from the Uruguay Round. But the influence of RTA's on the multilateral process is still uncertain, and they hold the potential to harm nonmembers. Because the two processes can provide important, mutually reinforcing influences, U.S. support of both can benefit U.S. agriculture.

List of Abbreviations

AFA	1996 U.S. Israel Agreement on Food and Agriculture
AFTA	ASEAN Free Trade Area
APEC	Asia Pacific Economic Cooperation Forum
ASEAN	Association of South-East Asian Nations
CACM	Central American Common Market
CAP	Common Agricultural Policy (of the EU)
CARICOM	Caribbean Common Market
CEEC	Central and East European Countries
CEFTA	Central European Free Trade Area
CER	Closer economic relations
CES	Constant elasticity of substitution
CET	Constant Elasticity of Transformation/Common external tariff
CGE	Computable General Equilibrium
CSREES	Cooperative State Research, Education, and Extension Service, USDA
CUSTA	Canada-U.S. Trade Agreement
EC	European Community
EEC	European Economic Community
EFTA	European Free Trade Area
ERS	Economic Research Service, USDA
ESIM	European Simulation
EU	European Union
EU-CEE	Euoprean Union-Central and East European Association Agreements
FDI	Foreign direct investment
FTA	Free Trade agreement
FTAA	Free Trade Area of the Americas
GATT	General Agreement on Tariffs and Trade
GAMS	General algebraic modeling system
GE	General equilibrium
GTAP	Global trade analysis project
LDC	Less developed country
MERCOSUR	Common Market of the South (Mercado Comun del Sur)
MFN	Most favored nation
MOU	Memorandum of understanding
NAFTA	North American Free Trade Agreement
NIS/B	Newly Independent States and Baltics
OECD	Organization for Economic Cooperation and Development
PROCAMPO	Mexican farm income support program
ROO	Rules of Origin
RTA	Regional Trade Agreement
TFP	Total factor productivity
TRQ	Tariff rate quota
UR	Uruguay Round
URA	Uruguay Round Agreement
USDA	U.S. Department of Agriculture
WTO	World Trade Organization