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INTERNATIONAL TRADE POLICY REPORT

Gaylon B. Booker
National Cotton Council
Memphis, TN

Abstract

International trade policy has had a major influence on the economic health of the U.S. cotton industry and will continue to do so, with increasing influence, in the months and years ahead.

Introduction

The focus of my report this morning is International Trade Policy. If I do nothing else, I hope to convince you that international trade policy has had a major influence on the economic health of the U.S. cotton industry. And in the months and years ahead, it will have even more influence.

I believe I am safe in saying that, in previous trade discussions, our negotiators have not placed a high priority on achieving terms and conditions that were favorable for U.S. agriculture and the U.S. textile industry. If they have, the only conclusion that can be drawn is that they were poor negotiators. The record suggests that they have done a lot more giving than receiving, and we can no longer afford to allow them be generous with U.S. market access without getting something meaningful in return.

Trade Liberalization

Trade liberalization is without question among the Bush Administration's highest priorities. (Figure 1) We have seen a number of new agreements completed already and more are being negotiated.

New multilateral agreements are being negotiated under the auspices of the World Trade Organization. Additionally, Ambassador Zoellick is negotiating new bilateral and regional agreements as fast as he can. He has served notice that if progress slows down on one, he will simply turn his attention to another.

The Administration was given a leg up on negotiations when Congress accorded the President TPA authority (perhaps better known as fast track authority) just before the August recess last year. This means any agreement negotiated by USTR will be brought to Congress for an up or down vote, with no amendments.

Omnibus Trade Bill

That authority was, in reality, part of an omnibus trade bill that also amended existing legislation relating to the Caribbean and sub-Saharan Africa regions. (Figure 2) It also renewed legislation for the Andean region and extended coverage to textiles and apparel. Still another component amends existing law to provide greater benefits to workers who have been adversely affected by imports.

Existing Textile Tariffs

This visual (Figure 3) illustrates why I say that preservation of the U.S. textile industry has not been a high priority for our negotiators in the past. If a textile or apparel manufacturer abroad wants to ship their products to the U.S., the effective tariff rate averages 8.9%. By contrast the effective rates for textile and apparel products entering Argentina ranged from 40 to 50+%, Brazil ranged from 40 to 70+%, China ranged from 20 to 36+%, India ranged from 50 to 70+%, and Pakistan ranged from 40 to 60+%.

Existing Allowable Ag Tariffs

We have the same kind of unlevel playing field in agricultural product tariffs. This visual (Figure 4) shows the average US tariff in the red bar to the left. By comparison, the EU's average tariff is 31%, Japan's 51%, Korea's 66% and India's 114%. The average world tariff rate is 62%.

Something's wrong with this picture. Who was looking out for U.S. agriculture when this agreement was struck?

I don't have to tell you about the incessant, mindless criticism we've heard about U.S. agricultural subsidies, especially since passage of the Food Security and Rural Investment Act of 2002. And the cotton program has taken the brunt of the criticism.

Core Problems

But let's examine some core problems. (Figure 5) If we want to ship our agricultural products abroad, we face an average tariff rate of 62%, with the rate in many countries exceeding 100%. Our competitors abroad can ship their products into the U.S. and pay a modest 12% tariff, on average.

The EU spends $2 billion to $5 billion a year on export subsidies, while the US spends only about $20 million – mostly on dairy. We could spend more but we don't.

We hear incessant railing about the big payments going to US farmers but, again, let's compare some numbers. The EU is permitted to spend up to $67 billion annually for trade distorting domestic subsidies, while US spending is limited to $19.1 billion. We could add Canada to this chart (with allowable domestic subsidies at $23 billion and Japan, with $30 billion).

Two weeks ago I took a call from an EU Journalist who wanted to know how we reacted to Brazil's challenge of our cotton program … and how did we respond to the World Bank's assertion that our program is harmful to poor African farmers?

While I don't expect my response to show up in print, we made it clear that if our program has <u>any</u> effect on farmers in Brazil, Africa or any other nation it is minute compared to the aggregate effect of a host of other factors, including:

- The Asian financial crisis
- A faltering global economy
- Currency manipulation
- A tripling of world production capacity for textile polyester – cotton's primary competitor in the textile market; and
- Revenue and tax policies of their own governments that deprive farmers of normal returns from the market.

Most of you saw the Wall Street Journal article last June that took our program to task for harming West African cotton farmers. That article, like so many others, failed to address the obvious problems. If they had made more than a superficial inquiry, they would have learned that the cotton growing West African governments of the former French colonies sit astride the marketing system for agricultural commodities and extract the equivalent of extraordinary export taxes from their own growers. Governmental agencies and parastatal organizations control access to seeds, fertilizer, ginning, sales and transportation.

If the writers of the article had wanted to check, they would have found that cotton growers in open market countries received prices about 12 cents a pound higher than the West African countries during the 2000 and 2001 marketing years. Cotton growers in Egypt, India, Pakistan and Sudan face similar situations, resulting from their own governments' revenue and tax management that is completely unrelated to U.S. farm programs.

Farm/Trade Must be Compatible/Fair

Congress returns to Washington this week to begin work on appropriations bills. As that process resumes, there will also be initiatives to provide agricultural disaster relief -- which our industry certainly needs and which the National Cotton Council supports. At the same time, there will be calls for the cost of disaster assistance to be offset by reductions in farm program spending. Senator Grassley has promised that a reduction in payment limits will be considered as one way to offset disaster spending. That, of course, would put the offset burden squarely on the shoulders of the cotton industry.

Meanwhile, Ambassador Zoellick and his colleagues in the Office of the US Trade Representative will press forward on the Administration's trade agenda. As these broad policy agendas continue to unfold, it will be important to make policymakers at all levels understand that global farm policy and international trade policy must be compatible and fair. (Figure 6)

Good farm policy is absolutely linked to trade policy. We cannot have good farm policy in the absence of good trade policy and vice versa.

For the cotton industry, good farm policy and good trade policy must take into account the interests and needs of the US textile industry. All of us have become keenly aware of the economic stress that our domestic textile industry is experiencing. We cannot export enough cotton to maintain a viable US cotton industry – we MUST find a way to provide better underpinning for the domestic textile industry.

The economic viability of both the US cotton and textile industries hinges on:

- Agreement on core issues, especially regarding farm and trade policy;
- Broadening our coalition beyond our seven segments; and
- Aggressively pursuing our goals, both with the Administration and on the Hill.

If we do these things well, I believe we can generate enough support to hold essential farm bill provisions and have a real influence on terms and conditions that are eventually approved in new trade agreements. If we don't get together and move aggressively with the broadest possible coalition, we may not be able to hold the provisions of new farm law that we fought so hard to get. And we won't get the trade provisions we need to compete in a global arena that's characterized with fewer subsidies, lower tariffs and phased out quotas.

Reconciling Farm and Trade Policy

Certain principles must be maintained if global farm and trade policy are to be reconciled so that developed countries such as the US can be viable. (Figure 7) For example:

- US farm programs cannot be unilaterally reduced or phased out
- US agricultural and textile tariffs cannot be further reduced until other nations reduce their tariffs to US levels
- Market access be reciprocal
- Non-tariff barriers must be eliminated
- Export subsidies must be eliminated, or harmonized
- Improvements must be made in international trading disciplines and dispute settlement procedures (and the US must have the will to use the tools that are available).

Summary US-Doha Proposal

This visual (Figure 8) summarizes the US proposal in the Doha Round. Our negotiators are looking for substantial improvement in market access; reductions, and eventual phase-out, all forms of export subsidies; and substantial reductions in trade distorting domestic supports.

Swiss Formula 25

With respect to tariffs, they propose to use a protocol known as the "Swiss Formula 25" (Figure 9) to reduce tariffs over a five year period. As this visual shows, it would not reduce tariff rates that are now higher than ours down to US levels. But it would get them much closer – the higher the existing tariff rate, the greater the reduction. The plan would allow no country to have a tariff greater than 25%.

Export Subsidies

This visual (Figure 10) depicts the problem we face in export subsidies. The EU accounts for 87% of global spending for export subsidies compared with 1% by the US. Our negotiators propose to solve the problem be phasing out export subsidies over a 5-year period.

Domestic Support Proposal

US negotiators propose to bring down trade distorting domestic subsidies substantially. (Figure 11) The proposal calls for reducing non-exempt domestic support to 5% of member countries' total value of agricultural production over a 5-year period. The approach would establish the same standard for calculating every country's permitted level of domestic support, and it would eliminate the so-called blue box loophole. Under the US proposal, there would be no limit on green box spending.

US negotiators say the approach they propose (Figure 12) would level the playing field. Under the US proposal, EU spending would phase down from $67.2 billion to $12.5 billion, while US spending would fall from an allowable level of $19.1 billion to $10 billion – certainly a more equitable situation than we currently face.

Proposal vs. Agreement

It is one thing to lay down a proposal and it is another thing to convince other parties to accept it. (Figure 13) We can expect the EU to resist any proposal that does not permit them to retain subsidy advantages. Negotiations will continue for a long time.

US negotiators hope to establish modalities by March 31 of this year and to complete negotiations by January 1, 2005.

You may or may not like the US proposal. Certainly, it requires reductions in US agricultural subsidies and existing tariff levels. But it would require other developed nations to bring theirs down even more. Given the "going in" position of US negotiators, we can't expect to see a final agreement that looks better for us. And we will have to be diligent to ensure that the final agreement does not perpetuate the existing disadvantage we face.

Agreement vs. Compliance

Even if the new WTO agreement includes fair and equitable market access and subsidy provisions, they will do us little good (Figure 14) unless we also have an improved system of international trading disciplines and dispute settlement procedures.

And Congress should insist that USTR make full use of the dispute disciplines and dispute settlement provisions available. In fact, Congress should not ratify new agreements until USTR demonstrates resolve to deal with existing non-compliance problems.

China TRQ Agreement

This visual (Figure 15) depicts what will happen otherwise. In its WTO accession agreement, China agreed to open its market for 3.75 million bales of imported cotton. Of that total, 33% was reserved for state-owned enterprises, but the rest was to be given what is known as "national treatment." This means imported cotton must be treated the same as domestic cotton in all respects, including access to it by Chinese textile mills.

As the agreement has been implemented, only 6% of the quota has been given national treatment, and even that small piece of the pie has been awarded to mills in such small individual quotas that importing has been impractical. USTR agrees that this practice puts China in violation of its accession agreement. They have asked China to change their implementation practices, but Chinese officials have refused and have announced their intention to administer the program the same way in 2003.

Chinese Textile Exports to US

Meanwhile, China has made full use of WTO provisions to increase their textile exports to the US. (Figure 16) In 2002, Chinese textile exports to the US, in eight categories for which quotas were removed, increased by 604%.

And look how they made the big US market penetrations. (Figure 17) The average price of the 8 product categories was reduced by 72%. Guess what will happen to those prices once they kill US production. I guarantee you prices will be hiked and there will be no lasting benefits for US consumers.

This kind of abuse will continue until the Chinese are forced to abide by their accession agreement. We have urged USTR to request consultations under WTO dispute settlement provisions and if the consultations are not successful to request that a dispute settlement panel be convened.

We are also urging Congress to insist that USTR make full use of available tools to force compliance by China and other nations before bringing new agreements to them for fast track approval.

Upcoming Bilateral and Regional Agreements

There will be no absence of new agreements brought to Congress for ratification. (Figure 18) The Administration is working on agreements, or have announced plans to begin discussions, with Chile, Singapore, Australia, and a Free Trade Area of the Americas, while continuing WTO discussions in the Doha Round.

The effort to bring a regional free trade agreement to Central America will be all the more problematical as these nations already participate in textile trade preferences provided by the Caribbean agreement.

As these agreements are being negotiated, it will be important for the US cotton and textile industries to work together to achieve what we mentioned earlier. (Figure 19) We must make sure that global farm and trade policies are fair and equitable. To be successful, we will have to reach timely agreement on core issues, broaden our coalition and pursue our goals aggressively.

TPA Vote in Textile States

Otherwise, we will very likely witness the same kind of outcome we experienced with the omnibus trade bill last year. Although the Council, the American Textile Manufacturers Institute and the American Yarn Spinners Association eventually reached agreement on specific provisions to recommend, our agreement was reached only a couple of weeks before the final vote was taken on the bill. We simply got to the party too late.

As a result, look at the House vote count in the major textile states. (Figure 20) There were 18 yeas and 18 nays. We simply can't afford to have this kind of division on issues that are critical to the economic viability of the US cotton and textile industries. A holdout by two or three House members could have been key to our getting some very important concessions made. Remember, the bill passed the House by only 3 votes.

Regional Fabric Quota Comparisons

This visual (Figure 21) illustrates what's at stake. The red bars reflect the combined regional fabric and T-Shirt quotas that existed under the old law, before passage of the omnibus bill last year. The light blue bars show the quota levels that the Council, ATMI and AYSA agreed to support. The brown bars show what we got.

Had we reached agreement earlier, I think it is very likely that we could have achieved our quota goals. All it would have taken was a handful of Textile Caucus and Cotton Belt members to hold out for our provisions we sought. Instead, House leadership made concessions to labor advocates to Trade Adjustment Assistance to get the narrow margin they needed for passage.

Summary

Whether it is trade policy, farm policy or the host of other issues that affect our economic viability, our strategy must continue to begin with consensus among the Council's seven segments. (Figure 22) Then we must broaden that coalition wherever possible and we must work together aggressively to ensure that our objectives are achieved.

In the months and years immediately ahead, holding onto the farm policy provisions we fought so hard to get and getting fair and equitable trade policies must be at the very top of our agenda.

Figure 1. Trade Liberalization.

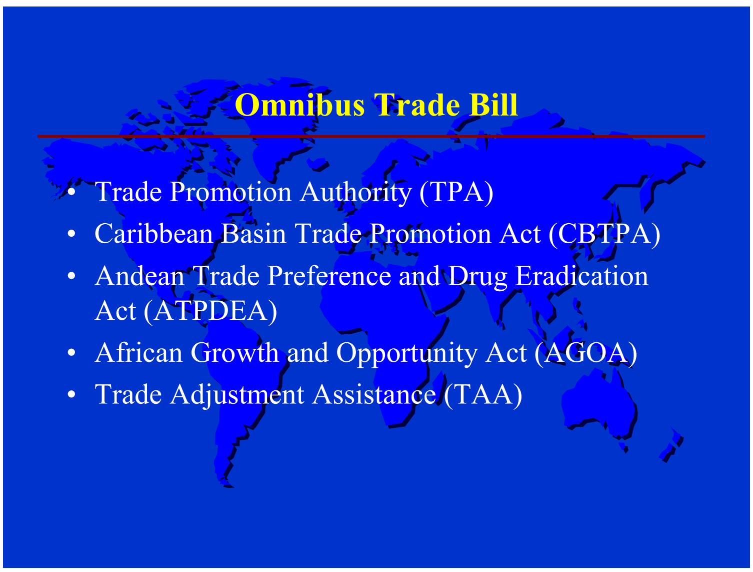


Figure 2. Omnibus Trade Bill.

Figure 3. Existing Textile Tariffs.

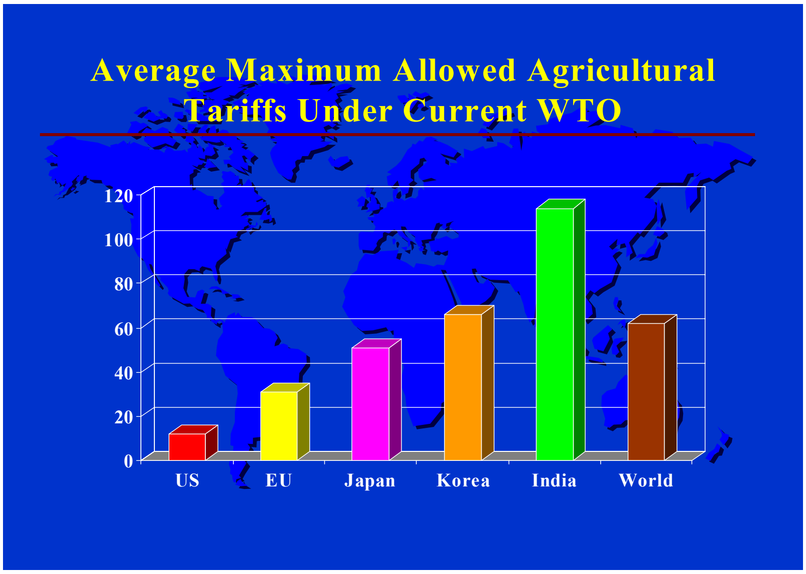


Figure 4. Existing Allowable Ag Tariffs.

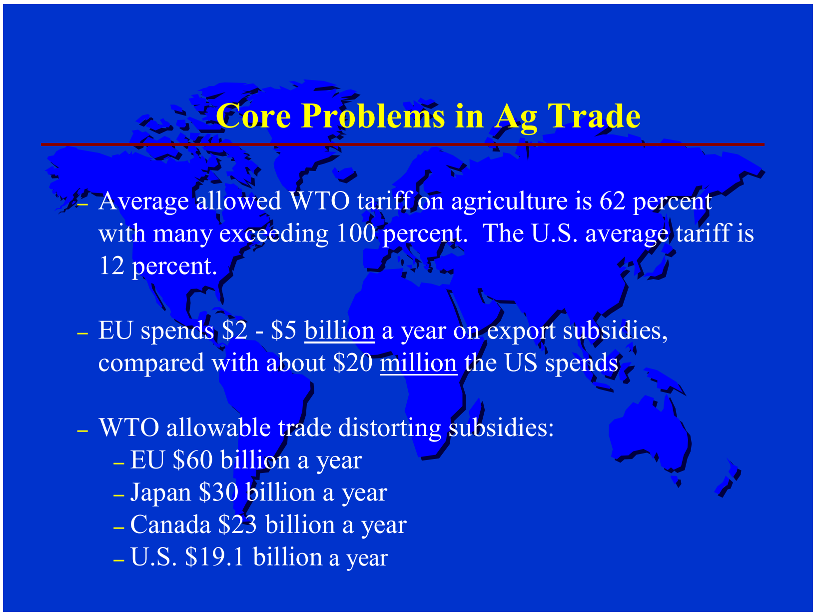


Figure 5. Core Problems.

Figure 6. Farm/Trade Must Be Compatible/Fair.

Figure 7. Reconciling Farm and Trade Policy.

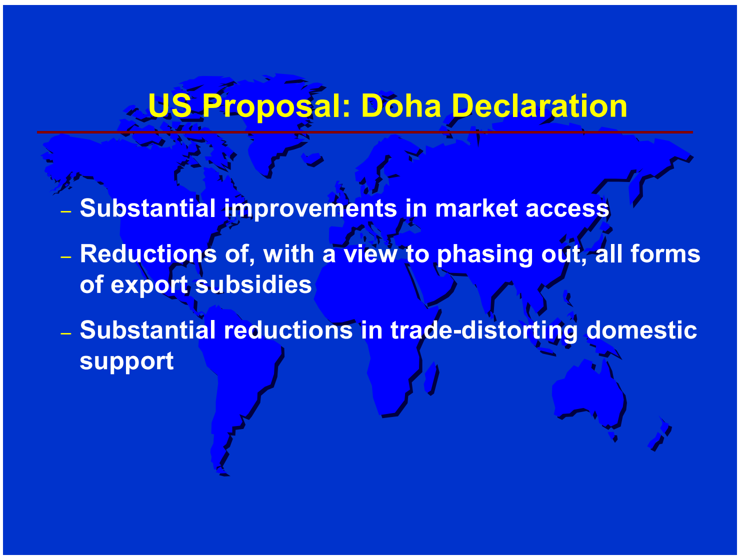


Figure 8. Summary US Doha Proposal.

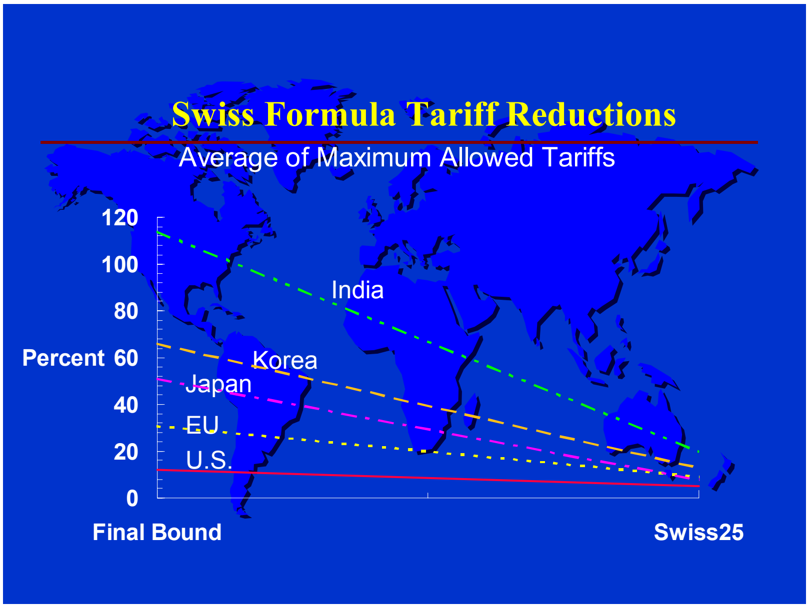


Figure 9. Swiss Formula 25.

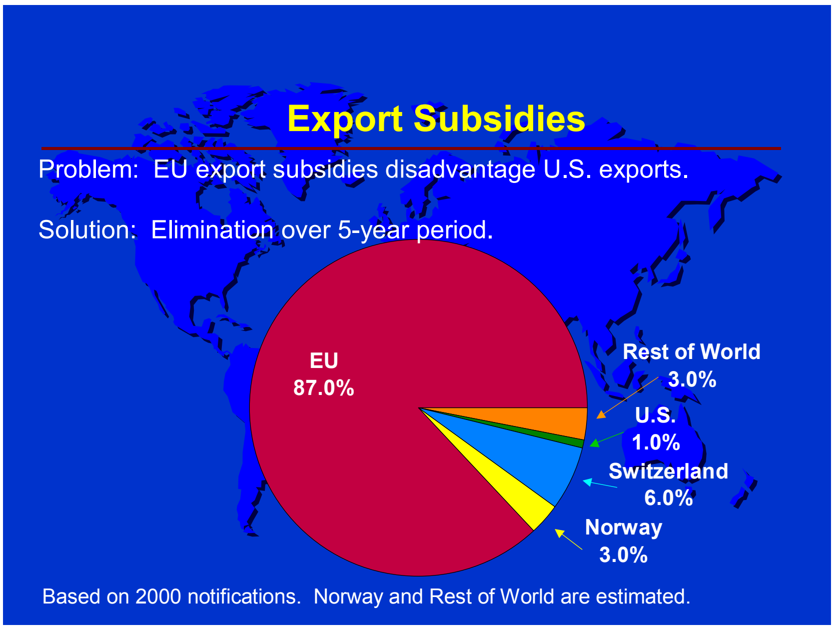


Figure 10. Export Subsidies.

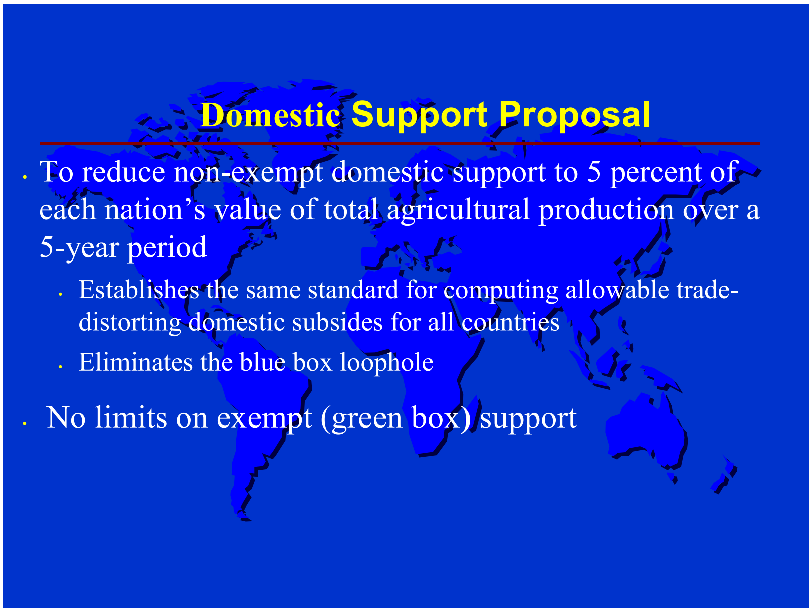


Figure 11. Domestic Support Proposal.

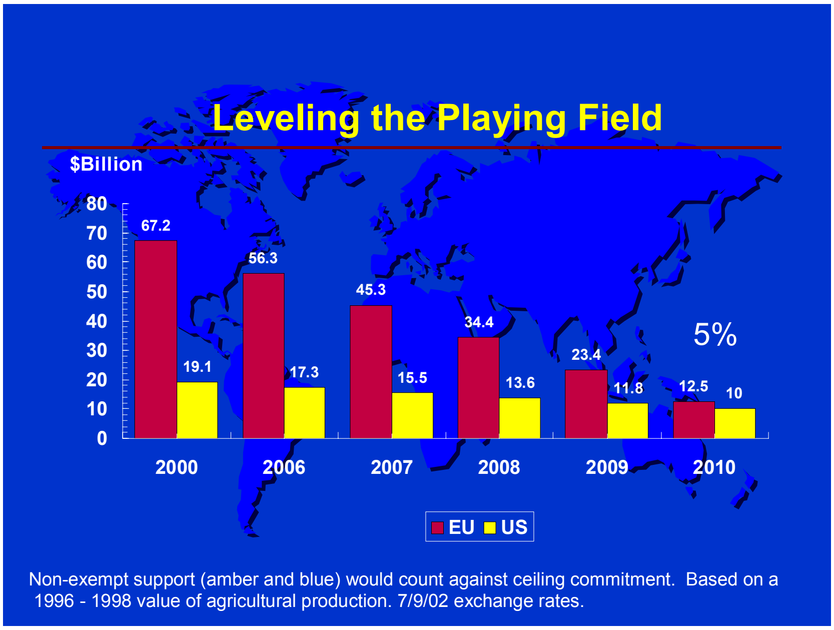
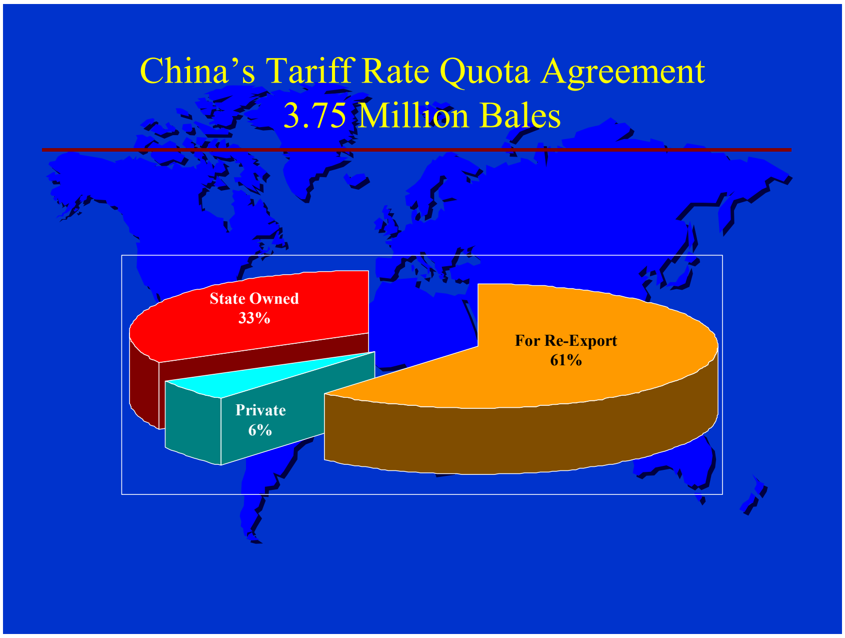


Figure 12. Domestic Support Proposal

Figure 13. Proposal vs. Agreement.

Figure 14. Agreement vs. Compliance.



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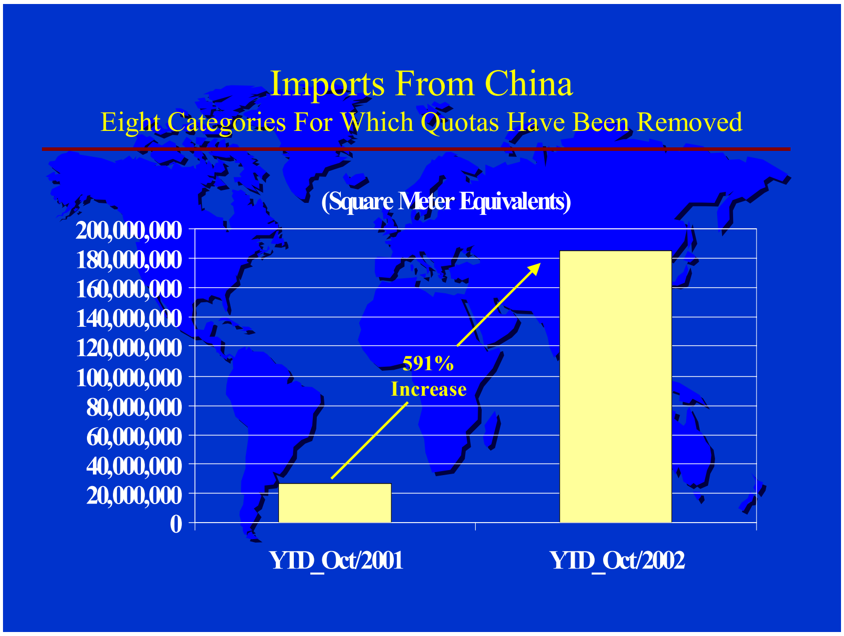
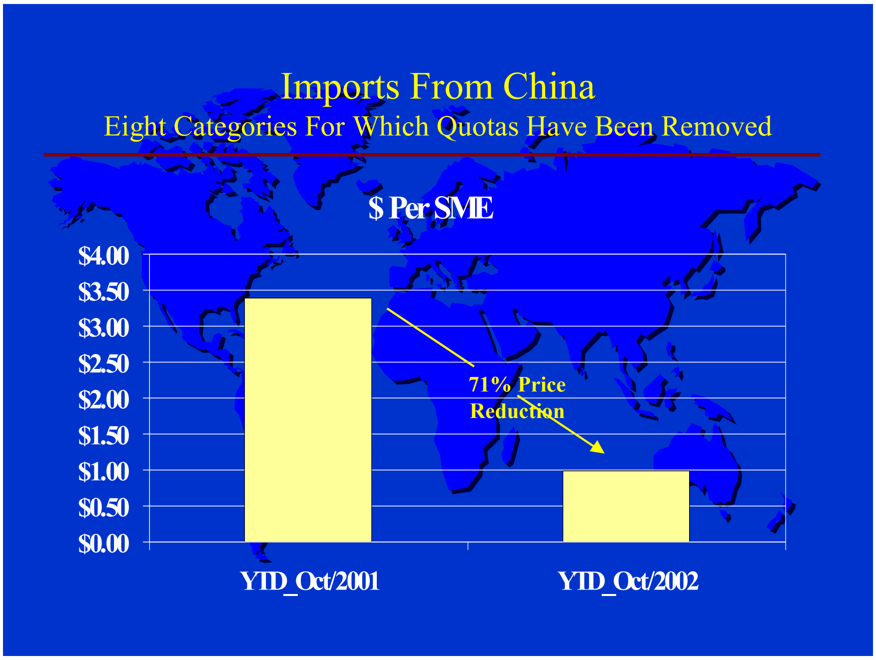


Figure 16. Chinese Textile Exports to US.



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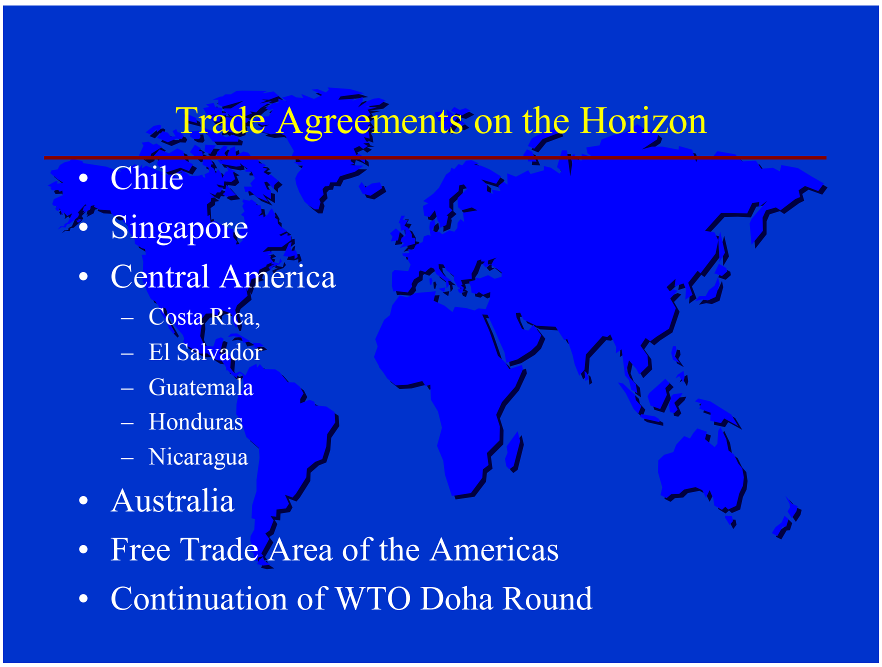

Figure 18. Upcoming Bi-lateral and Regional Agreements.

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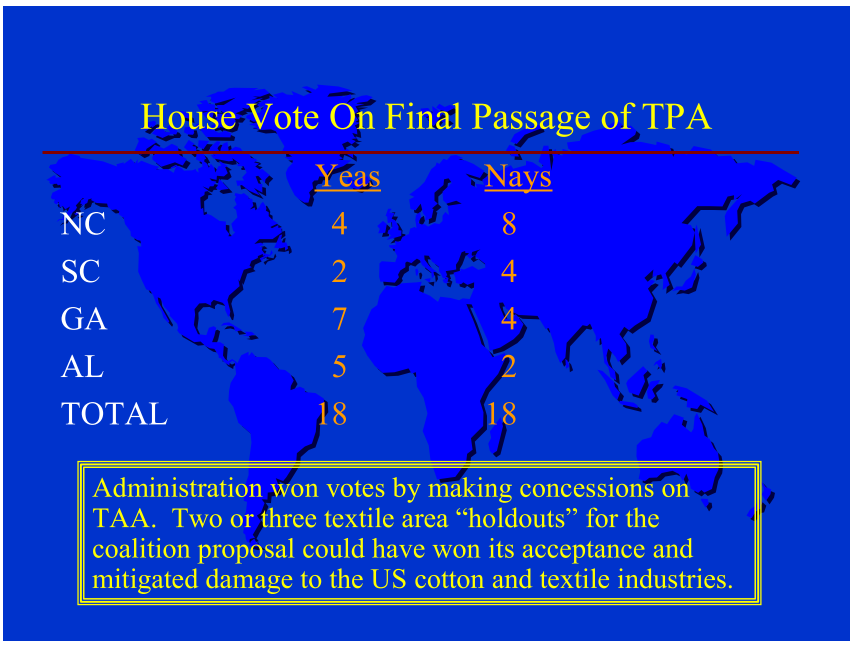

Figure 20. TPA Vote in Textile States.

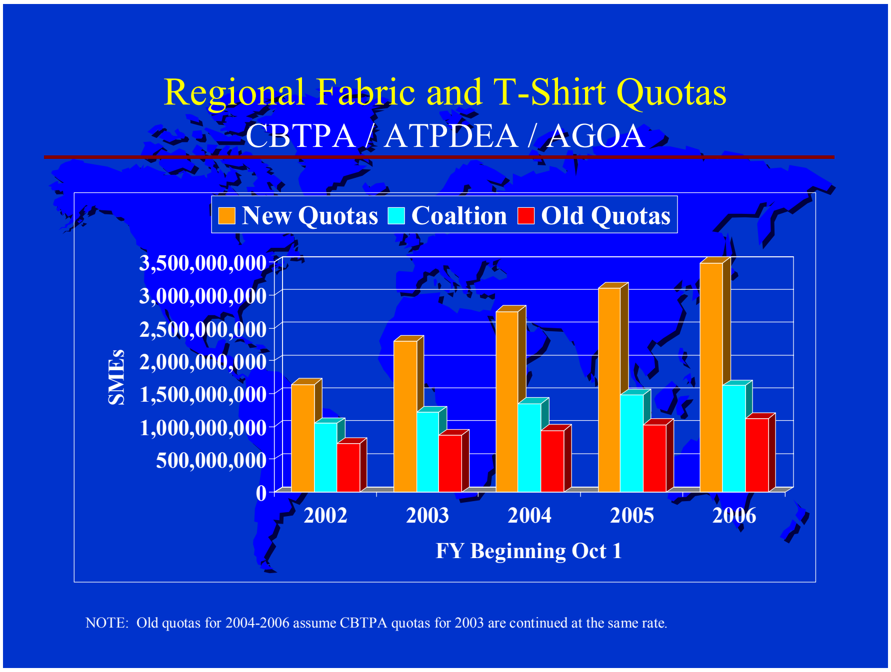

Figure 21. Regional Fabric Quota Comparisons.

Figure 22. Summary.