

3. Reforming NAFTA's Agricultural Provisions

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NAFTA's agricultural provisions have always been controversial, particularly for people in Mexico. Mexico's geographically-based comparative advantages in supplying off-season fruits and vegetables to a hungry U.S. market were undeniable. Equally undeniable were the risks to Mexico's large smallholder population, many of whom relied on crops that competed with U.S. imports proposed for liberalization. NAFTA's

liberalization of agricultural trade produced the expected results, with staple crops and meats flowing south and seasonal fruits and vegetables flowing north. The problems

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relate to the social and environmental consequences of market failures that plague the sector and to asymmetries between the trading partners, which are particularly acute in agriculture. NAFTA should be reformed to guarantee a more sustainable and equitable plan for agricultural integration.

I. THE NEED FOR REFORM

Corn is emblematic of NAFTA's problems. In Mexico corn (maize) is produced by a wide range of growers, including a small number of high-yield industrialized farms and some three million smallholders employing a wide range of farming practices and generally getting yields one-third (or less) of those of U.S. producers. Add to this already-vast asymmetry at the time of NAFTA's implementation the high levels of U.S. corn subsidies and the Mexican government's commitment to reduce its own extensive systems of support. When the Mexican government unilaterally liberalized corn markets, well ahead of NAFTA's 14-year transition schedule, U.S. corn flooded the Mexican market. Over two million people have since left agriculture, a drop of more than 25 percent.¹ With limited employment-generation elsewhere in the economy, many have added to the rising flow of migrant laborers.²

The trade flow results of NAFTA's agricultural provisions have been entirely predictable, if accelerated by Mexico's unilateral liberalization of most crops:

- Mexican producers increased exports of fruits and vegetables to the United States significantly. Exports came overwhelmingly from a small number of states with highly industrialized agriculture and relatively developed infrastructure. Though there was employment growth, new jobs were limited in these capital-intensive production systems, except for a rise in seasonal employment filled by migrant labor from other parts of Mexico.
- U.S. producers saw some loss of market share in these sectors, though impacts were limited due to the seasonal nature of most Mexican production and restrictions on imports during U.S. growing seasons. (Impacts were limited in sugar due to a long-running dispute over the treatment of U.S. corn sweetener exports.)
- U.S. producers saw significant increases in their exports of maize, soybeans, meats, and a variety of other staple goods.
- Mexican producers of those same goods saw prices fall significantly (50 percent in real terms for maize) with the dramatic rise in imports. Though vulnerable families did not overwhelmingly abandon their farms, many entered or increased their participation in the migratory labor force, either seasonally within Mexico, permanently to growth centers in Mexico such as tourist areas, or permanently to the United States.

Thus the principal need for reform of NAFTA's agricultural provisions is rooted in the wide development gap between the United States and Mexico in key staple and food crops. The Mexican government did not take advantage of the transition periods built into NAFTA's liberalization schedule to improve the competitiveness of most producers, though the largest industrialized growers received some assistance. Promised public investment in yield-enhancing projects such as irrigation never materialized, in part because Mexico's financial crisis at the start of NAFTA and its bank bailout drained public coffers. But it is worth stressing here that a more sensible transition period and higher levels of public investment would likely not have addressed the asymmetries between the staple-food sectors in Mexico and the United States.

It is critical to address these problems because job creation in Mexico has been disappointing and poverty remains high, particularly in rural areas, fueling the migratory flow to the United States. Mexico's food dependency

has grown dramatically under NAFTA, and the food crisis, which sparked tortilla riots and protests, highlighted the fallacy that Mexico could count on the United States for a reliable supply of cheap food. Finally, weak regulatory regimes have contributed to repeated food-safety issues in highly integrated supply chains while providing little market oversight to prevent anti-competitive business practices.

II. OVERARCHING PRINCIPLES AND GOALS FOR REFORM

The main goal for reforming NAFTA's agricultural provisions is to address the continued asymmetries between Mexico's agricultural systems and those of its NAFTA counterparts and to restore public policy flexibility, principally in Mexico, to allow the government to address those asymmetries and the many market distortions that pervade agricultural trade. Successful measures should lead to improved food security, declining rural poverty, reductions in rural migration, greater attention to the environmental impacts of agricultural trade, and a slow shrinking of the gaps between Mexico and its agricultural trading partners.

Reform measures primarily involve concessions from the governments of the United States and Canada. What they get in return is the long-term economic prosperity of one of their most important trading partners, prosperity that will lead to increased trade in goods, reductions in Mexico's exportation of its people, and potentially reductions in social unrest and illegal business activities.

III. RECOMMENDED INSTRUMENTS, POLICIES, AND PROVISIONS

The reforms needed to achieve these goals are relatively straightforward but require political will, particularly in Mexico, to execute. Up to now, that political will has been lacking. For example, there are steps the Mexican government could take without changing the substance of NAFTA, to better protect and develop its smallholder sector, particularly in maize. Mexico can:

- Justify the imposition of protective tariffs as countervailing measures to offset high U.S. farm subsidies.
- Expand its own government support for smallholders, since subsidies are not restricted under NAFTA and Mexico's current support levels remain billions of dollars below the country's allowable limits under the WTO.

- Use its participation in the Cartagena Protocol on Biosafety to restrict imports from the United States, because they contain large quantities of genetically modified corn and Cartagena recognizes the precautionary principle.
- Seek voluntary export restraints from the United States on sensitive products such as white corn and beans.³

Deeper Reforms

To address continued asymmetries and Mexico's need for food security and livelihoods, more extensive reforms to NAFTA would be required.

Borrow from the Doha Round. NAFTA countries could incorporate into the agreement concepts now being developed in the Doha Round of WTO negotiations: special and differential treatment (SDT), special products (SP), and special safeguard mechanisms (SSM).

Special and Differential Treatment—The concept of SDT recognizes asymmetries in development between trading partners. NAFTA incorporated few SDT measures, and many of those in agriculture, such as the transition periods for sensitive crops, were not implemented. Asymmetries remain, and they are particularly acute in agriculture. SDT can be made concrete in NAFTA's agricultural provisions through:

Special Products—In the Doha negotiations, these are defined as crops of particular importance for food security, livelihoods, or rural development. At the WTO, much work has gone into defining criteria a country would need to meet to justify declaring a crop a special product. Current proposals call for granting developing

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countries the right to declare up to 12 percent of their agricultural tariff lines special products. Many of the import-sensitive crops grown by Mexico's smallholders would clearly meet these criteria, most notably maize and beans, the staples

of the Mexican diet. Farm groups have offered a minimum list of six agricultural products—maize, beans, milk, coffee, sugar, and meats—for SP status at the WTO. These and five others—wheat, sorghum, rice, eggs, and fish—are included in Mexico's Ley de Desarrollo Rural Sustentable as agricultural goods Mexico should

petition the WTO for SP status. All but coffee are import-sensitive products in North American trade. Because NAFTA supersedes the WTO, SP exemptions at the WTO would be largely meaningless for Mexico. Establishing a Special Product category within NAFTA, with clear and agreed criteria for its use consistent with emerging WTO disciplines, would by itself address many of the concerns over the impacts of NAFTA in agriculture. The proposed U.S.–Korea FTA offers a precedent for flexible treatment as it excludes rice from liberalization.

Special Safeguard Mechanism—NAFTA included an emergency safeguard measure consistent with the principle that developing countries be permitted to cushion their producers from import surges. The NAFTA clause expired with the completion of the final phase-out of protection in the transition period. This needs to be amended and made more timely and effective for the party affected by the import surge, in line with G33 proposals at the WTO.

Borrow from European integration. Others in this project address the need for public investment directed primarily toward Mexico to address asymmetric development, as with a revitalized North American Development BANK (NAD-BANK) with an expanded mandate and budget. Such North-South public investment certainly served the European Union well in its efforts to integrate disparate trading partners. As many have pointed out, the disparities are much greater in North America. The NADBANK funds have been miniscule by comparison to EU integration funds. Such funds would be critical to addressing asymmetries in agricultural development. Mexican researchers have shown that Mexico could more than double the country's maize production using existing technologies if there were public investment in communications infrastructure, irrigation, credit, and agricultural extension. Most important, the water-rich areas where such investment makes the most sense are in the relatively underdeveloped southeastern parts of Mexico.⁴ Such poverty-reducing public investments are beyond the resources of the Mexican government alone. They would go a long way toward addressing several of the persistent market failures in the sector.

Address environmental externalities. Environmental externalities abound in agriculture. When more highly industrialized, high-input agricultural systems, with many negative externalities, are brought into direct competition through trade with more sustainable low-input systems, with their positive externalities, the effect is what has been referred to as the globalization of market failure.⁵ The management of agricultural trade needs to take such externalities into account, recognizing, for example, that the price of chemical-intensive U.S. corn does

not reflect its true costs, nor is the true value of the native Mexican maize it is displacing reflected in its market price.⁶ It is unlikely such costs and values will soon be incorporated into market-based pricing mechanisms. It will be important to develop payment for environmental services schemes, backed by public funds, to address the problem.

Respect precaution, protect maize biodiversity. Special measures should be taken to protect maize biodiversity in Mexico, the center of origin for this important global food crop. The issue of genetically modified corn is of particular importance and highlights both the promise and the failure of NAFTA's environmental regime. Through a model and inclusive citizen-petition process, the CEC commissioned a high-level study of GM contamination, first documented in Oaxaca. The wide-ranging peer-reviewed study, completed in 2003, may still represent the most exhaustive research into transgenic gene flow ever conducted. The findings included the clear recommendation that more precaution was warranted, particularly in the importation of GM corn in kernel form from the United States, the likely source of the contamination.⁷ Not only was this study largely suppressed due to opposition from the three governments (the papers still have not been published in book form), the recommendations from NAFTA's environmental body have been ignored. Clearly NAFTA's environmental institutions need more teeth, a matter that is addressed in more detail by others.

Reform related intellectual property rules. A reformed agreement should allow parties to exclude living organisms from patenting, permit *sui generis* systems to protect native plant varieties, require disclosure of the sources of genetic material used in new inventions, and observe the highest standards for consent and benefit-sharing. NAFTA should recognize the pre-eminence of important environmental treaties, as recommended in the Environment chapter of this document, particularly the Convention on Biological Diversity and the Cartagena Protocol and the International Treaty on Plant Genetic Resources for Agriculture, known as the Law of the Seed.⁸

Address market concentration and commodity market speculation. Anti-trust enforcement has been weak to non-existent in both the United States and Mexico. This has serious implications for agricultural markets, which were highly concentrated before NAFTA took effect and are even more so now. There is an urgent need to address competition issues in agriculture, as are measures to regulate speculation in commodities markets. Financial speculation generates price increases and volatility through U.S. commodity exchanges, which

undermine cash prices and reduce public and private investments in agriculture, due to the unpredictability of rate of return. Because anti-competitive business practices and speculation represent significant distortions to agricultural markets, government measures to correct those distortions are warranted. Again, the use of a more expansive and effective SSM could help address such issues in the absence of effective anti-trust enforcement. For example, when the full liberalization of NAFTA's agricultural provisions was imminent in January 2008, the large corn buyers that control an overwhelming share of flour markets used the threat of purchases in the United States to drive down producer prices at key harvest times in Mexico. Such uncompetitive practices need to be regulated, and governments need to be empowered to intervene.

Ideally, a tri-national body would oversee competition issues as they affect cross-border trade. For example, livestock operations are now highly integrated, with different operations performed in different countries. Ranchers have long complained of anti-competitive practices, such as so-called "captive supply" by packers that can result in price manipulation. Regulating such practices is now beyond the scope of any one government, suggesting the need for stronger measures at the regional level. Similarly, anti-trust actions in response to proposed mergers and acquisitions (M&A) are empowered only to address competition issues within each nation's borders. Given the levels of integration, in agriculture and other sectors, NAFTA needs a tri-national body to establish clear regulations for M&A activities that may contribute to uncompetitive business practices.

Other Suggested Reforms

There are many additional reforms that would improve the integration of North American food and agricultural markets. A few are worth noting briefly.

Grain reserves. Public food reserves are critical both to food security and to smoothing the price volatility that characterizes most agricultural markets. A well-functioning regional grain reserve for a key crop such as corn could ease price volatility while improving food security.

Allowing an international coffee agreement. NAFTA explicitly forbids Mexico from entering into any new international coffee agreement that restricts trade in coffee (Art. 703.3). Such international supply-management schemes should not be excluded by NAFTA. In fact, the recent volatility in commodities prices highlights their value in stabilizing markets.

Improved food safety regulation. The lack of effective continental food safety and animal and plant health regulations has caused significant disruption to agricultural trade. The current NAFTA sanitary-phyto-sanitary (SPS) rules and the related consultation process are not adequate to address the underinvestment in SPS infrastructure, training and best practices, which has resulted in trade disputes.

NAFTA has shifted agricultural trade in North America in predictable ways. The social and environmental consequences of those shifts are severe and should be addressed. Mexico remains far behind its North American counterparts in agricultural development. These asymmetries should have been addressed before liberalization proceeded, particularly in sensitive crops. They should be addressed now.

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2 Polaski, S. (2006). *The Employment Consequences of NAFTA*. Testimony Submitted to the Senate Subcommittee on International Trade of the Committee of Finance. Carnegie Endowment for International Peace. Available at: www.carnegieendowment.org/files/naftawrittentestimony.pdf.

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7 See the online studies at the North American Commission for Environmental Cooperation (NACEC). *Maize and Biodiversity: The Effects of Transgenic Maize in Mexico*. Retrieved August 6, 2009, from NACEC website: www.cec.org/maize/resources/chapters.cfm?varlan+english.

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