U.S. Agriculture Trade Update – December 2011
Department of Economic Analysis

In this edition:

- EU Debt Crisis Update: Bob Young, Chief Economist
- FTA Update, WTO COOL Case, Russia WTO Accession, EU Investigation of U.S. Ethanol Subsidies, China Cotton Purchase, Trans Pacific Partnership, Mexico Trucking, USDA Outlook for U.S. Agricultural Trade: Veronica Nigh, Economist

Recommended Links:

- Outlook for U.S. Agricultural Trade

Next Quarterly Trade Update:

- March 1, 2012

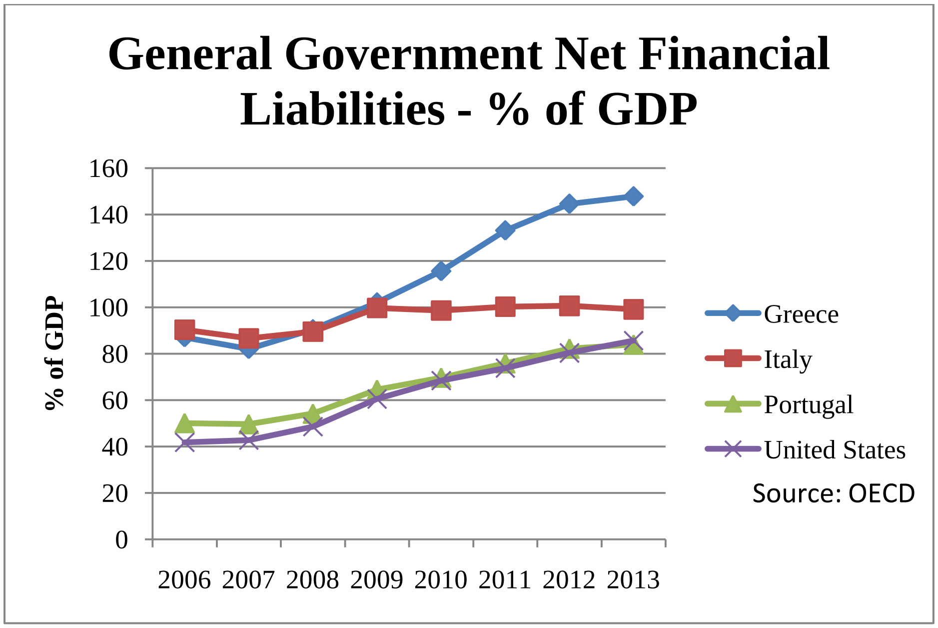
Over the last few years it's been pretty easy to write a trade newsletter: Doha is deadlocked, the FTAs with South Korea, Colombia and Panama show no movement, what is the U.S. trade strategy, does the U. S. have a trade strategy, the U.S. responds to WTO dispute against it, etc. Does this sound familiar? It's been a slow few years, but my how things can change in just a few months. We've got a lot of developments to discuss, a lot of them are positive, some negative, and some that could go either way.

EU Debt Crisis – Why Do I Care?

Seems like every day there's another installment in the whole EU debt crisis debacle. The whipsawing it has created in our own equities markets ought to be enough to capture your attention just on its own. Triple digit swings in the Dow on a daily basis – sometimes big triple digits – have become a common occurrence.

Another reason for concern is the effect it could have on our own banking system. To the extent our banks and other financial institutions have exposure to the debt issued by Euro zone countries, they could find themselves at significant risk if a default or even a breakup of the Euro were to occur. Think of the wipeout of MF Global as a good example or the pounding Bank of America stock has taken over the last few months because of their holdings.
But what are some of the other more fundamental issues and lessons we can take from this whole affair?

Probably the most fundamental lesson to be learned as we watch the governments of Greece, Spain, Portugal and Italy face phenomenal increases in the cost of borrowing money is: never get yourself in that position to begin with. But we don't seem to be willing to heed that lesson. In fact when you look at the numbers, we're actually not all that different than say, Portugal. And we can almost see Italy from where we are.



The markets have turned against these countries because there is at least some expectation that they could default on their sovereign debt. In order for investors to take on this perceived increase in risk, the price of the bond has to go down, which directly translates to higher interest rates. And we have seen the interest rates Greece now has to pay for investors to buy their bonds jump up to over 20%.

The United States is still seen as a very safe haven for investors to park their money. That's essentially why our government bonds are still going for historically low interest rates. Auctions of our bonds tend to have far more interested buyers than we have bonds to sell as money coming out of Europe looks for a home. In short, the United States can act like it is above all of this fray.

But that would be exactly the wrong signal to take.

One of the truly frightening things to come out of this entire process is how fast the markets can turn against a country once the doubt has crept in. The difference now between Italian and German debt is over 4%. The average interest the United States is now paying on our debt is 2.85% and the total cost of debt service for 2011 was $454 billion. Imagine that impact of that average interest rate just going up 1 or two full percentage points.

That's a lesson we should be taking from this entire crisis.

Free Trade Agreements

On, October 21, 2011, President Obama signed three bilateral free trade agreements between the United States and Korea, Colombia and Panama.

Once implemented, it is estimated the agreement with South Korea will bring a $1.9 billion gain for U.S. agriculture exports and would eliminate two-thirds of tariffs immediately. The Colombia agreement will bring a $370 million gain in agriculture exports and will eliminate 80 percent of tariffs immediately while the Panama agreement will bring a $46 million gain in agriculture exports and will eliminate 50 percent of tariffs immediately.

The legislatures of Colombia, Panama, and most recently on November 22, 2011, South Korea, have ratified their respective agreements. Now that the U.S. and each partner have signed the agreements, partner countries will meet to review both countries' laws and regulations, and ensure compliance with the obligations of the agreement that will take effect on the day the agreement enters into force. The provisions of the FTAs provide for entry into force, the official start of agreement implementation, through the exchange of formal diplomatic notes at a time agreeable to both countries.

It is widely expected that the U.S.-Korea FTA will be the first of the three to enter force. South Korea's National Assembly made all the necessary changes to their domestic laws, 14 in total, at the same time that it consented to the KORUS FTA. The exact time table for the implementation of the agreements will be determined in mid-December. Both the U.S. and Korean leadership are pushing for FTA implementation as soon as January 1, 2012.

The Panama and Colombia FTAs will likely take longer to implement, both due to necessary changes in their domestic laws, and because of political complications. As U.S. trade officials travelled to Colombia and Panama during the second week of November to formally kick off the process of implementing the free trade agreements. In order to bring themselves in line with their FTA commitments, the legislatures of both countries need to ratify several international treaties related to intellectual property. Panama will have to implement measures to comply with the FTA is by changing the way in which it administers its tariff-rate quota system. The FTAs can only enter into force once the President Obama certifies that Colombia and Panama have taken the necessary measures to comply with the provisions of the deal that go into effect immediately. At present, there is no indication of how long the implementation process with Panama and Colombia will take. It is speculated, however, that the implementation process could still take eight or nine months, though is unlikely that it will take a longer than a year.

WTO COOL Case Heats Up

On November 18 the World Trade Organization (WTO) released the details of dispute settlement findings against the U.S. on country-of-origin-labeling (COOL) of meat. Separate cases were brought by Canada and Mexico, and the U.S. asked that a single document be released with two Panel Reports, one for each case. The U.S. has 60 days to appeal the decision, which it will likely do, or "a reasonable period of time" to come into compliance or face punitive tariffs on exports from the U.S. to Canada and Mexico equal to the benefits of the lost trade.

The primary finding of the panel was that the COOL muscle meat labels violate Articles 2.1 and 2.2 of the TBT. The ruling determined that COOL, particularly in regard to the muscle cut meat labels, violates Article 2.1 because it affords imported livestock treatment less favourable than that accorded to like domestic livestock; and the COOL measure violates Article 2.2 because it does not fulfil the objective of providing consumer information on origin with respect to meat products.

Article 2.1

In the context of muscle cuts, the Appellate Body determined that the COOL measure accords less favourable treatment to imported than to like domestic livestock through three means. First, they found that the different categories of labels under the COOL measure accord different treatment to imported livestock. Second, the COOL measure involves segregation and, consequently, differential costs for imported livestock. Third, through the compliance costs involved, the COOL measure creates any incentive to process domestic livestock, thus reducing the competitive opportunities of imported livestock.

Article 2.2

The Appellate Body found that overall, the mandatory labelling scheme under the COOL measure falls short of providing consumers with information on the country of origin of meat products in an accurate and clear manner.

They acknowledge that labels required to be affixed to meat products according to the requirements under the measure provide additional country of origin information that was not available prior to the COOL measure. They also agree that the labelling requirements under the COOL measure may have reduced consumer confusion that existed under the pre-COOL measure and USDA grade labelling system.

However, they agreed with the Mexico and Canada that origin information on labels as prescribed by the measure does not ensure meaningful information for consumers, except origin information on Label A. Specifically, considered in light of the origin definition as determined by the United States for meat products, the description of origin for Label B and Label C is confusing in terms of the meaning of multiple country names listed in these labels. Moreover, the possibility of interchangeably using Label B and Label C for all categories of meat based on commingling does not contribute in a meaningful way to providing consumers with accurate information on origin of meat products.

Now What?

The U.S. must notify the Dispute Settlement Body of its intention to appeal within 60 days. If the U.S. decides to appeal, it must be limited to issues of law covered in the panel report and legal interpretations developed by the panel.

Bottom line: Unless the U.S. appeals the ruling and then receives a favorable appeal ruling, COOL law will need to be repealed or rewritten in order for the U.S. to meet its obligations to global trading partners.

Russia WTO Accession

It seems that Russia's bid to become a member of the WTO has finally come to a successful conclusion. Russia's accession package was adopted in the Working Party on the Accession of the Russian Federation on 10 November 2011. The Working Party will send its accession recommendation to the 15 - 17 December 2011 Ministerial Conference, where Ministers are expected to approve the documents and accept Russia as a WTO Member.

What finally made the deal possible was a package, brokered by Swiss mediators, that includes an agreement between Georgian and Russian governments that will put in place sophisticated systems for cargo tracking and audit as part of an international monitoring of trade to be carried out by a neutral private company.

Market Access Package

The final market access agreement has yet to be publically released, but we definitely now know some of the highlights on the negotiated tariff schedule and the final TRQ volumes. In the case of Russia, 80-90% of its commitments will be implemented up front.

First, the tariff schedule: Vegetables, fruits and nuts that are not grown in Russia will become cheaper. The tariffs for oranges, mandarins, pineapples, mangos, pistachios and peanuts will not be above 5 percent. The tariffs for imported milk, cream powder and condensed milk will be reduced from 25 to 20 percent. Wine and beer will become cheaper: tariffs for wine will be decreased from 20 to 12.5 percent, the ones for beer from 60 eurocents to 1.8 eurocents per liter.

Second, the final TRQ volumes:

Chicken:
- ***TRQ 1***: 250,000 MT frozen, boned chicken parts, Global TRQ, IQ: 25%, OQ: 80%
- ***TRQ 2***: 100,000 MT frozen, mechanically de-boned chicken, Global TRQ, IQ: 25%, OQ: 80%, EU-country specific allocation: 80,000 MT

Turkey:
- ***TRQ***: 14,000 MT, turkey, Global TRQ, IQ: 25%, OQ: 80%

Pork: Phased out by 1/1/2020, and replaced by a single 25% tariff
- ***TRQ 1***: 400,000 MT fresh, chilled and frozen pork, Global TRQ
- ***TRQ 2***: 30,000 MT pork trimmings, Global TRQ, IQ: 25%, OQ: 80%

Beef: Extended indefinitely, but if unilaterally eliminated, all beef subject to a single 27.5% tariff
- ***TRQ 1***: 530,000 MT frozen beef, Global TRQ, Country specific allocations: EU: 60,000 MT, U.S.: 60,000 MT, Costa Rica: 3,000 MT, IQ: 15%, OQ: 55%,
- ***TRQ 2***: 40,000 MT fresh and chilled beef, Global TRQ, IQ: 15%, OQ: 55%,

Whey:
- ***TRQ***: 15,000 MT, Global TRQ, IQ: 10%, OQ: 15%

Domestic Support

We also now know what level of trade distorting support, Current Total Aggregate Measure of Support (CTAMS), Russia can provide its agricultural producers. Russia's CTAMS of $9 billion will be reduced to $4.4 billion by 2012. For reference, the U.S. is capped at $19.1 billion. An additional constraint for Russia, Product-Specific Support is capped at 30% of CTAMS cap would be in place until December 31, 2017. All agricultural export subsidies are eliminated.

Permanent MFN

President Obama and U.S. Trade Representative Ron Kirk have highlighted the need to extend permanent most favored nation (MFN) status to Russia or else risk putting U.S. exporters at a disadvantage. Without permanent MFN in place, the U.S. will have to invoke a non-application clause which will mean U.S. exporters will not get the full benefit of Russia’s concessions made as part of its WTO accession package.

Section 401, Title IV of the Trade Act of 1974 – also known as the Jackson-Vanik amendment- requires Russia and seven other former Soviet states to comply with free emigration policies before enjoying normal trade relations with the United States. The U.S. Congress must vote to remove

Russia from Title IV of the Trade Act before the U.S. president can grant Russia permanent normal trade relations (PNTR).

EU Takes Up Investigation of U.S. Ethanol Subsidies

The EU's trade authority announced November 29 that it is starting Antidumping and Countervailing Duty investigations of U.S. ethanol exports. They will try to determine whether US ethanol exporters are receiving unfair state subsidies and selling their fuel to Europe at illegally low prices. Specifically, trade officials will investigate EU industry allegations that the Volumetric Ethanol Excise Tax Credit (VEETC) and Small Ethanol Producer Tax Credit in the US allow its exporters to cut their EU selling price. The European Commission investigation could result in import tariffs as early as next year on millions of gallons of the fuel if EU officials unearth evidence of unfair trade practices in the US.

The investigation was predicated on a recent surge in U.S. exports of ethanol to the European market. Year-to-date U.S. ethanol exports to the EU reached 210.8 million gallons, a 181% increase from the 75.2 million gallons exported January-September 2010. Total year-to-date U.S. ethanol exports to the world have surged to 746.5 million gallons. A considerable amount of US ethanol exports are being shipped to meet ethanol use requirements in the importing market.

The association of European renewable ethanol producers, ePURE, which requested the European Commission to investigate imports of fuel ethanol from the United States, had this to say "This impressive trend is the direct result of US federal and sub-federal subsidies, which allow US operators to adopt aggressive pricing practices on the European market. These very low prices have a direct and negative impact on the EU industry: the European ethanol industry is very small in comparison to the US industry and a lot of ethanol producers are still in a take off phase." We will keep you up to up to date as this case unfolds.

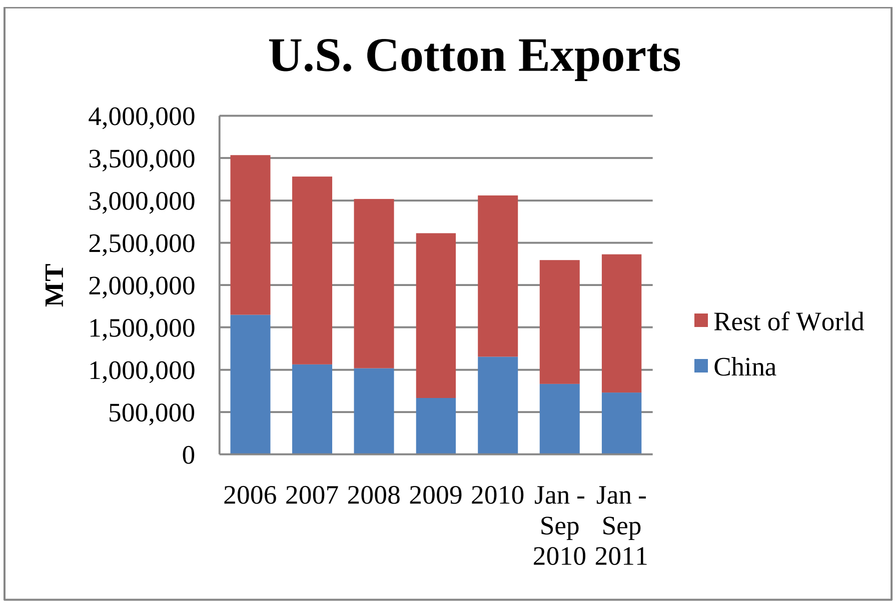
Also interesting, on the import side, year-to-date U.S. ethanol imports reached 172.9 million gallons, an 86% increase over January-September 2010 imports. Most of the imports are from Brazil, going into California to meet their low carbon fuel standard and to help fill the advanced biofuel subcategory of the RFS. The tables below give a fuller picture of the degree of ethanol swapping that is occurring in the global market.

US Denatured and Undenatured (non-beverage) Ethanol Exports								
Area/Partners of Destination	2006	2007	2008	2009	2010	Jan - Sep 2010	Jan - Sep 2011	Period/Period % Change
	Million Gallons							
World Total	36.9	150.2	157.8	113.3	403.5	250.1	746.5	198
European Union-27	18.2	118.3	128.5	54.3	119.4	**75.2**	**210.8**	**181**
Canada	7.9	23.6	21.2	18.0	116.4	76.1	189.4	149
Brazil	0.0	0.0	0.0	1.5	21.6	14.0	**202.0**	**1,347**

US Denatured and Undenatured (non-beverage) Ethanol Imports								
Area/Partners of Destination	2006	2007	2008	2009	2010	Jan - Sep 2010	Jan - Sep 2011	Period/Period % Change
	Million Gallons							
World Total	720.6	508.4	578.3	286.5	124.5	93.1	172.9	86
Brazil	452.8	225.2	247.1	65.7	77.6	52.6	**85.8**	**63**
Canada	21.1	22.2	14.8	26.4	26.6	22.5	15.0	-33

China Back in the Cotton Market in a Big Way

China recently made its largest purchase of U.S. cotton in eight years. Growers and merchants sold China 217,015 MT (996,100 bales) of upland cotton in the week ended Nov. 4, says USDA, the most sold in one week since October 2003. The chart below does not include the recent purchase, but is included for context. U.S. 2011 calendar year exports of cotton are on pace to exceed 2010 exports, which were up 17% from the 2009 level. Large purchases by China only help.

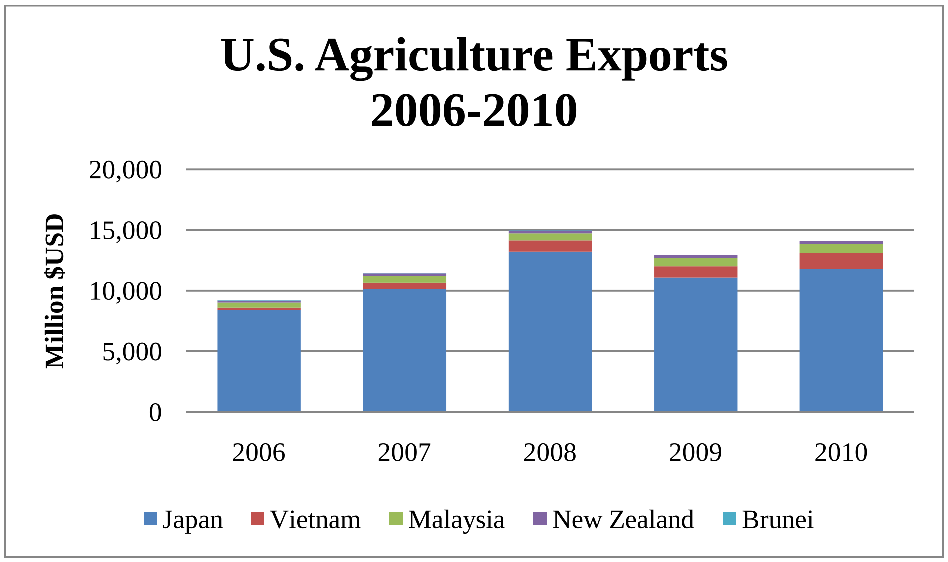


Room for More at the Trans-Pacific Partnership (TPP) Table?

On November 12, 2011, the Leaders of the nine TPP countries – Australia, Brunei Darussalam, Chile, Malaysia, New Zealand, Peru, Singapore, Vietnam, and the United States – announced the achievement of the broad outlines of an ambitious Trans-Pacific Partnership (TPP) agreement at the annual summit of the Asia-Pacific Economic Cooperation forum. A successful agreement could turn TPP into the most significant economic bloc on the planet, larger than the European Union. Taken together, the TPP nations would be America's fifth-largest trading partner.

Despite the good news and already large potential, it was Japan that stole the show with its own announcement. The stakes grew even larger when Japanese Prime Minister Noda signaled his country's interest in joining the talks. Japan's interest quickly prompted Canada and Mexico to say that they might want a seat at the table as well.

While the addition of Japan (and Canada, and Mexico, and…) has peaked traders' interest, leaders from the existing TPP partners have repeated numerous times that the goal is to finish the negotiations by 2012. Despite the large opportunities, negotiators fear that the addition of more parties will slow the negotiations down and prevent the completion of a successful agreement according to schedule. Many question whether Japan is willing to take on the necessary reforms of its agricultural sector, which has been the primary obstacle to broader efforts at liberalization for the country. With that large question aside, the potential is clear. U.S. agricultural exports to existing TPP partners with which we don't already have an FTA are dwarfed when compared to Japan. Decisions about taking on additional members will be made soon. Leaders of the nine TPP countries have instructed negotiators to meet in early December. Scheduling of additional negotiating rounds will also be determined at that time.



Whether Japan, or any other country, joins the TPP negotiations or not, one thing is clear, the Obama administration needs Trade Promotion Authority. Thankfully, USTR Ron Kirk signaled on December 1 that the administration intends to do just that. Under TPA, the administration can negotiate trade deals with other countries or trading partners and bring them to Congress for an up-or-down vote with no amendments allowed. Kirk said that TPA would be needed to complete talks for the Trans-Pacific Partnership next year. Farm Bureau supports the renewal of trade promotion authority.

<u>Mexico Trucking …Again</u>

You will recall that in July, U.S. Transportation Secretary Ray LaHood gave the go-ahead for an 18-month pilot program allowing Mexican trucks to enter the U.S. from approved companies, seemingly ending the Mexico Trucking Dispute. In response to the announcement, Mexico agreed to cut the tariffs it had been applying in retaliation in half earlier, with the remainder to be dropped when the first Mexican trucks began entering the U.S.

Mexico lived up to its end of the bargain and dropped all retaliatory tariffs at the end of last month. Naively, many of us thought that we had seen the end of the trucking dispute for a while. However, on November 23, the International Brotherhood of Teamsters, Public Citizen and the Sierra Club filed suit to block Mexican trucks from operating in the United States, giving new breath to the debate.

This new, and potentially negative, development comes as growth in trade between the United States and its NAFTA partners has been rebounding for the poor economic conditions of the last few years. The Bureau of Transportation Statistics reports that "trade using surface transportation, was 13.8 percent higher in September 2011 than in September 2010, totaling $77.7 billion, according to the Department of Transportation. The value of U.S. surface transportation trade with Canada and Mexico, the United States' North American Free Trade Agreement partners, in September 2011 rose 35.7 percent in two years from September 2009 and 8.3 percent in three years from September 2008."

So far the suit hasn't disrupted trade, but we'll keep you informed as this case unfolds.

USDA Outlook for U.S. Agricultural Trade

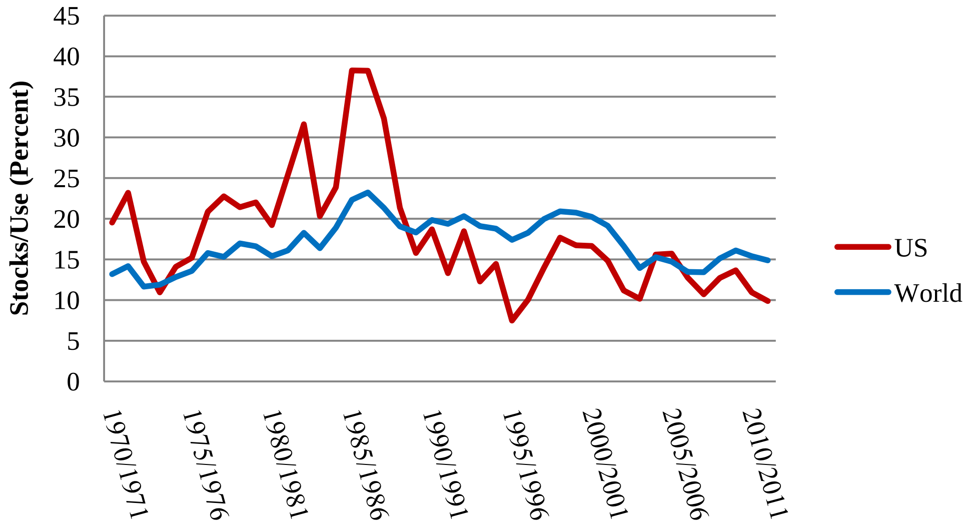
On November 30, 2011 USDA released their quarterly Outlook for U.S. Agricultural Trade. Fiscal 2012 agricultural exports are forecast at $132 billion, down $5 billion from the August forecast and 4 percent ($5.4 billion) below final fiscal 2011 exports of $137.4 billion. The decline is primary attributed to wheat (down $2.2 billion), corn (down $1.3 billion) and oilseeds and products (down $2.3 billion). Livestock products including red meat and poultry exports on the other hand are forecasted to increase by $0.9 billion. Despite the downward revision, if exports reach the $132 billion forecast, 2012 agricultural exports will be the second highest on record.

U.S. agricultural trade, fiscal years 2008-12, year ending September 30						
Item	2008	2009	2010	2011	Forecast fiscal year 2012	
					Aug.	Nov.
	Billion dollars					
Exports	114.9	96.3	108.7	137.4	137	132
Imports	79.3	73.4	79	94.5	105	105.5
Balance	35.6	22.9	29.7	42.9	32	26.5

Source: Compiled by USDA using data from U.S. Department of Commerce, Census Bureau.

Declines are primarily led by increasing downward pressure on prices as the world market builds wheat, corn and soybean stocks and improves the stocks-to-use ratio. The ratio of global ending stocks to total use can be a reliable indicator of market prices. The stocks-to-use ratios for wheat and rice suggest reasonably comfortable stock levels. Currently, the global stocks-to-use ratios for corn and soybeans are improving from the near record lows of the recent past.

Stocks-to-Use Ratio for Total World Grains and Oilseeds



Source: Compiled by AFBF using data from USDA's World Agricultural Supply and Demand Estimates and Production, Supply, and Distribution Database, November 2011.