EU-US Trade and Investments Partnership:

Outline of a possible negotiation strategy for EU agriculture

The Transatlantic Trade and Investment Partnership (TTIP) negotiations were launched on June 17, 2013.

TTIP aims at creating the largest Free Trade Area in the world, and at setting a host of harmonized standards between the two largest trading blocks. These common standards could, by the sheer size of the trade affected, become the de facto new world standards.

TTIP's expected level of ambition surpassed anything achieved so far, setting the pace for further trade deals and hopefully prompting other countries to move forward in the stalled WTO negotiations.

The impact of TTIP on the agriculture sector could be large, larger than any other free trade deal negotiated so far, and larger than what was expected out of the WTO Doha round (with the exception of domestic subsidies).

It is therefore hardly surprising that the reactions to the TTIP in the EU agricultural sector have been mostly cautious, defensive. The sector by and large fears the impact of concessions that could be made to a more competitive US agriculture.

Farm Europe attempts to go beyond the usual positioning, and to provide a more focused and realistic assessment of the deal. This paper also explores the dynamics of the negotiation. Some sectors might benefit, others will face additional competition. In particular with regard to those facing additional competition, Farm Europe outlines what could be done to improve the EU position.

The state of negotiations

Tariff offers were exchanged on February 10, 2014. However the initial drive to quickly conclude the TTIP negotiations ("in one tank", as it was put at the time) has faced a set of roadblocks in a number of areas since 2014.

There were misunderstandings on what the level of ambition of the tariff offers exchanged should be, with the EU accusing the US of presenting an offer that could hardly be accepted as a basis for negotiation.

Also, a high-stake political controversy arose on the ISDS (Investor-State Dispute Settlement) chapter, with very active and vocal opponents within the EU to be found in some NGOs, and even in some mainstream political groups. That controversy found an echo across the Atlantic, with strong opposition to ISDS heard also from sectors in the US Congress.

The EU also felt a lack of commitment from the US side, explained by the fact that the US would have prioritised the conclusion of the TPP (Trans Pacific Partnership) negotiations.

The result of these drawbacks was that progress in the negotiations was lacklustre, to say the least.

Agricultural issues remain contentious, particularly those perceived as consumer safety issues - e.g. hormone treated meats, GMOs. The EU, at its highest level, was obliged to reaffirm that it would never accept imports of hormone treated meat, nor lower high EU safety standards.

Following the change in the Commission in late 2014, there was a new push to inject fresh momentum into the talks. It is still early days to evaluate the success of the new attempts to revive the talks, but there are indications that prospects are brightening.

The US President has finally obtained TPA (Trade Promotion Authority), which is seen as essential to conclude TPP and TTIP. TPA gives Congress the authority to only accept or reject in block a trade deal, preventing cherry-picking of parts, which was clearly a great concern for countries negotiating with the US.

The US and her TPP partners are now moving to the end game of the negotiation, which would free the US to turn its eyes towards the EU.

It is also to be expected that President Obama would like to leave these two very large trade deals as part of his legacy.

Therefore there are strong indications that TTIP negotiations are bound to resume and accelerate by the end of 2015, with a view to some form of conclusion in 2016. Agricultural market access and regulatory issues will continue to be a major challenge for US and EU negotiators as they embark on more intensive negotiations. Also of interest to these negotiations are recent farm policy reforms in both the EU and the US.

The results of EU CAP reforms, which have increased EU's competitiveness for certain commodities (e.g., dairy and sugar), as well as the outcome of other EU FTA negotiations, in particular with Canada, are of significance to TTIP.

How far these developments will inform the EU negotiating position is an open question. It could be expected that they do not guarantee an ambitious result, in part due to concerns that further liberalisation might jeopardise the EU's still fragmented farm sector. Moreover, EU farm organisations have taken keen note of the results of the recently agreed FTA with Canada (CETA), in particular with respect to beef and pork market access. When they extrapolate CETA to what might be the potential outcome of a FTA with the United States, a bigger and more powerful partner, they become more wary about providing additional concessions.

To compound these anxieties, and likely fierce resistance to any ambitious deal, these groups are also taking into account the offers exchanged with Mercosur, another big agriculture player. While conclusion of the Mercosur negotiations is not expected any time soon, there is a strong concern that, in the future, a deal might be reached at least with Brazil, a top agricultural exporter and competitor.

In this context, the negotiations with Japan could provide some breathing space for the most affected sectors, and help to counterbalance the impact of TTIP to a certain extent. Japan is a significant importer of meat and grain products, and the EU will play an offensive role on agriculture in this FTA.

In March 2013, the United States adopted a new farm bill, which modifies support programs for most field crops (wheat, maize, oilseeds, cotton, peanuts) by eliminating decoupled direct payments and introducing new risk management programs and encouraging the use of crop insurance, coupled with conservation requirements. US dairy support has become more market-oriented, reflecting the increasing competitiveness of this sector in world markets. Possible changes to US biofuel policy, in the form of a reduced renewable fuel standard, could also impact US crop production trends. While these policy reforms are unlikely to drastically change US market conditions, they are worth considering in the context of US farm sector expectations for these negotiations, particularly given EU largely higher tariffs and regulatory barriers.

Both the United States and the EU have complex domestic support systems, but neither side has agreed to negotiate domestic support policies in FTAs. Ironically, the U.S. justification for not negotiating on domestic support is that it will not agree to new disciplines if the EU is allowed to continue to support at high levels. While this objection could be addressed in a negotiation, neither side is likely to be motivated to negotiate domestic support.

The following summary identifies some of the key sectorial issues facing the agricultural negotiation and outlines Farm Europe's positions and recommendations. It highlights the practical difficulties facing negotiators and the basic questions posed to policy-makers: how far will this Free Trade Agreement actually free up trade in protected agricultural sectors? Where do the most important EU offensive interest lie? And where is the EU more vulnerable? What are the most significant challenges and how can they be accommodated?

General overview of Trade in Agriculture Products

In 2014, the EU had a nearly Euro 6 billion trade surplus in agriculture with the US.[1] This reflected a long-term trend of expanding exports of EU products and stagnant US imports, with the EU achieving a neutral trade balance in 1998, growing and maintaining a surplus for the next 8 years with no sign of change. In contrast, the United States has an almost $40 billion global agricultural trade surplus, while the EU has traditionally had a balanced trade account across the agricultural sector, with a very small trade deficit in 2012, the latest year for which data are available (Source: WTO).

In 2014, top US imports from the EU were spirits (Euro 3.3 billion), wine (Euro 2.8 billion), beer (Euro 1.2 billion), cheese and nonalcoholic beverages (Euro 0.7 billion each), and olive oil (Euro 0.7 billion). These are top EU exports globally, building on high quality food processing and strong brands.

Top US exports to the EU were led by oilseed products (Euro 2.3 billion), fruits and nuts (Euro 2.0 billion), spirits (Euro 0.7 billion), and wine and miscellaneous food preparations (Euro 0.4 billion each). Leading global US agriculture exports, such as beef, pork, poultry, dairy, maize, rice, and various fruits and vegetables were all less than Euro 200 million.

The simple average of US MFN agricultural tariffs is around 12%. The EU average is around twice that level (precise calculations are difficult, due to calculation methodologies for converting specific (e.g., Euro x/MT) tariffs into ad valorem equivalents (e.g., y %)). Studies generally show the average EU tariff to be two to four times the average U.S. tariff for agricultural products.

The EU has also to address a more diverse and fragmented sector than the US. A particular case at hand is that of the ultra-peripheral EU regions, where the economic and social fabric is particularly exposed to external pressures.

The EU is thus facing a paradox in TTIP: it benefits from a large and stable trade surplus with the US, but it has in general a less competitive and more protected agriculture.

[1] All 2014 data is for the EU-28.

Meat Products

The EU and the United States are roughly in trade balance in beef, pork and poultry products. Globally, the United States has exported over Euro 13 billion in these products per year, but exports to the European Union have never exceeded Euro 400 million. EU meat exports into the United States in 2014 were around Euro 600 million. While the US industry is a global leader in competitiveness, the EU focuses its exports on certain niches that exploit a strong reputation for high quality. In spite of the economic fundamentals, the surprising result of near trade balance in this sector is explained by high EU tariffs, low U.S. tariffs, gourmet consumers in the United States and SPS regulatory barriers.

US tariffs are relative low for these products (26% for beef outside of the large TRQ, and substantially lower for pork and poultry). EU tariffs are substantial, ranging from 40% to over 100% for most products. In addition, all three of these products face serious trade restrictions through sanitary barriers: the European Union bans beef treated with growth hormones (despite CODEX approval of these products and a WTO panel finding against the EU), bans pork treated with ractopamine (a growth promoter used in the United States and other meat exporters that has also been approved by CODEX), and bans U.S. poultry treated with pathogen reduction treatments, such as chlorine. Nevertheless, exporters in both the EU and the US have an interest in updating the bilateral veterinary equivalence agreement signed over 15 years ago.

The EU is eager to see BSE-related restrictions removed on its exports of beef products from all EU Member States, and for the US to recognise the EU as a single entity. US sanitary requirements are strong for pork and poultry also, but the EU has managed to service U.S. pork market niches with high priced products and is not considered competitive in poultry exports.

Different standards on animal welfare, which concern in particular the poultry and eggs sectors, are also an issue in the EU, where producers face higher standards and the related higher costs.

Tariff elimination in the meat sector would create a huge challenge for the EU meat and livestock sector, in particular if sanitary barriers were removed as well. The Commission (DG Agri) has estimated the elasticity of the European market to be around -5; a 20% reduction in tariffs could result in an increase in imports of approximately 100%.

As noted above, high tariffs are a constraint for US exporters, but sanitary barriers have effectively banned pork and poultry exports and limited beef exports to non-hormone production.

The EU has aggressively protected this sector in other FTAs, including in the recently-concluded agreement with Canada, but that did not prevent granting Canada preferential duty-free TRQs for pork (80,000 tons), beef (50,000 tons), and bison (3,000 tons). It is worth noting that these volumes were only reached at the last minute, and they do incorporate payment for Canadian concessions on GIs.

It should be underlined that although the EU is adamant not to accept imports of hormone-treated beef, it has accepted a TRQ for hormone-free beef. It should be expected that in TTIP the EU will also be obliged to grant significant market access to hormone-free US beef. No single sector will be excluded from the negotiations, and it is illusory to think that the beef sector, or other meat sectors, would be the odd exception. On the contrary, inclusion of beef and other meats is a necessary condition for the conclusion of TTIP from the US side, and the EU knows it.

Therefore, TTIP will inevitably have a significant impact on the EU meat sector, and in particular to the more exposed and fragmented beef production chain. The EU will have to open her beef market for hormone-free US beef, for volumes that will certainly not be lower than those agreed with Canada.

Any increase in imports will have a multiplied effect on the suckler cow sector: dairy cows constitute two-thirds of European supplies of beef to the common market. The supply of meat from the dairy cow herd is linked to the evolution of the milk market, the elasticity of this supply to the EU meat market being weak. Henceforth, the adjustments caused by the results of the TTIP negotiations will be above all bearing by the European industry of suckling cows.

The EU should rather anticipate the shock than pretend that it will not happen and try to manage its consequences ex-post. It is far better to prepare the sector to face more competition than to mend its consequences.

Farm Europe believes the key is to negotiate TRQs instead of accepting tariff elimination, and to buy enough time, through a long implementation period, to better structure the sector. In this context, the European Commission should be called to present a comprehensive plan without delay with appropriate financing means, to improve the structure of the sector, including producers and processors.

Dairy Products

Dairy products are one of the leading EU exports to the United States, led by cheese (Euro 0.8 billion in 2014). US dairy exports to the EU totaled just over Euro 0.2 billion in 2014. Both sides have market access through lower duties on tariff-rate quotas, with the EU having substantial access to the US market through country-specific quotas obtained through the WTO. Out-of-quota duties in the United States generally range from 30% - 50%, while EU out-of-quota duties are generally in the 50% - 150%, with some as high as 250%.

Non-tariff measures are a key problem to EU exports (Grade A certification, and other US food safety rules). TTIP should be the opportunity to address these issues and find simpler and better solutions. The EU is also critical of the role played by CWT (Cooperatives Working Together) on supporting US exports. Possibly the most contentious part of the dairy negotiation, after tariff negotiations, will be EU requests for the United States to claw-back the use of six common cheese names in the US market, such as parmesan or feta cheese, and to accept to market only geographic indications (GIs) made in Europe.

The EU has consistently pushed for the widest possible recognition of its GIs, particularly in the dairy sector. The EU has shown that she is prepared to pay for the recognition of its GIs through additional concessions in other sectors, as evidenced in the recent EU-Canada agreement where the EU obtained additional protection to its GIs by accepting larger concessions in the meat sectors. The value of recognising the six GIs, which are already exported to the US market lies in balance with the additional concessions that should most probably be given in exposed sectors, like beef and other meats.

The United States is a competitive dairy exporter, pushing other countries to remove tariffs aggressively in previous Free Trade Agreements. The EU, in the aftermath of the abolition of the milk quota, should also show now a more offensive stance in this sector to expand exports of its high value added products.

Farm Europe believes that TTIP should lead to free trade in dairy products and to the elimination of regulatory trade barriers. The value of additional protection to some EU GIs should be assessed through the lens of economic criteria to make sure that the benefits outweigh the costs.

Grains and oilseeds

Grain trade is largely composed of US exports to the EU. The United States is a leading global exporter and imports only limited quantities, usually specialty grains or product from Canada. The EU is also a leading wheat exporter, but imports rice and coarse grains and protects all grain markets with substantial tariffs. One should note, however, a gap in competitiveness in these sectors between the US and the EU which has tended to widen in recent years, and which is linked to the evolution of input costs and the stagnation of European yields.

Some access is afforded to the EU market through WTO commitments under TRQs and limits on the 'margin of preference' afforded to EU product compared to imports.

US exports to the EU have fallen substantially from thirty years ago. In 2014, US exports were just over Euro 400 million. US tariffs on grain are low, whereas EU tariffs range from 40% to 90% (except for husked rice, which are 10% - 20%).

US maize and maize by-product exports are constrained by the EU GMO policy. This has reduced the largest U.S. grain export and limited the ability of the United States to compete for the EU's WTO TRQ for maize established as compensation for loss of access during the Spanish and Portuguese accession to the EU.

US rice access to the EU has also benefited from terms negotiated in the Uruguay Round and the accession of the EFTA countries to the EU. Similarly, US wheat exporters have been able to gain some access to the EU market, in particular for high protein and durum wheat. However, the EU soft wheat and rice markets are both protected by high tariffs and reference price schemes. **Elimination of these tariffs in a bilateral agreement would be a substantial advantage to U.S. exporters.**

In the case of wheat, the results of the EU FTA with Canada, a direct competitor to the United States for this product, are particularly relevant as EU tariffs will be eliminated. This indicates that the EU can now compete on a stronger footing. **But regarding the US an issue of concern to the EU producers remains, as the new Farm Bill offers price coverage to US farmers, whereas the CAP relies on decoupled support, which is a disadvantage when prices are low.**

Turning to oilseeds, the EU is a significant importer of soybeans and soybean meal, driven by structural deficits in the EU animal feed sector and a MFN tariff bound at zero in the WTO. US soybean oil exports face moderate tariffs, less than 10%, enough to slow US exports. The United States imports negligible quantities of EU vegetable oils (other than olive oil, reported with the fruit and vegetable sector.)

Despite the zero or relatively low tariffs, US soybean and products exports are restricted by EU GMO policy, as noted above. This policy could also negatively affect the EU farming sector, as GMO-free imports are more costly, thus adding to the feed costs in the EU.

The EU biofuel policy is an even bigger issue in the oilseed sector for biodiesel. Production of biodiesel is an important outlet for the EU oilseed sector, and adds a significant amount of protein as a by-product, which is beneficial to the EU feed sector that suffers from a large protein deficit. For the EU sector to compete with the US it should benefit from a regulatory framework that provides stability and room for expansion.

Farm Europe expects that the TTIP could result in the elimination of tariffs in the grains and oilseeds sector. In this case, the EU biofuels policy should

enable the EU biodiesel production to expand, rather than serve to constrain it, to allow the EU to compete on an equal footing with the US. The internal distortive mechanisms in force in the Farm Bill should be taken into account by EU negotiators for any concessions such as for wheat, to ensure a level playing field for the EU sector, and specific protections should be maintained for certain highly sensitive products, like rice.

Starch and Ethanol

The EU starch industry has been constrained by a number of factors, unlike the US industry: the sugar regime limitations on the production of isoglucose, the higher maize and energy prices, and the lesser scale.

TTIP could bring about similar maize prices in the EU and the US. The end of the sugar quotas in 2017 will lift the limitations on the production of isoglucose. However, the other factors hampering the EU industry will remain intact.

The EU sector needs therefore time and investment to rise to the challenge of the competition from the US.

The same can be said about the EU ethanol sector, which relies more heavily on sugar beet as raw material, whereas in the US ethanol is made mostly out of maize. Previous and running US programmes have greatly helped the sector develop, whereas in the EU development is still at early stages. **Farm Europe is therefore of the opinion that the EU industry needs time and an appropriate regulatory framework and safeguards to meet US competition**.

Biofuels can be an important outlet for the EU grains and sugar producers. As biofuels production generates protein rich products, it has the potential to reduce the large EU deficit. **Farm Europe believes it is time to objectively evaluate the costs and benefits of producing biofuels in the EU, and factually assess its impacts including the mitigation of the EU protein deficit, instead of succumbing to prejudice and targeted campaigns**.

Fruit and Vegetables, Nuts and Olive oil

The United States has a growing trade surplus with the European Union in this sector. In 2014, U.S. exports were led by nuts, in particular almonds, pistachios, walnuts), and dried fruits.

Leading EU exports are olive oil at over Euro 0.7 billion and olives at over Euro 250 million in 2014. Some leading global US exports, such as oranges, orange juice, apples, grapes, and stone fruits have limited exports to the EU so far.

US tariffs in this sector are generally low, but a few products are still sensitive to import competition (including olive oil and olives). Olive oil standards could, however, be a sticking point in the negotiations, as US olive oil producers push for the approval of US-specific standards, which EU exporters believe will disadvantage their exports. EU tariffs are moderate in general, but are substantial for some import sensitive products that are export priorities for the United States, such as citrus (30% tariff), apples and pears (40%), and fruit juices (50 – 150%). In addition, the application of the EU entry price system to these products effectively raises the tariff on low-priced imports to protect high prices in the EU, and reduces imported quantities even as it helps to preserve high prices in the EU market.

The sector is highly diversified, but it can be argued that the EU has its own strengths and competition from the US is cushioned by the fact that the US production is concentrated in the west coast, increasing transport costs to the EU.

There are fewer high profile SPS barriers in this sector, although food safety laws are of growing complexity and concern on both sides. A genuine regulatory cooperation and simplification could bring tangible benefits for the EU sector. While in past FTAs the EU has protected the entry price system for these products, it is possible that the EU could view resolution of SPS issues affecting their products as a trade-off for the entry price system, which targets low price imports from other origins.

Farm Europe expects that free trade and the elimination of non-tariff barriers could be, in general, beneficial to this highly diversified sector, as long as rules of origin are strictly respected.

Wine and beer

The EU has a substantial trade surplus in wine and beer trade. US wine exports to the EU have increased, but still lag significantly behind US imports. Beer tariffs are zero in both countries (which is also the case for distilled spirits), but US wine tariffs (around 20%) are higher than in the EU (10% or less).

Trade in alcohol products is highly regulated in both countries. Eliminating non-tariff barriers is important to boost the benefits of trade. The bilateral wine agreement of 2006 envisioned further negotiations to align the two markets, which may occur in the FTA.

A package of import duties and taxes, from which US wines are largely exempt, apply to European wine exports to the US. While wines imported to the US are subject to a tax which varies depending on alcohol content, many US producers benefit from tax cuts in this area. This distortion in treatment is found on the state-level as well, where taxes and excise duties are applied to imported wines, while local producers have access to tax breaks and credits.

At the same time, the negotiations are also an opportunity for the EU to raise concerns regarding additional GI protection. However, the GI issues which remain (use of some generics and semi-generics) are limited.

Farm Europe defends that the EU should be offensive in this sector, building on the renewed competitiveness of its sector, and concentrate its efforts first and foremost at eliminating tariffs and non-tariff barriers in the negotiations.

Sugar and other Processed Products

The EU has a positive trade balance in processed products with the US. EU Exports are led by snack foods, roasted and instant coffee, spices and other consumer oriented products. US exports are led by snack foods, pet foods, and other consumer oriented products. The trade flows reflect the strength of EU brands for quality and niche products and relatively open US market for processed products.

US tariffs on processed products are generally low, unless there are dairy or sugar components in the product. EU tariffs can be substantial, as duties are based on a complex formula takes into account sugar, dairy, and starch components and calculates a duty designed to ensure the level of protection for these base products remains high. This system is generally referred to as the “Meursing Table”, and its reform has been a long-standing US objective.

As with reforms of the entry price system, the EU has been reluctant to reduce protection for processed products in bilateral FTAs. This impulse may be shared in the United States with respect to sugar-containing products, an area traditionally protected in the United States, where both the EU and US tariffs exceed 100% and where both will be concerned about importing third-party sugar incorporated into sugar-containing products.

However, for Farm Europe, the elimination of EU sugar production quotas after 2017 points to a more ambitious EU position for sugar and sugar-containing products over the longer term, as more competitive sugar production should expand as a result of this reform. Nevertheless, special attention should be paid to specific sugar products, given their vital role in the economic development of some less favoured areas. This is the case, for example, with the EU’s outermost region and the production of so-called "raw brown sugar intended for direct consumption", and for rum production, taking into account the very high level of subsidies in the US. In addition to that the EU should strive for strict rules of origin, as the US market is to a degree open to NAFTA (Mexico) and in the future TPP (Australia) exports.

Sanitary and Phytosanitary issues (SPS)

It is the inclusion of SPS issues that separates TTIP from other trade negotiations in agriculture. The problem is that the EU and the US maintain fundamentally different approaches to risk management. The EU follows the "precautionary principle" which in its eyes justifies banning growth promoters or GMOs (now in many EU member states). The US asserts that it applies a science-based approach.

It is difficult to conceive that the EU and the US will be able to agree on this entire chapter. But it is equally difficult to conceive that SPS issues will be left aside in TTIP. The reason is quite straightforward: tariff concessions can be voided by SPS barriers. But issues like hormones and GMOs have proven far more resilient to agreement.

What are the potential consequences? The case of hormones in beef is illustrative. The EU lost the WTO case, and is now paying compensation to the US. But the compensation deal is being contested in the US, as the benefits have diminished (due to the increased exports of other countries). Beef is one of the sectors where the EU shows a significant gap of competitiveness vis-a-vis the US. Tariff discussions will already be of great consequence. The hard stance of the EU on banning hormone beef makes it even harder for the EU sector to limit concessions in access to non-hormone treated beef.

Farm Europe expects that with the exclusion of hormones and GMOs, other SPS issues can be addressed and a mutually agreed solution found.