Sweet or Sour?

The U.S. Sugar Program and Threats Posed by DR-CAFTA

The Bush Administration has negotiated the Dominican Republic-Central America Free Trade Agreement (DR-CAFTA) with six other countries: the Dominican Republic, Costa Rica, El Salvador, Guatemala, Honduras and Nicaragua. One sector that will be directly affected by DR-CAFTA is the U.S. sugar program.

The U.S. sugar program is the only major U.S. commodity program that guarantees fair prices to farmers, operates at no cost to taxpayers and prevents export dumping at below the cost of production. The U.S. sugar program balances supply and demand through a three-tiered approach that includes:

1. A non-recourse loan program.
2. Marketing allotments (domestic quotas),
3. Import restrictions through a tariff-rate quota (TRQ) system.

DR-CAFTA threatens to destroy the careful balance of supply and demand achieved through the current U.S. sugar program.

DR-CAFTA proposes a 15-year schedule that gradually increases the amount of sugar from Central America allowed into the U.S.

Disrupting the U.S. sugar program

Congress has set a mandated "trigger level" of 1.39 million metric tons of sugar imported into the U.S. It is essential to the maintenance of the sugar program for imports not to exceed this trigger level. If sugar imports do exceed the trigger level, the three-tiered approach of the program would be knocked out of balance by a congressionally mandated suspension of marketing allotments and the release of excess sugar reserves onto the market. These two events, combined with increasing sugar imports, would dramatically lower prices paid to sugar farmers.

The U.S. Trade Representative (USTR) estimates that during DR-CAFTA's first year, increased sugar market access for Central American countries would amount to about 1.2 percent of U.S. sugar consumption, and grow to about 1.7 percent by year 15. Even this slight increase gives the U.S. sugar program a dangerously small buffer before it reaches the 1.39 million metric ton trigger level (see table 2).

Not included in USTR's estimation are additional expected surges in imported sugar already allowed from Mexico under NAFTA and from other major sugar producing countries that are part of pending trade agreements. Mexico will have the right to import unlimited amounts of sugar into the U.S. under the North American Free Trade Agreement starting in 2008. DR-CAFTA would set the standard on sugar for all future trade agreements. Therefore, pending trade agreements with Thailand, Panama, the Andean countries, South Africa and all of South America (Free Trade Area of the Americas) would likely include sugar. Approval of any of these pending agreements could bring substantial tonnages of additional sugar into the U.S. domestic market, causing the 1.39 million ton trigger level to be exceeded.

Table 1. 15-year phase-in of DR-CAFTA tariff rate quotas in metric tons

CAFTA sugar import access	2003-04 quota	Increase year 1	Increase year 2	Increase year 15[a]	Total, year 15	Annual increase year 16 +
Guatemala	50,546	32,000	32,640	49,820	100,366	+940
El Salvador	27,379	24,000	24,480	36,040	63,419	+680
Nicaragua	22,114	22,000	22,440	28,160	50,274	+440
Honduras	10,530	8,000	8,160	10,240	20,770	+160
Costa Rica	15,796	11,000 2,000[b]	13,220	16,080	31,876	+220
Dominican Republic	185,335	10,000	10,200	12,800	198,135	+200
Total	**311,700**	**109,000**	**111,140**	**153,140**	**464,840**	**+2,640**

a. DR-CAFTA TRQ increases vary from country to country from years 2-15.

b. Additional organic 2000 mt TRQ allocated to Costa Rica.

Table 2. Would DR-CAFTA suspend supply and inventory management?

Trigger level from Farm Bill		1.39
2003-04 total non-NAFTA imports	(1.139)	
CAFTA 15-year TRQ increase	(0.153)	
Less combined CAFTA and non-NAFTA imports		(1.292)
Remaining buffer before marketing allotments suspended		(0.098)

NOTE: All figures above are in millions of metric tons.

DR-CAFTA would likely cause a price drop for sugar farmers in U.S.

By contributing increasing sugar imports that could cause the trigger level to be exceeded, DR-CAFTA would likely result in sharp decreases in U.S. sugar prices. A 2003 North Dakota State University (NDSU) study projected that if sugar imports were to rise over the current TRQ level—either under DR-CAFTA or NAFTA, under other trade agreements or a combination of these—domestic sugar prices would fall significantly. And as prices dropped, U.S. sugar producers and sugar mills would go out of business. The NDSU study projects "that domestic supply would decrease 25% for sugar beets and 15% for sugar cane for every 10% decrease in price." If sugar imports were to exceed 2 million tons, the NDSU study concludes that U.S. sugar beet production would cease all together, and the remaining cane producers would be left with less than 20 percent of the total U.S. domestic market.

DR-CAFTA would negatively impact many poor countries

The U.S. sugar program's TRQ system currently allocates 1.139 million mt, or about 13 percent of U.S. domestic sugar food consumption, to 41 countries. All these countries receive the U.S. supported price of about 20 cents per pound (raw value) for the sugar they export to the U.S., which is more than double the world market price of about 9 cents per pound (raw value). If the U.S. sugar program is broken, prices would drop and imports would increase. But it is likely the spoils would not be divided equitably among the 41 countries exporting sugar to the U.S. Although a few of the world's lowest cost sugar exporters (e.g., Australia, Brazil, South Africa and Thailand), may make up in volume what they lose in price by gaining a greater share of the U.S. domestic market, other countries would lose much of the value of their existing quota as U.S. domestic sugar prices fall to the world dump market price.

For example, Haiti, one of the poorest countries in the world, currently holds a TRQ of 7,258 metric tons. At the current U.S. support price of 20 cents per pound (raw value), the value of Haiti's TRQ is $3,200,230. If the U.S. price were to fall to the current world dump market price of 9 cents per pound (raw value) under the dismantlement of the U.S. sugar program, then the value of Haiti's TRQ would fall to $1,440,104—a net loss of $1,760,126—more than half its current TRQ value.

Finally, if current TRQ allocations were eliminated altogether, there is no guarantee that poorer developing countries would retain any access to the U.S. domestic market, because they would be forced to compete with lower cost exporters.

DR-CAFTA could turn sugar into a dumped commodity on international markets

Unlike other major U.S. commodity programs, the sugar program actually prevents dumping on the world market at below the cost of production. But DR-CAFTA contains a provision that may change that. The sugar compensation mechanism in the DR-CAFTA would allow the U.S. government to buy out Central American importers rather than allow them to use their increased quotas under the agreement. Estimates for the cost of this program run as high as $28 million in the first year of the agreement alone.

The sugar compensation mechanism also allows the U.S. government to use surplus sugar or surplus sugar-containing products as compensation instead of money. This could turn the U.S. sugar program from a non-dumping program into a dumping program. It could result in the U.S. passing its surplus sugar or even other commodities through Central American countries and onto the world market. If cash were to be used, it would change the program from a no-cost program into a taxpayer-subsidized program requiring budget outlays.

For decades, the U.S. sugar program has offered a sound policy model that has successfully created market stability at little public expense, while avoiding the structural over-production that leads to dumping onto international markets. We should look to the U.S. sugar program, and other supply management programs around the world, for lessons on how to solve the current global farm commodity crisis.

The full report, *Sweet or Sour?: The U.S. Sugar Program and the Threats Posed by the Dominican Republic-Central America Free Trade Agreement,* is available at tradeobservatory.org.

 Copyright Institute for Agriculture and Trade Policy