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## ISSUES AFFECTING LATIN AMERICAN AGRICULTURE AND FUTURE TRADE NEGOTIATIONS<sup>3</sup>

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### BACKGROUND

Agriculture and agro-industry are central components for the economies of Latin America and the Caribbean (LAC). Currently they account for approximately 25 percent of the regional GDP, and for the primary agricultural sector alone, about 10 percent. For several countries such as Guatemala, Guyana, Haiti, Honduras, Nicaragua and Paraguay, just the primary agricultural sector represents more than 20 percent of the GDP; in others such as Brazil, Colombia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Panama and Suriname, that participation is between 10 percent and 20 percent. In terms of employment, the primary agricultural sector represents more than 25 percent of total employment, with several countries showing greater participation: Belize (33 percent), Bolivia (47 percent), Ecuador (33 percent), El Salvador (36 percent), Guatemala (52 percent), Haiti (67 percent), Honduras (about 40 percent), Paraguay (39 percent), and Peru (36 percent).

Agriculture also has a large multiplier effect (i.e., how many dollars of activity in the rest of the economy are created by an additional dollar in agricultural activity), which has been calculated as about 4. Also, poverty issues and agriculture are related in Latin America. About 35 percent of rural population is poor while only 15 percent of urban population falls under that category (but the total number of poor in urban areas is larger than in rural areas because a large percentage of the population lives in cities in LAC). Rural poverty is related to the existence of very small farms and lack of investment in human capital and infrastructure. There are a large number of small producers, many of whom are under the level of what could be called a family farm: out of 17 million producers in LAC, about 15.7 million have less than 3 hectares.

At the same time, LAC is a large reservoir of natural resources. LAC has only 8 percent of world population but it has 23 percent of potential arable land, 46 percent of tropical forests, and 31 percent of fresh water. However, about 210 million hectares (14 percent of the productive area) show moderate to severe erosion. This problem is in part linked to poverty and lack of productive opportunities.

Obviously the performance of the agricultural sector is crucial to sustainable development in Latin America and it is linked to poverty and environmental issues. It is important to remember these facts in trade negotiations.

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<sup>3</sup> These remarks are based mainly on Diaz-Bonilla, 1999 and Diaz-Bonilla and Reca, 1999.

## **PRODUCTION**

The pattern of agricultural production growth has not been uniform during the last 25 years. During the 1970s there was a distinct acceleration in agricultural production in LAC as high world prices fueled the expansion of exportable and import-substitution agricultural products and strong domestic demand sustained those products that were non-traded goods. Although the agricultural sector and rural areas were affected by a policy strategy biased toward the industrial sector and urban areas, supportive world markets and domestic income growth appear to have been enough to generate comparatively higher growth rates in the agricultural sector of LAC.

During the 1980s world and domestic conditions for the agricultural sector of LAC changed substantially. Devaluation of exchange rates and progressive advance of trade liberalization removed at least part of the policy bias indicated. Real exchange rates (defined as the price of tradable over non tradeable) increased in many countries in the region, favoring export and import substitution agricultural productions. However, reductions in government expenditures in infrastructure and technology, as well as the elimination of marketing and price support programs that were benefitting some specific crops and livestock products in certain countries, tended to affect supply negatively. Also the higher cost of imported inputs (as a result of devaluation), and the reduction of credit to agriculture by the public and private banking sectors (partially linked to macroeconomic stabilization programs), had a negative impact on agricultural production. Slow down in domestic demand affected livestock and dairy production because they are dependent on domestic consumption. The crisis of the industrial sector carried over to some agricultural raw materials, and the weakness in world markets hit exportable agricultural goods hard and made it difficult for LAC governments to continue the support of some import-substitution products, such as wheat in Brazil and Chile.

As a result of this combination of positive and negative conditions, agriculture fared better than the rest of the economy during the harsh decade of the 1980s and continued to grow albeit at lower rates than before. In the 1990s, after a slow start due to the continuation of low growth at the world level and in the region, LAC's agricultural production picked up again, at least until 1998. The full impact of the financial crises that began in 1997 in Asia is still to be seen.

## **TRADE**

Agricultural trade is very important in Latin America. There are many countries where agricultural trade still makes up more than 50 percent of exports. In the 1960s, Latin America exported 7 dollars for every dollar of imports. Now, Latin America exports somewhat less than 2 dollars for every dollar of imports, which makes the region still a large net exporter of agricultural products.

The structure of agricultural exports in Latin American has changed over time. In the 1960s, Latin America was a cocoa, coffee and sugar exporter (these products represented more than 60 percent of all agricultural exports). In the last two decades,

however, there have been important changes in the structure of exports with the increase in oilseeds, and fruits and vegetables. Oilseeds and their products went from 3-4 percent in the 1970s, to about 20 percent of all agricultural exports in the late 1990s. Fruits and vegetables jumped from about 7 percent in the 1970s, to close to 30 percent of all agricultural exports today. In terms of trade negotiations these products pose different questions compared to the traditional tropical products, but they also differ somewhat from those raised by cereals. For instance, expansion of trade in fruits and vegetables may be more linked to Sanitary and Phytosanitary issues, rather than export subsidies.

An important characteristic of agricultural trade (and, in fact, of all international trade) in the region, is the steady increase in the share of intra-regional commerce, which, for the Americas (including the United States and Canada), moved from a quarter of total agricultural exports in 1981-83, to more than a third by mid-1990s. Among LAC countries Brazil is the less dependent on the region for its agricultural exports and imports, while Mexico appears on the other extreme of the spectrum. Other countries with greater diversification in the destination of exports and the source of imports of agricultural products and food are Argentina, Chile, Peru and, to a lesser extent Uruguay and Colombia.

Regional pacts have had an impact on the trade flows of their respective members. Clear cases are Mexico with regard to NAFTA and Uruguay, Paraguay and (to a lesser extent) Argentina with respect to MERCOSUR. But, for obvious reasons, NAFTA also has a strong presence in the trade flows of non member countries in the region, including Brazil.

All in all, the process of trade liberalization that has taken place in the region and the implementation of trade agreements have fostered agricultural trade. This has led to larger coefficients of internationalization, measured as exports over production and imports over consumption, for a variety of agricultural products, indicating a larger exposure of LAC's agricultural sector to world markets.

Within the region, different markets have been developing, each one with its own characteristics. For instance, LAC as a whole is a net importer of grains, creating a market where, within the region, Canada, the United States and Argentina compete, and the functioning of those markets are determined by the rules of NAFTA, MERCOSUR or other sub-regional trade pacts. There is also a market for oilseeds and vegetable oil where the United States, Argentina, Brazil and sometimes Canada, may be competing for market share in countries like Venezuela or Mexico. This competition is also influenced by regional trade pacts. Similarly, there is a very complex pattern of trade flows in fruits and vegetables, meat, dairy and other products, depending on different factors such as the time of the year (in fruits and vegetables), the regional trade pacts and agricultural policies in different countries.

In general, the evolution of trade flows will depend on trade and agricultural policies in the Americas and elsewhere, which, in turn will be influenced by different multilateral, regional and bilateral agreements that will result from the complex

negotiations ahead. These negotiations include the continuation of the process initiated during the Uruguay Round, and, for the countries of the region, the possibility of creating a Free Trade Area of the Americas, as well as extraregional negotiations such as the participation of NAFTA countries and Chile within APEC, and the discussions between MERCOSUR and the European Union.

## **THE MACROECONOMIC SITUATION**

Though agricultural and trade policies are very important to define trade patterns, it is obvious that the latter are increasingly being influenced by macroeconomic developments and by the flows of capital that change with macroeconomic policies and conditions. Treating the balance of payments as an accounting identity, the current account (mainly the trade account including non-factor services plus payments for factor services) has to be equal to the capital account and the change in foreign reserves. Trade negotiations are concerned with the trade component (including non factor services) of the balance of payments. Currently, however, what is driving much of the dynamics of the trade balance is the capital account. When capital is flowing in, there is an acceleration of growth with multiplier effects in the economy, and usually a trade deficit emerges due to price and income effects. When capital leaves a country the process works in reverse and the trade deficit disappears (or it changes into a trade surplus). Whatever has been negotiated on the trade side may be overwhelmed by developments taking place at the level of macroeconomic variables and capital flows. Consequently, macroeconomic policies, including the issue of macroeconomic coordination, may become more important in trade negotiations over time.

## **POLITICAL ECONOMY OF NEGOTIATIONS**

The political environment of future WTO negotiations, or for the creation of a Free Trade Area of the Americas, is going to be different from the one that prevailed in the Uruguay Round. From the point of view of the United States, while the focus in the previous round was on grain and oilseeds, future negotiations may center increasingly on more difficult products such as sugar, peanuts, citrus, beef and others. While much remains to be done at the level of grains and other products (especially vis-a-vis the European Union) the United States may or may not be in the position of offering leadership in the negotiations depending on the balance of interests within the agricultural sector of those groups that may benefit and those that may not.

In Latin America, the dynamics for trade negotiations may depend on the efforts of Brazil to put together a South American bloc to enable it to negotiate with the United States one-on-one. The negotiations between MERCOSUR and the Andean Pact to create a South American free trade region are well advanced. On the other hand, the convergence of economic recessions in Brazil and Argentina are creating tensions within MERCOSUR, which although not threatening to break the trade pact, complicate the possibility of developing common negotiating positions in

the region. At the same time, there are attempts to create a free trade area between MERCOSUR and the European Union, which will most certainly be postponed until the WTO negotiations are finished.

The evolution of those national and international coalitions of interests will define the shape of the future trade negotiations in agriculture within the Continent and at the world level.

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## ECONOMIC ADJUSTMENT IN CHILE

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In discussing economic adjustment in Chile, it is important to know a little about Chile's recent history and performance. Chile is a small country with a small economy, endowed with very limited resources. It is far from markets and isolated. It has a very heterogeneous topography, climate and ecological area. It is also a solitary island surrounded by natural frontiers--the Andes on the east, a huge desert on the north, the Pacific Ocean on the west and islands on the south. Chile had a president at the end of the last century who said, "Chile is such a small country with so many problems, why don't we sell it and buy something closer to Paris."

The farm structure in Chile is very diverse. There are about 150,000 small farmers. Of those, about 20,000 are integrated and comprise what is really Chilean agriculture. Chile is trying to convert all of its disadvantages into comparative advantages. Sometimes it is said that Chile has undergone a miracle. I believe that there have been no miracles in Chile. Chile has been a guinea pig of every type of economic theory and strategy and we have learned our lesson.