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DELEGATION OF THE COMMISSION OF THE EUROPEAN COMMUNITIES

January 20, 1987

To: Sir Roy

From: Giancarlo Chevallard

You will find attached the "argumentaire" USTR has prepared and is actually circulating in town to relevant media people.

cc:

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"A European View of U.S. Trade Feud:"

U.S. Counterarguments

The following points respond to arguments raised by EC Commissioner Peter Sutherland in his Wall Street Journal article entitled, "A European View of U.S. Trade Feud." Sutherland's piece was prompted by the enlargement dispute between the United States and the European Community. He embellishes his arguments with examples intended to illustrate the EC's general free trade stance and specific liberalizing measures taken in the agriculture and steel sectors.

U.S.-EC Enlargement Dispute

EC Argument:

> We are "witnessing the collapse of rational debate." The U.S. is attempting to "appease protectionists in its own camp" or "looking for dramatic test cases in the hope of scoring political points." It is counterproductive to "blame someone else for one's own failings."

U.S. Response:

-- The U.S. is not responsible for initiating this dispute. The recently announced U.S. actions are intended only to protect our trade rights in the face of new EC restrictions on almost one billion dollars in U.S. exports.

-- The U.S. has tried to resolve the issues raised by EC enlargement through "rational debate." During the years preceding accession, Secretary of State Shultz, Secretary of Agriculture Block, USTR Brock and Secretary of Commerce Baldrige repeatedly asked EC Commissioners to discuss the provisions of the accession treaty, and the problems these provisions might raise, prior to its implementation.

-- In Ambassador Yeutter's first meeting with EC Commissioners De Clercq and Andriessen in December, he raised our concerns regarding certain provisions of the accession treaty, and asked that the EC sit down and discuss its plans with us. Ambassador Yeutter raised this issue on two more occasions with Commissioner De Clercq in January and February of this year.

-- Under GATT rules, the EC had an obligation to consult with us before implementing these measures. Nevertheless, the EC notified the GATT of its intended actions only 17 days before the new restrictions took effect.

-- U.S. officials have travelled to Brussels several times this spring in order to obtain more detailed information on the

EC's new restrictions. Prior to taking any action ourselves, we held high-level meetings with EC officials, and asked that the EC (1) suspend its quotas in order to allow the GATT time to decide whether they were legal, and (2) hold negotiations with us immediately to agree on appropriate compensation for increased tariffs on over $600 million in U.S. corn and sorghum exports. The EC has thus far refused these requests.

-- In light of the tremendous amount of U.S. exports at stake, and the EC's apparent unwillingness to resolve these issues in a timely fashion, we chose a measured response, designed to ensure that both sides have an equivalent incentive to resolve this dispute quickly.

EC Argument:

The "narrow" U.S. focus on losses in agricultural exports resulting from the entry of Spain and Portugal into the EC fails to take account of "overall gains" which U.S. exports will experience as a result of EC enlargement.

U.S. Response:

-- The EC's contention that U.S. exports of industrial products to Spain and Portugal will increase as a result of accession is largely a hypothetical one.

-- First, reductions in industrial tariffs are scheduled to be phased in over seven years, while tariff increases on agricultural imports were fully implemented on March 1.

-- Second, U.S. industrial exporters will face increased competition from EC suppliers in Spain and Portugal, since all tariffs between the EC and Spain and Portugal will be eliminated.

-- Finally, previous experience does not support the EC's contention. Following Greece's entry into the EC in 1981, the U.S. share of total Greek imports fell, while the EC's share of total imports rose.

U.S.-EC Trade Relations

EC Argument:

The EC is the world's largest free trader. The EC has reduced protectionism in Europe by dismantling such barriers to trade as tariffs, quotas, and state subsidies.

U.S. Response:

-- The EC is indeed a large trader, though the EC accounts for 30 percent of world trade only if trade among its members is included. If external trade comparisons are made, the EC's numbers are about the same as those of the U.S.

-- For the EC to consider itself the world's largest <u>free</u> trader is a most dubious proposition. The Community is highly protectionist in a myriad of ways, and probably has more techniques and mechanisms to constrain imports than any political entity in the world. Many people believe that the EC has become increasingly protectionist in recent years as its economies have stagnated and as it has lost its international competitiveness in many products, especially in newer areas such as high technology.

-- U.S. imports accounted for 62% of LDC exports of manufactured products to the industrial world in 1984, while the comparable share for the EC was just 23%.

-- While EC tariff levels are about the same as those in the U.S., the EC often uses "grey area" and other non-tariff measures which are not reported to the GATT. EC voluntary restraint agreements on consumer electronics, textiles and steel coming from Far Eastern countries significantly distort trade patterns, shifting these exports to U.S. markets. Other EC practices which distort world trade include restructuring subsidies, government procurement practices, and the Common Agricultural Policy (CAP).

Industry

A. Aircraft

EC Argument:

U.S. complaints about excessive state supports for aircraft are founded less on facts than on U.S. reluctance to accept international competition in a sector dominated by the U.S.

U.S. Response:

-- U.S. complaints are based solely on our rights under the GATT Agreement on International Trade in Civil Aircraft and the GATT Agreement on Subsidies and Countervailing Duties. They have nothing to do with U.S. reluctance to accept international competition in trade in civil aircraft.

-- As a matter of policy, we welcome such competition provided it is conducted on a fair basis in accordance with international agreements. We seriously question whether continued government support of Airbus Industrie is consistent with the provisions of these international agreements. Such state supports do not lead to fair competition; rather, they preempt the private marketplace.

-- One of our major difficulties is that the European governments have so far been unwilling to disclose the amount of their aircraft subsidies. For that reason, we have initiated a series of consultations with the European governments in order to come to a joint understanding of what is proper governmental behavior in light of the provisions of the international agreements.

B. Steel

EC Argument:

The EC maintains that its steel industry has restructured while the U.S. industry has not. It claims to have eliminated more than 18 percent of its hot-rolling production capacity since 1980, and 19 percent of its crude steel capacity. EC reduction in employment has been as high as 42 percent, representing 280,000 job losses.

U.S. Response:

-- While the Europeans have reduced capacity significantly, much excess capacity still remains. On the U.S. side, raw steel capacity now stands at 127 million net tons, down from 153.7 million net tons in 1980, representing a reduction of 17 percent.

-- Operating costs in the U.S. steel industry have dropped 17 percent since 1982. Employment costs have been reduced by 35 percent.

-- Employment in the U.S. steel industry fell from 325,100 workers in 1982 to 237,000 workers in 1985. At the same time, the productivity of the U.S. steel worker increased by over fifty percent between 1982 and 1985.

EC Argument:

The EC claims that state subsidies linked to a restructuring plan have been virtually eliminated and they consider that the European industry can stand on its on two feet.

U.S. Response:

-- While EC state subsidies have been virtually eliminated in a few countries (West Germany and the Netherlands), the impact of these subsidies will continue to benefit the industry over the next decade.

-- Subsidy levels remain significant in other EC countries (France, the UK, and Italy). Moreover, as many European steel companies are operating in the red, it is likely that they will continue to demand government support.

EC Argument:

The EC claims that U.S. competitiveness has declined because of protection given to the steel industry. Cries of unfair competition are unfounded.

U.S. Response:

-- Cries of unfair competition by the U.S. steel industry are not at all unfounded. Our current steel program is predicated on numerous findings of unfair trade practices (such as dumping and injurious subsidies) in the EC and elsewhere.

-- In 1981, the EC asked <u>us</u> to negotiate a bilateral voluntary restraint agreement on steel in order to avoid the imposition of heavy antidumping and countervailing duties in response to the filing of several hundred petitions by the U.S. steel industry. This agreement was recently renewed.

Agriculture

EC Argument:

The European Community contends that is is portrayed as unfairly protectionist and that this simply is not true, particularly in the area of agriculture.

U.S. Response:

-- The European Community's Common Agricultural Policy (CAP) is highly protectionist. Prices for most agricultural crops are prescribed by the Commission of the European Community, and are supported at levels far above world market prices. Isolated from normal supply and demand forces, prices within the EC have continued to rise despite a downturn in world markets.

-- To protect domestic prices from foreign influence, the EC has established a system of variable levies, quotas, minimum import prices and other protective mechanisms. Using these devices, the EC has virtually isolated many of its agricultural commodity sectors from the effects of world market forces.

-- The EC is still a major food importer, bringing in $82 billion worth of agricultural imports during 1983. However, the EC's policy of high farm price supports in conjunction with widespread import protection and a massive system of agricultural export subsidies under the CAP has caused a dramatic shift in the Community's net trading position for a number of key commodities. Putting it another way, the EC has been stimulating excess production through skyhigh price supports, and then shoving the excess on the world market through export subsidies.

- At the start of the 1970's, the EC was a net importer of over 20 million Metric Tons (MT) of grains annually. Since then, Community exports have increased to such an extent that in 1982/83, EC net exports of grains reached 11 million MT.

- The EC has gone from being a net importer of white sugar to being the world's largest exporter. Exports totaled 5.6 million MT, on a raw basis, in 1982/83. EC sugar exports have demolished the world market for that product with prices falling to as low as .03/lb. in 1985. This has had a devastating effect on other sugar exporters, most of whom are LDCs.

- Prior to 1973/74, the EC was a net importer of beef and veal. In recent years, the EC has been the world's largest exporter of these products, thanks to export subsidies that have been nearly as great as the value of the underlying products themselves.

o In poultry, the EC has moved from being the world's largest importer in the mid-1960's to currently being the world's largest exporter.

-- These shifts, due almost entirely to EC intervention in its agricultural sector, have had a major impact on the volume and pattern of world agricultural trade and have significantly reduced marketing opportunities within the EC and in third country markets for efficient agricultural producing countries like the U.S.

-- The primary remaining markets for U.S. agricultural products within the EC are for soybeans and certain other livestock feed ingredients. The only reason we have been able to maintain these markets is that the U.S. has a zero duty GATT binding obtained in a previous round of trade negotiations. On several occasions, the EC has threatened to introduce measures which would impair that concession. After threat of U.S. retaliation, the EC has thus far withdrawn its proposals.

EC Argument:

"It is estimated that the EC price support level this year will be approximately $19 billion, compared with a U.S. figure of $21 billion."

U.S. Response:

-- EC statements that the U.S. spends as much or more than the EC on agriculture are false. With the exception of 1983 (when the U.S. took 83 million acres of land out of production in an effort to shore us global market prices) U.S. budget expenditures for farm supports have been lower than those of the EC for every year from 1978 to 1984. Estimates for 1985 also put U.S. expenditures lower than those of the EC. Furthermore, the EC numbers include only expenditures by the Commission; they exclude farm supports provided by individual countries, which typically total to about the same amount those provided by the Commission.

-- Another important difference lies in how those sums are spent. We have been using nearly all our support money in a non-confrontational way - through income payments to farmers, storage payments on excess production, and diversion payments to idle land. The EC, on the other hand, has made almost no effort until recently to reduce production, and has moved its surpluses onto the world market in a highly confrontational way, undercutting the prices of our producers and those of other exporting nations.

EC Argument:

"The EC does subsidize exports but....it has always done so in full conformity with GATT".

U.S. Response:

-- GATT rules on agricultural export subsidies are unclear. A GATT panel established to consider a U.S. complaint against the Community's export subsidies for wheat flour could not make a definitive finding because of difficulty in interpreting the rules.

-- In the case of pasta, a GATT panel agreed with the U.S. view that EC subsidies on pasta violate the Community's obligations under the GATT Subsidies Code, but the EC has blocked adoption of the panel report.

-- The EC's export subsidy system on sugar was found in 1979 to threaten serious prejudice to the interests of Australia and Brazil. The EC blocked GATT recommendations for change, and EC export subsidies have continued to cause great damage to other, mostly developing countries.

June 1986

Subm'd to XXIV:5 WP

Note From the United States
4 December 1986

An Overview of the Tariff Impact on Contracting Parties Trade of Spanish and Portuguese Accession to the European Community

The attached tables present a summary of the impact of the introduction of the European Community tariff schedule will have on Spain's and Portugal's trade with GATT contracting parties other than the members of the EC10. In the first table, the impact is measured in terms of the amount of trade covered by changes in tariffs and variable levies. In the second table, actual duties foregone or collected for these changes in tariffs or variable levies.

The analysis was carried out using the tariff files supplied by the European Community for XXIV:6 negotiations with the United States. We used as a basis for analysis the tariffs of the EC10 rather than the trade weighted average for the EC12. In addition, we estimated the *ad valorem* equivalent of EC10 variable levies effective in the early Spring 1986. Values in these tables are in millions of ECUs and reflect average 1983/84 trade volumes.

The results of table 1 show that about 6.4 billion ECUs of third country trade with Spain and Portugal would experience tariff decreases as a result of the extension of the EC10 tariffs to trade with Spain and Portugal. Tariffs and variable levies would be increased on 3.2 billion ECUs. In addition, the European Community has not indicated how it intends to handle the 96 tariff items that are currently blank in the tariff so we treated those as adverse to third country interests. These blanks cover about 1.9 billion ECUs of third country trade with Spain and Portugal. There are no changes in tariffs on 4.2 billion ECUs. The overall impact shows that tariffs decrease on about 6.4 billion ECUs while they increase or are of otherwise adversely impacted on 5.1 billion ECUs.

Table 2 shows the impact on a duties collected basis. In this case the results are remarkably different from the prèvious table. Duties foregone are about 675 million ECUs. Increased duties collected however are almost double that amount, 1,328 million ECUs. This marked adverse impact on third country trade is further amplified when the impact of the 96 blanks, 1,859 million ECUs, are added into this. In this case, the disadvantages to third countries on a duties collected basis is nearly 5 times as great as the advantages for third countries trading with Spain and Portugal.

Tables 3 and 4 provide the same information as tables 1 and 2, but from the point of view of U.S. trade with Spain and Portugal.

TABLE 1
An Overview of the Effect of Extending the Tariff System of the EC-10 to GATT Contracting Parties Trade with Spain and Portugal: (1983/84 Trade)

	Total Imports of Spain and Portugal (millions of ECUs)
1) Global trade with Spain and Portugal where tariffs are decreasing	
a. Bound	3439.2
b. New Bindings	2963.1
c. Unbindings	85.1
d. Remaining unbound	3.9
	6491.3
2) Global trade with Spain and Portugal where tariffs are increasing	
a. Bound	132.2
b. New Bindings	1730.2
c. Unbindings	723.8
d. Remaining unbound	595.7
	3181.9
3) Global trade with Spain and Portugal where tariffs remain the same	
a. Bound	396.5
b. New Bindings	3792.0
c. Unbindings	0.6
d. Remaining unbound	1.2
	4190.3
4) 96 Blanks	1858.7

TABLE 2
An Overview of the Effect of Extending the Tariff System of the EC-10 to GATT Contracting Parties Trade with Spain and Portugal: (1983/84 Trade)

		Duties Collected or Foregone (millions of ECUs)
1)	Global trade with Spain and Portugal where tariffs are decreasing	
	a. Bound	-415.6
	b. New Bindings	-258.6
	c. Unbindings	-0.7
	d. Remaining unbound	0.0
		-674.9
2)	Global trade with Spain and Portugal where tariffs are increasing	
	a. Bound	7.4
	b. New Bindings	111.3
	c. Unbindings	623.2
	d. Remaining unbound	586.4
		1328.3
3)	Global trade with Spain and Portugal where tariffs remain the same	
	a. Bound	0.0
	b. New Bindings	0.0
	c. Unbindings	0.0
	d. Remaining unbound	0.0
		0.0
4)	96 Blanks (Trade Coverage)	1858.7

TABLE 3
An Overview of the Effect of
Extending the Tariff System of the
EC-10 to the United States
Trade with Spain and Portugal:
(1983/84 Trade)

	TRADE COVERAGE ~~Duties Collected or Foregone~~ (millions of ECUs)
1) U.S. trade with Spain and Portugal where tariffs are decreasing	
a. Bound	1138.6
b. New Bindings	595.1
c. Unbindings	.2
d. Remaining unbound	.6
	1734.5
2) U.S. trade with Spain and Portugal where tariffs are increasing	
a. Bound	47.0
b. New Bindings	497.6
c. Unbindings	450.8
d. Remaining unbound	547.6
	1543.0
3) U.S. trade with Spain and Portugal where tariffs remain the same	
a. Bound	215.3
b. New Bindings	273.8
c. Unbindings	0.0
d. Remaining unbound	0.1
	489.2
4) 96 Blanks	1113.7

TABLE 4
An Overview of the Effect of
Extending the Tariff System of the
EC-10 to the United States
Trade with Spain and Portugal:
(1983/84 Trade)

	Duties Collected or Foregone (millions of ECUs)
1) U.S. trade with Spain and Portugal where tariffs are decreasing	
a. Bound	-147.5
b. New Bindings	-68.3
c. Unbindings	-0.0
d. Remaining unbound	0.0
	-215.8
2) U.S. trade with Spain and Portugal where tariffs are increasing	
a. Bound	2.1
b. New Bindings	0.0
c. Unbindings	455.5
d. Remaining unbound	537.9
	995.5
3) U.S. trade with Spain and Portugal where tariffs remain the same	
a. Bound	0.0
b. New Bindings	0.0
c. Unbindings	0.0
d. Remaining unbound	0.0
	0.0
4) 96 Blanks (Trade Coverage)	1113.7