

441.2(103)

No. 1/89
February 3, 1989

Contact: Ella Krucoff
(202) 862-9540

E.C.-U.S. ECONOMIC AND TRADE RELATIONS

1988 REVIEW AND CURRENT ISSUES

The European Community and the United States are closely linked politically and economically. They are both partners and competitors in the trade sphere, and are active participants in the Uruguay Round of multilateral trade negotiations taking place in Geneva.

ECONOMIC AND TRADE LINKS

The Community and the United States are both leaders in the world economic and trading system. Together, they account for over 30 percent of world trade, and thus have a major responsibility for the management of the system.

They also represent more than 70 percent of the industrialized world's (OECD members) Gross Domestic Product. In 1987, E.C. investment in the United States amounted to \$158 billion, while U.S. investment in the Community accounted for \$127 billion (of a total U.S. overseas investment of \$309 billion). They are also linked by the size of their combined industrial output: some 35 percent of world steel production, 55 percent of world car production and 70 percent of world aircraft production.

The Community and the United States are major markets for each other, with trade between them totaling 128 billion European Currency Units* (ECUs, more than \$147 billion) in 1987.

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EC OFFICE OF PRESS AND PUBLIC AFFAIRS

Washington: 2100 M Street NW Seventh Floor Washington DC 20037 / telephone (202) 862-9500 / telex 64215 EURCOM-UW

New York: 3 Dag Hammarskjöld Plaza 305 E 47th Street New York NY 10017 / telephone (212) 371-3804 / telex 661100 EURCOM-NYK

The Community of Twelve was by far the U.S.'s leading export market that year, taking \$60.6 billion--about 24 percent--of U.S. exports. By comparison, Canada took \$59.8 billion, also near 24 percent, and Japan took \$28.2 billion, or about 11 percent. 1988 projections in combined E.C./U.S. trade are about \$166 billion.

There has been a remarkable increase in bilateral trade between the Community and the United States over the past decade, although the figure fell slightly in 1986 and 1987. (See chart on page 13.)

Until recent years, the Community regularly ran up a trade deficit with the United States. At times, this deficit was high, as in 1980, when it was almost 20 billion ECU. However, because of the strength of the U.S. dollar, the trend has been reversed. In 1987 the Community had a surplus of 15.7 billion ECU, although it still recorded a deficit on agricultural products. Over the last thirty years, U.S./E.C. trade has been remarkably balanced.

U.S. January to November data shows a considerable improvement in the U.S./E.C. trade balance. The U.S. trade deficit with the E.C. has decreased from \$18.6 in 1987 to \$8.1 billion in 1988.

There is no overall agreement between the Community and the United States covering their trade and economic relations in a general manner. They are linked, however, by a broad range of multilateral agreements to which they are both parties. In addition, a number of accords have been concluded to cover specific sectors.

Euratom-U.S.

This was the first agreement signed on behalf of the European Atomic Energy Community (Euratom), less than five months after the entry into force of the Euratom Treaty in 1958. This agreement, supplemented by another accord later that year, establishes a framework for cooperation on peaceful uses of nuclear energy, including the supply of nuclear fuel to the Community by the United States.

At the end of the 1970s, the United States Government proposed updating parts of the agreements relating to safeguards throughout the nuclear cycle, and talks have been taking place.

In July 1986, the Community and the United States signed a joint declaration of intent on research into radiation protection. In December 1986, they signed a scientific and technical cooperation agreement on thermonuclear fusion.

Environment

Since 1974, E.C. Commission and U.S. Administration officials have held regular meetings to exchange information on environmental issues. They also meet in international fora such as the Organization for Economic Cooperation and Development (OECD) and United Nations Environment Program (UNEP) to tackle such problems as ozone depletion, waste and global climate warming.

High technology

The E.C. Commission and the U.S. Administration in 1983 set up a working party to exchange information related to advanced technology and to pinpoint sectors for cooperation. Discussions take place each year on such issues as biotechnology, semiconductor technology, superconductivity, and high definition television.

The two parties agreed in 1987 to exchange information regularly on technical and political developments in the telecommunications sector. Working parties have been established on technical standards, public procurement, competition and statistics.

SPECIFIC RECENT PROBLEMS

Hormones

In response to deep European consumer concerns and considerable pressure from the European Parliament, the E.C. Council of Ministers decided in December 1985 to ban the use of hormones in meat as from January 1, 1988. Transitional measures were applied to avoid any disruption of the internal market and to give external suppliers an opportunity to conform to

the new health standard. On January 1, 1989 the ban went into force for meat traded between member states and for any meat imported. On that same date, in disagreement with the ban, the United States retaliated and unilaterally raised tariffs to 100 percent on seven Community products. They are boned beef, pork hams and shoulders, processed tomatoes, coffee extracts, lightly fermented alcoholic beverages, fruit juices, and packaged pet food.

The Community's directive is non-discriminatory since it applies equally to all meat regardless of origin--domestic or imported. All other major suppliers such as Australia, New Zealand, Brazil and Argentina are maintaining their trade by sending hormone-free meat to the E.C.

The E.C. Council of Ministers has invited the United States to suspend its illegal and unilateral sanctions which are to be challenged in the GATT. They have also approved E.C. counter-measures which would raise E.C. tariffs to 100 percent on walnuts and dried fruit from the United States. The volume of trade affected would be about \$100 million, approximately the same amount affected by the U.S. retaliation.

On February 20, the Council will take stock of the situation and consider when to put their counter-measures into force.

The Uruguay Round - General Agreement on Tariffs and Trade (GATT)

The Community and the United States cooperated to launch the Uruguay Round of trade negotiations in September 1986. The talks are covering agriculture, services, intellectual property rights, textiles, safeguards, dispute settlement and other subjects.

Last December in Montreal trade ministers undertook a midterm review of the multilateral negotiations. Although framework agreements were reached in eleven out of fifteen sectors, no text was concluded in four areas: agriculture, textiles, intellectual property rights, and safeguards. This placed the entire Round on hold until April 1989. The main standoff was between the United States and the European Community over agriculture. Although both parties agree that excessive subsidies distort agricultural markets, the U.S. insists on total abolition of trade distorting subsidies. The E.C. considers this an extreme and unrealistic

position and prefers to settle for substantial and beneficial results which are realistically possible.

The Community wants to strengthen GATT and to complete the Round on time. Solutions must be found to end the stalemate. The E.C. and the U.S. are under considerable world pressure to resolve their differences.

U.S. trade legislation

The Community's major concern about its relations with the United States centered on the Omnibus Trade and Competitiveness Act passed in 1988. This Act contains many protectionist provisions which could seriously affect the Community, and the E.C. Commission and Council of Ministers had called on the United States not to adopt them. While acknowledging that the final text is less protectionist than the previous ones, the Community nevertheless considers that the provisions:

- confirm that the United States is tending to interpret international trade rules unilaterally;
- still enable the United States administration to take measures against its trading partners, even if the GATT rules have not been violated;
- increase the danger of protectionist measures being taken under pressure from lobbying;
- run counter at least to the spirit, if not the letter of the standstill commitments made at Punta del Este.

The Council of Ministers meeting of September 29 adopted a statement in which it expressed "serious concern at the protectionist potential of the Omnibus Trade and Competitiveness Act of 1988". The Community will monitor the situation closely and will insist on its rights within GATT if its interests are affected by implementation of this law.

Airbus

The United States challenges the subsidies received by Airbus Industrie, a four-nation European consortium. In March 1987, it requested discussions with the Community in the framework of the GATT Committee on Trade in Civil Aircraft, and those have been taking place. The two parties are attempting to reach a common interpretation of Articles 4 (government-directed procurement) and 6 (government support) of the GATT Agreement on

Trade in Civil Aircraft. They have made progress on the interpretation of Article 4, but are still divided on the interpretation of Article 6.

At a ministerial-level meeting in London on October 27, 1987 the parties agreed they wanted to resolve the problem by negotiation, and developed guidelines for future discussion. In March 1988 a second ministerial meeting was held at Constance, Germany. The negotiators were instructed to look into the exact terms of government support, procedures for transparency and the definition of "commercial business practices."

The Community denies that Airbus subsidies violate international trading rules. The Civil Aircraft agreement does not prohibit government subsidies; it only obligates countries to try to avoid adverse effects on trade. The U.S. industry would have difficulty proving adverse effects because its sales rose substantially last year.

The U.S. exports annually nearly \$5 billion worth of aircraft and parts to the Community, while the E.C. exports \$3 billion worth to the U.S.

The Community argues that the United States government also supports its aircraft industry-- through massive defense contracts and government-funded research and development. The U.S. has spent more than \$75 billion in aeronautical research and development since Airbus was formed in 1970.

Airbus is responsible for major advances in aircraft design, technology and innovation, stimulating technological progress by its major competitors.

Soybeans

The U.S. Administration in January 1988 made a formal request to the GATT for a dispute panel following a complaint filed by the American Soybean Association against the E.C.'s oilseed and protein crop subsidies. The soybean group charged that E.C. subsidies discriminate against imports of U.S. soybeans and soybean meal, saying those imports had fallen by 40 percent since 1982.

The Community regretted the Administration decision, noting that it is the U.S. soybean farmer's best customer. The E.C. regularly takes between 45 percent and 50 percent of all U.S. soybeans and approximately the same percentage of soymeal. In fact, it imported 14 percent more beans and 21 percent more meal from the U.S. in fiscal 1987 than in the previous year. The E.C. insists that if a GATT panel found injury, it must be quantified. The GATT panel has been established, but has not yet completed its report.

While E.C. soybean imports from the U.S. have fallen since 1982, over the longer term total imports from all sources have increased substantially. Brazil's exports of these products to the Community since 1982 have almost doubled, and Argentina's have tripled.

The American decision comes more than 20 years after the Community implemented a support system for oilseeds and protein crops, when the general question of farm support is under negotiation in the Uruguay Round and after the Community had introduced mechanisms for limiting production in this sector. The Community plans to promote further discipline in this sector through substantive price cuts, limitation on government purchases and penalties for overproduction.

GATT Waiver for U.S. Agriculture

Following the U.S. request for a panel on soybeans, the E.C. requested a GATT dispute panel on the GATT waiver that allows the U.S. to limit imports of certain agricultural products. The so-called temporary waiver was granted in 1955 and applies to dairy products, sugar, cotton and peanuts, but the E.C. request concerns initially sugar and sugar products. The Community charges that the waiver leads to economic distortions in trade flows and has not been used according to its original purpose to solve agricultural surpluses.

U.S.-Japan Semiconductor Accord

The GATT published its conclusions in 1988 on a 1986 complaint filed by the Community against an agreement on semiconductors concluded between the United States and Japan. The panel stated that the agreement violated international trading rules and threatened the Community's legitimate interests.

The Community was particularly concerned about two aspects of the agreement: the monitoring by Japan of semiconductor export prices in third countries and the subsequent arbitrary price increase for Japanese semiconductors on the Community market.

The Community argued that it should determine for itself whether Japanese semiconductors are being sold below fair value in Europe, and whether such sales injure the E.C. industry.

U.S. Import Measures

GATT panels in 1987 condemned two U.S. import measures that the Community had complained were discriminatory--the "Superfund" tax on oil imports and the "customs user fee," which is in fact a supplementary customs duty. The Community expects U.S. authorities to adapt their regulations to comply with the panels' reports.

Fisheries

An agreement on access by Community fishermen to U.S. fishing zones was signed in February 1977, and renewed for the period 1984-89. The Community may consider a U.S. proposal to extend the agreement for a further two years. But, the Community has expressed its deep disappointment over both the substantial cuts made in the allocations to its fishermen and the progressive tightening of conditions attached to even these much reduced opportunities.

RECENT SETTLEMENTS

Pasta and citrus

The Community and the United States in August 1987 resolved a longstanding conflict over E.C. export refunds (subsidies) for pasta products. The United States argued that the refunds violated international trade rules prohibiting subsidies for processed products.

The E.C.-U.S. accord, which took effect October 1, 1987, does not challenge the principle of the E.C. pasta refunds. However, the Community agreed to reduce its refunds for pasta exported to the United States by 27.5 percent. It also agreed to ensure that 50 percent of its pasta exports to the U.S. take place under a system known as "inward processing relief."

Under this system, the Community imports a primary product--in this case durum wheat, which comes almost exclusively from North America--without applying import levies, and exports an equivalent amount in pasta products without export refunds.

The United States, for its part, agreed not to restrict E.C. pasta exports nor to reopen the pasta dispute at GATT level.

The pasta dispute was earlier entwined with a separate trade conflict over E.C. tariff preferences for citrus fruit from certain neighboring Mediterranean countries. Because of its objections to these preferences, the United States in 1985 slapped high customs duties on pasta products from the Community. The Community retaliated by increasing duties on walnuts and lemons from the United States.

This dispute was resolved in August 1986, when the parties agreed to reduce tariffs or increase quotas on certain products--the Community on citrus fruit and almonds, the United States on products affecting Mediterranean countries, notably olives and olive oil. The United States agreed not to make further complaints about the E.C. Mediterranean citrus preferences. The two parties also agreed on a "modus vivendi" for resolving the pasta dispute.

Enlargement

In January 1987, the Community and the United States settled a dispute over import measures resulting from the E.C. enlargement to include Spain and Portugal. The U.S. had objected to provisions of the Accession Treaty that it claimed would adversely affect its corn, sorghum and soybean exports. The Community argued that the effects of enlargement had to be evaluated as a whole, without singling out the agricultural sector. Spain and Portugal's trading partners, it noted, would benefit from a significant reduction in customs duties on a wide range of industrial products entering the two new member states.

Following particularly difficult negotiations, during which the parties threatened retaliatory and counter-retaliatory measures, the parties signed a four-year agreement. The Community agreed to buy 2 million tons of corn and 300,000 tons of sorghum annually at reduced levies, and to reduce customs duties on a range of industrial and processed agricultural goods. It

also agreed that Portugal would no longer reserve 15 percent of its grain market for E.C. suppliers as provided in the enlargement treaty.

Steel

Steel trade has been a source of recurring friction between the Community and the United States. Following a series of negotiations, the last of which ended in September 1986, virtually all the Community's steel exports to the United States (about 6 million tons a year) are now covered by restraint arrangements which will expire in September 1989.

AGRICULTURE

The United States often attacks the E.C.'s Common Agricultural Policy (CAP), charging that export subsidies give European farmers an unfair advantage in world trade. The Community argues that these subsidies comply fully with GATT rules, and moreover, that the U.S. has a wide range of direct and indirect subsidies of its own. Budget estimates for 1986 and 1987 show the United States spent more than double per farmer, compared with the Community.

The Community also emphasizes in response to allegations of protectionism that it remains the U.S. farmer's best customer and the world's biggest importer of agricultural products. It has traditionally run a trade deficit in agriculture with the United States. In fiscal year 1988, the Community easily retained its position as the U.S.'s main export market with imports from the U.S. rising again to reach \$7.5 billion--or more than 20 percent--of all U.S. farm exports. This enabled the U.S. to enjoy an increased farm trade surplus of \$3.4 billion with the Community.

Tensions between the Community and the United States over agriculture stem largely from the decline in U.S. farm exports, which fell from \$48 billion in fiscal year 1981 to \$28.6 billion in fiscal year 1987. Due to subsidies they have begun to recover, however, rising by 27 percent in fiscal year 1988 after a 10 percent gain in 1987. The Community has long argued--and this view is now widely accepted--that the previous decline was primarily due to U.S. price support levels, the high dollar in the early 1980s, and increased self-sufficiency and lack of money in developing countries.

The United States since 1985 has embarked on an aggressive policy of increasing its share of world agricultural markets. One example of this is the Export Enhancement Program, which has provided \$1.5 billion worth of commodities to U.S. exporters since early 1986 to help them boost agricultural sales, especially of wheat, on foreign markets. The U.S. Trade Act continues this program increasing possible expenditure by \$2.5 billion.

The European Community and its trading partners have condemned this move, which it believes is unwarranted and has disrupted world trade in agricultural products.

These frictions are the manifestation of a deeper phenomenon: the structural imbalance at world levels in several agricultural sectors, which require serious changes in agricultural policies in the main producing countries. The Community has readjusted the CAP over the last few years with substantial results in production, particularly in the milk, beef and grain sectors. The Community hopes these adjustments, which are extremely hard on European farmers, will be accompanied by similar modifications in the farm policies of the United States and other trading partners. For this reason, the Community attaches particular importance to the agriculture discussions that are taking place in the Uruguay Round of GATT talks. (See section on Uruguay Round, page 4.)

BACKGROUND

Although there is no formal agreement establishing a general framework for relations between the Community and the United States, contacts between the two sides are frequent: consultations between officials, exchanges of visits by U.S. Secretaries and E.C. Commissioners, and close contacts through the Commission Delegation in Washington and the U.S. Mission in Brussels have taken place since the founding of the Community. Members of the U.S. Congress and the European Parliament also meet twice annually.

In 1981, it was decided to step up dialogue at the political level and since then a large U.S. Cabinet-level delegation led by the Secretary of State has met each year with a Commission delegation headed by the Commission President.

The ground rules applied to the bilateral relationship between the Community and the United States are those of multilateral organizations such as the GATT and the OECD. In trade, general GATT rules apply, notably the Most Favored Nation clause. Thanks to these rules, the GATT contracting parties have been able to set up a relatively transparent nonpreferential structure for trade tariffs and, through the GATT rules and codes, accept binding arrangements for most other matters concerning trade. In terms of quantitative restrictions, trade has been almost totally liberalized.