CHAPTER 3
Effect of Market Access Provisions for Goods: Sector-specific Assessment

This chapter provides assessments and views of interested parties on specific merchandise sectors. Many sectors in U.S.-Peru bilateral trade that represent leading products by volume were not selected for in-depth analysis because these sectors are not expected to experience large changes directly as a result of the implementation of the U.S.-Peru TPA. In addition, the products in many of these high-volume sectors enter the United States free of duty or at very low rates of duty; the removal of such small barriers is not expected to substantially affect trade flows or investment. Examples of high-volume sectors include minerals and metals, such as copper, gold, silver, tin, and zinc, and energy-related products, such as petroleum and natural gas.

Sectors were selected for analysis in this chapter on the basis of a number of criteria, including the importance of the sector in terms of bilateral trade; the likelihood of increased export opportunities for U.S. producers relative to other foreign suppliers; the extent and speed of trade liberalization under the TPA and its potential for increasing U.S. trade; the opinions of industry representatives; and the apparent sensitivity of certain U.S. industries to trade liberalization. The Commission's assessments in this chapter are based on industry knowledge and expertise of USITC industry analysts, industry sources, reports by U.S. industry and functional trade advisory committees on the TPA, and written submissions received in response to the Commission's *Federal Register* notice of institution for this investigation.[1] These sectors are grain, cotton, sugar and sugar-containing products, asparagus, meat, textiles and apparel, leather goods and footwear, and pharmaceuticals. Unlike the assessment conducted in the previous chapter, which analyzed the potential effect of the TPA from an economy-wide perspective, this chapter focuses primarily on sector- and industry-specific institutional factors. These include sector-specific assessments of the potential effects of factors such as price-band levies, duty drawback, SPS measures, government land policy, and consumer perceptions and tastes. This partial equilibrium focus of the sector-specific assessments complements the economy-wide analysis, providing both breadth and depth to the Commission's assessment of the potential effect of the U.S.-Peru TPA.

Summary of Assessment

Although the TPA may have a perceptible effect on U.S.-Peru bilateral trade in a specific sector, given the small size of U.S. trade with Peru in relation to total U.S. trade and the entire U.S. sector-specific markets, the TPA is not expected to have a large effect on total U.S. imports, exports, or production for any given sector.

- **Grain:** The TPA is expected to increase U.S. exports to Peru of wheat, rice, and corn as a result of the immediate removal of tariffs for some products and eventual phase-out of TRQs and associated large over-quota tariff rates. The TPA will also enhance U.S.

[1] A copy of the *Federal Register* notice is in app. B.

suppliers' competitive position vis-à-vis other regional suppliers and remove the distortions created by Peru's price-band levy system.

- **Sugar and sugar-containing products:** The TPA is not expected to substantially affect U.S. imports or exports of sugar or sugar-containing products primarily because of the TPA requirement that Peru be a net exporter. Peru's less efficient production, limited growth of the U.S. sugar TRQ for Peru, and the relatively small market in Peru compared with the U.S. market are other mitigating factors.

- **Asparagus:** Although the TPA is not expected to have additional market-access effects on U.S. asparagus farmers, permanent duty-free access to the U.S. market, especially for frozen and preserved asparagus, may spur additional investment in Peru by U.S. grower-suppliers and processors, expanding year-round imports of fresh asparagus, and increasing Peruvian imports of frozen and preserved asparagus at the expense of imports from other sources.

- **Meat:** Despite the long phase-out periods for tariffs on some meat products, the increased market access (some limited to duty-free access through TRQs) provided by the TPA is expected to increase market penetration of U.S. exporters in the Peruvian market. This increase will likely result from the removal of high tariffs, enhanced competitive advantages vis-à-vis regional suppliers, and increased regulatory and SPS cooperation. Given the size of the U.S. market and efficiency of U.S. producers, the TPA is unlikely to have an effect on U.S. imports of meat products.

- **Textiles and apparel:** Liberalization of textiles and apparel trade under the TPA is likely to result in a small increase in imports from Peru, largely at the expense of other import sources rather than domestic producers. These effects are driven by Peru's small share in the U.S. market, certain rules of origin constraints, and increasing competition from other suppliers, especially China. As a result of the existing duty drawback program[2] in Peru, the TPA effect on U.S. exports of textiles is expected to be minimal. Given the differing types of apparel products supplied by the Andean countries, the expiration of ATPA will not likely induce much trade diversion in the short term. Possible long-term trade diversion will be mitigated by increasing international competition from other foreign suppliers.

- **Leather goods and footwear:** Although the TPA may result in a large percentage increase in imports of leather goods and footwear from Peru, the absolute value is likely to be small. The ability of Peruvian producers to take advantage of increased market access is mitigated by a lack of economies of scale and increasing competition from other import sources, such as China.

- **Pharmaceuticals:** Given Peru's expanding domestic health care market, the intellectual property rights (IPR) protection provisions in the TPA, and immediate duty-free entry into Peru for many pharmaceutical products, the TPA is expected to increase U.S. exports of pharmaceutical products. Anticipated increases are, in large part, driven by government procurement-related provisions allowing U.S. exporters to be more competitive in supplying Peru's state health care institutions.

[2] The duty drawback program allows Peruvian producers to recoup duties paid on textiles if subsequent apparel products are exported to the United States.

Grain (Wheat, Rice, and Corn)[3]

Assessment

The TPA is likely to have a substantial positive effect on U.S. grain exports, especially over the long term. The positive export effect results from increased market access through tariff removal and TRQ phase out, removal of Peruvian government support measures, and removal of competitive disadvantages vis-à-vis other grain suppliers to the Peruvian market. Exports could increase by an estimated 50 to 80 percent above the $107 million in U.S. grain exported to Peru in 2005. Approximately two-thirds of the expected additional U.S. grain exports will consist of U.S. rice, with the remainder divided equally between exports of U.S. corn and U.S. wheat. U.S. wheat exports should benefit immediately, but corn and rice exports will increase more slowly, over 6 to 17 years, because initial access is limited by TRQs. These results are generally consistent with the economy-wide analysis results that U.S. grain exports to Peru will increase substantially. However, by considering factors outside the scope of the simulation exercise (e.g., historic price-band protection that was very low in the simulation year), this analysis reaches different conclusions regarding the distribution of the increase among wheat, corn, and rice.

The TPA is likely to have no impact on U.S. imports of grain. Peru is a high-cost producer of grain and a net importer, exporting only small amounts, mostly to adjacent Andean countries. U.S. imports of grain from Peru averaged about $1 million annually from 2001 to 2005. U.S. MFN tariffs on grain are generally quite low, averaging 2.9 percent AVE from 2001 to 2005, and U.S. grain imports from Peru are duty free under ATPA.

The first full year of market access for U.S. grain exports to Peru is outlined in the tabulation below. Some highlights of the tabulation are immediate duty-free treatment for U.S. wheat and popcorn exports to Peru upon implementation of the agreement; up to 500,000 metric tons (MT) of U.S. yellow corn exports to Peru will receive duty-free access under the provisions of a TRQ; and up to 78,000 MT of U.S. rice exports to Peru will receive duty-free treatment in the first full marketing year of the agreement.[4]

U.S. grain exports to Peru in 2005 accounted for 1 percent of total U.S. grain exports to all countries ($11.4 billion).[5] Approximately 73 percent of U.S. grain exports to Peru in 2005 consisted of wheat; 19 percent, corn; and most of the remainder, rice. U.S. wheat exports to Peru totaled $78 million, and were primarily bread wheat rather than durum wheat. U.S. corn and rice exports to Peru totaled $20 million and $9 million, respectively, in 2005. The United States is a highly competitive grain exporter to many countries of the world, and supplied

[3] Includes HTS headings 1001 through 1006. The grain sector as described in this section of the report focuses on wheat, corn, and rice. Corn is the primary grain destined for livestock feed in the world. However, in Peru white corn is used solely in food, and yellow corn mainly in animal feed. Corn, barley, and sorghum are called "coarse grains" or "feed grains." Rice is traded as unmilled (rough) form, dehulled (brown) form, and milled or semimilled form.

[4] The TRQ for rice designates an Oct. 1 to Sept. 30 marketing year; therefore, assuming an implementation date of Jan. 1, 2007, the duty-free in-quota quantity of rice for marketing year one will be prorated to 9/12 of the base amount of 74,000 MT. The first full marketing year with a duty-free in-quota quantity of 78,000 MT will begin on Oct. 1, 2007 and run through Sept. 30, 2008.

[5] Compiled from official statistics of the U.S. Department of Commerce.

about 42 percent of Peruvian imports of grain in 2004 (the latest year for which data are available).[6]

U.S. grain exports to and market access in Peru

Product	U.S. exports to Peru		Peruvian market access		
	2001-05 average	*2005*	*First year TRQ*	*Over quota tariff*	*Basic rate, 2004*
	(1,000 metric tons)			(Percent AVE)	
Wheat	685	484	No quota	Free	17
Corn					
Yellow	170	196	500	25	12[a]
White	0	0	No quota	25	17
Popcorn	0.15	0	No quota	Free	12
Rice[b]	16	27	78	52	25[c]

Source: *U.S.-Peru TPA,* General Notes, Tariff Schedule of Peru, app. I; official statistics of the U.S. Department of Commerce; and USDA, FAS, "Peru Grain and Feed Annual 2005," 5, 8, and 12.

[a] Applied duty included a price-band levy that averaged 2 percent in the second half of 2004.
[b] Rice weight is given in milled rice equivalents; TRQ quantity is for the first full marketing year, which runs from Oct. 1, 2007 to Sept. 30, 2008.
[C] Applied duty included a price-band levy that averaged 14 percent in the second half of 2004.

Wheat

U.S. wheat exports will benefit immediately from the elimination of the applied 17 percent tariff on U.S. wheat; there are no quotas under the TPA nor does Peru impose a price-band duty on wheat imports (unlike rice and corn).[7] U.S. wheat exports to Peru are likely to increase by 5 to 15 percent above the 2005 level of U.S. wheat exports of approximately $78 million.

As the United States is the major supplier of wheat to Peru,[8] most of the expected increase in exports is driven by increased wheat consumption in Peru as a result of wheat duty elimination,[9] although some U.S. export sales may occur at the expense of competitors such as Argentina and Canada. South American grain has generally undersold U.S. grain in Peru in recent years, but the duty-free access that will be afforded by the TPA will narrow the price disadvantage. However, freight costs from the United States have been higher than from Argentina and Uruguay.[10]

[6] U.S. grain exports accounted for 42 percent of the $467 million of reported Peruvian imports in 2004, according to UN Comtrade data.

[7] The price-band system in Peru applies to imports of dairy goods, corn, sugar, and rice; the price-band system is similar to that maintained in the other Andean countries and Chile. Under this system, variable monthly duties, which may be positive or negative, are imposed on top of ad valorem tariffs to keep domestic prices within a predetermined range set annually. The system sets a floor price for domestic producers, and mitigates the changes in global prices on producers and consumers. USITC, *U.S.-Chile Free Trade Agreement*, 5, 90; and, USDA, FAS, "Peru Export Guide Annual 2005," 3, 5, and 8.

[8] In MY2004/05, Peru imported 90 percent of its domestic consumption of wheat. In 2004, the United States supplied about two-thirds of Peru's imports of wheat, with Canada and Argentina supplying the remainder. USDA, FAS, "Peru Grain and Feed Annual 2005," 3, 6, and 10.

[9] A 10 percent decline in wheat prices in Peru will likely lead to a nearly 4 percent increase in the quantity demanded. USDA estimated the Peruvian price elasticity of demand for wheat at -0.355. Elasticities represent 1989 data. USDA, ERS, *International Food Consumption Patterns.*

[10] USDA, FAS, "Peru Agricultural Situation CCC Programs in Peru 2003," 2.

In marketing year (MY) 2003/04, Argentine wheat (delivered to Peru) was priced about 3 to 5 percent below U.S. wheat.[11] Under Mercosur, Argentina received an 80 percent tariff reduction from the applied MFN rate.[12] In 2004, for example, Argentine wheat was dutiable at 3.4 percent AVE, and U.S. wheat was dutiable at 17 percent. The TPA immediately eliminates the competitive disadvantage for U.S. wheat exports inherent in Argentina's preferential duty in the Peruvian market.

The primary Peruvian government support for wheat has been the relatively high import duty and the 17 percent value-added tax (VAT) that Peruvian growers do not generally pay. Peruvian wheat production is quite small, supplying less than 10 percent of domestic wheat consumption. The effect on Peruvian wheat production is likely to be small.

Rice

U.S. rice exports are likely to increase in the long term by 10- to 15-fold above the 2005 U.S. rice export level of $9 million. Peruvian market access for U.S. exports of rice (and corn) will gradually expand through elimination of the Peruvian price band and the establishment and subsequent growth of TRQs for rice and corn (over a period of 6 to 17 years). In the 16th year of the TPA, duty-free access via the TRQ for rice amounts to 177,000 MT (currently valued at $50 million).[13] The expected increase in U.S. rice exports will likely stem from increased consumption caused by lower prices for rice after the duty elimination and, equally as important, a reduction in Peruvian rice production.[14] U.S. rice exports in 2004 to Peru consisted of 78 percent milled or semimilled rice, and 22 percent brown (husked) rice. As a result of an import ban (discussed below), there were no exports to Peru of U.S. rough or paddy rice in 2004; there was $3 million of U.S. rough rice exports to Peru in 2002. Removal of the SPS ban on rough rice under the TPA may result in future U.S. exports of rough rice to Peru.

The TPA also eliminates the competitive disadvantage of U.S. rice exports to Peru inherent in rice duty preferences for Uruguay. In 2004, Uruguay accounted for three-quarters of Peru's rice imports, with the United States supplying the remainder. As Peru imported relatively little rice (less than 3 percent of domestic consumption in MY2004/05),[15] any increased U.S. exports taken from competitor suppliers, such as Uruguay, will likely not be large.

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[11] In MY2003/04, U.S. soft red wheat (f.o.b. U.S. Gulf) was priced $2 per ton above Argentine wheat (f.o.b. Trigo Pan); the freight cost to Peru from Argentina was about $3 to $5 per ton lower than from the United States. Thus, the delivered price of Argentine wheat was $5 to $7 per ton (3 to 5 percent) below U.S. wheat. USDA, FAS, "Peru Grain and Feed Annual 2005," 7; and IGC, *World Grain Statistics 2003,* 9a–9b.

[12] USDA, FAS, "Peru Grain and Feed Annual 2005," 2.

[13] *U.S.-Peru TPA*, General Notes, Tariff Schedule of Peru, app. I, note 7(a). The average price of U.S. Southern long-grain milled rice, U.S. Gulf ports, was $312 per metric ton in MY2004/05. USDA, ERS, *Rice Outlook*, table 6.

[14] On the basis of USDA studies of Peru, a 10 percent decline in the rice price in Peru will likely lead to a nearly 4 percent increase in the quantity demanded, based on the price elasticity of demand for grain. Meanwhile, a 10 percent decline in the rice price would likely lead to a 5 percent drop in Peruvian rice production. Elasticity of supply represents database South American regional grouping, and trade liberalization elasticities represent 1989 data. USDA, ERS, *International Food Consumption Patterns;* and USDA, ERS, *Easticities in the Trade Liberalization Database*.

[15] USDA, FAS, "Peru Grain and Feed Annual 2005," 3, 6, and 10.

The TPA provides that the Peruvian price-band system will not apply to U.S. agricultural products, including those granted market access under the TRQs.[16] The over-quota tariff is a ceiling binding on the price band applied to rice (and corn) imports. However, if the price-band levy is lower than the over-quota tariff, then U.S. goods are dutiable at the lower price-band rate.[17] In the second half of 2004, the average price-band rate on rice amounted to 14 percent.[18] However, since 2001, price-band duties on rice have been as high as 116 percent.[19]

The Peruvian government has historically had an import substitution policy with regard to rice, which substantially increased domestic rice production, sometimes leading to lower producer prices, and excessive carryover stocks.[20] Rice imports were dutiable at 25 percent AVE, subject to the levy under the price-band system, and subject to the 17 percent VAT that domestic producers frequently do not pay.

The Peruvian SPS authority, SENSA, imposed an SPS ban on imports of rough rice from countries where the Kharpra Beetle is persistent, including the United States.[21] Under the TPA, the Peruvian government indicated that it would withdraw the specific decree banning rough rice imports from the United States, and would in the future, "apply standards on rice imported from the United States no less favorable than those applied to domestic products."[22] However, the Peruvian government reserves the authority to reimpose the ban, although as more scientific information on controlling the pest is exchanged between the United States and Peru, this may not occur. [23]

Corn

Over the long term, U.S. corn exports are likely to more than double from the $20 million level of U.S. exports to Peru in 2005. In the short term, however, growth is limited by quotas on U.S. yellow corn, with prohibitive over-quota tariffs. Nonetheless, there will be a substantial increase in U.S. duty-free access as the initial quotas are set well above the level of U.S. exports to Peru during the past 5 years. For white corn (and popcorn), there will be immediate duty-free, quota-fee access to the Peruvian market.

Anticipated increases in exports of U.S. corn will likely result from increased corn consumption in Peru stimulated by a lower domestic price (as the tariff is removed), as well as a reduction in Peruvian corn production.[24] In MY2004/05, Peru imported 38 percent of its corn consumption;[25] in recent years, Argentina accounted for two-thirds of Peru's corn imports, with the United States the only other significant supplier. In MY2003/04, Argentine

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[16] *U.S.-Peru TPA,* General Notes, Tariff Schedule of Peru, app. I, note 2(a).

[17] ATAC for Grains, Feed and Oilseeds, *Draft GF&O Report on U.S.-Peru TPA*, 2.

[18] USDA, FAS, "Peru Grain and Feed Annual 2005," 8 and 12.

[19] In Feb. 2002, the levy was $221/metric ton, and the U.S. export price was $190/metric ton. USDA, FAS, "Peru Grain and Feed," 10.

[20] USDA, FAS, "Peru Grain and Feed Annual 2005," 12.

[21] Ibid. U.S. rough rice was imported in 2002, but the ban was reimposed in 2003.

[22] Peru's Council of Ministers, *Letter Exchange on SPS/TBT Issues for the U.S.-Peru TPA*, #4.

[23] ATAC for Grain, Feed and Oilseeds, *Draft GF&O Report on U.S.-Peru TPA*, 4.

[24] The USDA studies of Peru indicate that a 10 percent decline in corn prices in Peru will likely lead to a near-4 percent increase in the quantity demanded, based on the price elasticity of demand. The same 10 percent decline in price will likely lead to a 4 percent drop in Peruvian corn production. Elasticity of supply represents database South American regional grouping, and trade liberalization elasticities represent 1989 data. USDA, ERS, *International Food Consumption Patterns;* and USDA, ERS, *Elasticities in the Trade Liberalization Database*.

[25] USDA, FAS, "Peru Grain and Feed Annual 2005," 3, 6, and 10.

corn (delivered to Peru) was priced approximately 9 to 10 percent below U.S. corn.[26] In 2004, as a result of a previous trade agreement, Argentine corn was dutiable at 3.4 percent while U.S. corn was dutiable at 17 percent.[27] The TPA eliminates the competitive disadvantage of U.S. corn exports to Peru inherent in duty preferences for Argentine corn. Consequently, as a result of the TPA, some market share may be taken from other suppliers, such as Argentina.

In the second half of 2004, the average price-band levy on yellow corn amounted to 2 percent, but price-band rates have been as high as 21 percent since 2001.[28] In addition to the price band, the government of Peru has provided support and assistance for corn growers in the form of rotating credit funds and a policy encouraging local poultry growers to purchase locally produced corn.[29] Some poultry operations purchase only Peruvian corn through agreements with Peruvian growers sponsored by the government (so-called "absorption requirements"). Under the TPA, the absorption requirements will be eliminated, further increasing the competitive advantage of U.S. grain exporters.

Views of Interested Parties

The U.S. grain industry endorses the TPA, and indicates that the agreement reduces Peruvian tariffs on grain and negates the adverse effects of Peruvian policies, such as price bands and the absorption requirements. The agreement will provide, in the industry's view, both immediate and long-term benefits to U.S. producers and processors of grain, feed, and oilseeds.[30]

Cotton[31]

Assessment

The cotton provisions of the U.S.-Peru TPA are uniquely significant because the U.S.-Peru TPA is the first U.S. bilateral FTA that provides for immediate duty-free, quota-free trade in cotton fiber between the United States and another trading partner.[32] The provisions of the U.S.-Peru TPA are likely to have a significant, positive effect on U.S. cotton exports to Peru. However, the increase is unlikely to have a significant effect on total U.S. cotton exports. From 2003 to 2005, total U.S. cotton exports averaged more than 2.9 million MT. Peru accounted for about 1 percent of this total. If the United States were to supply 100 percent of Peru's current cotton imports, U.S. exports would be expected to increase by about 3,500 MT, less than 0.2 percent of total U.S. cotton exports. The TPA is not likely to have

[26] In MY2003/04, the price of U.S. corn (f.o.b. U.S. Gulf) was $7 per metric ton above Argentine corn (f.o.b. Up River), making the delivered price of Argentine corn $10 to $12 per ton (9 to 10 percent) below the price of U.S. corn. USDA, FAS, "Peru Grain and Feed Annual 2005," 7; and IGC, *World Grain Statistics 2003*, 9a–9b.

[27] USDA, FAS, "Peru Grain and Feed Annual 2005," 2.

[28] Ibid, 8; and "Peru Grain and Feed Annual 2002," 7.

[29] Peru imports a substantial amount of yellow corn for poultry feed. By year 11 of the TPA, the import quota for U.S. corn expands to 895,000 metric tons, currently valued at $90 million. The average price of U.S. corn, No. 3 yellow. f.o.b., U.S. Gulf ports, was $99 per metric ton in crop year 2004/05. *U.S.-Peru TPA*, General Notes, Tariff Schedule of Peru, app. I, note 7(a); and *Oil World*.

[30] ATAC for Grains, Feed and Oilseeds, *Draft GF&O Report on U.S.-Peru TPA*.

[31] This sector includes cotton fiber classified under HTS headings 5201, 5202, and 5203, but the analysis focuses on trade in cotton classified under HTS 5201, cotton, not carded or combed.

[32] ATAC for Tobacco, Cotton, Peanuts and Planting Seeds, *Advisory Committee Report*.

an effect on U.S. cotton imports from Peru. These results are consistent with the economy-wide simulation that shows a small increase in Peruvian imports of U.S. plant-based fiber products.

The TPA makes permanent the duty-free treatment currently provided under ATPA for U.S. imports of Peruvian apparel and grants additional duty-free access to U.S. imports of Peruvian textiles. Since ATPDEA expanded ATPA in 2002, Peru's textile and apparel sector has grown by more than 25 percent, stimulating Peru's demand for cotton. Peru's textile and apparel industry currently has capacity to process about 100,000 MT of cotton annually.[33] From 2000 to 2004, Peru's cotton production averaged 53,556 MT.[34] To use its textile and apparel production capacity efficiently, Peru imported an average of 39,625 MT of cotton annually from 2000 to 2005, of which 27,155 MT, or more than two-thirds, were imported from the United States. Although the permanence of the TPA may induce additional investment in textile and apparel capacity, which likely will increase further Peru's demand for cotton, low productivity and high cost mitigate Peruvian producers' ability to supply additional cotton. Therefore, increased cotton demand is unlikely to be entirely supplied by domestic cotton production, and Peru can be expected to continue as a net importer of cotton.

Technical production issues will continue to limit Peru's ability to efficiently grow and supply cotton for the domestic textile and apparel industries. In the 1980s, Peru planted nearly 140,000 hectares of cotton; by 2000–2004, planted area had dropped to fewer than 76,000 hectares. The primary variety of cotton grown in Peru is a long-staple variety that accounts for approximately 78 percent of total cotton production. This variety requires a long growing season that makes it more susceptible to pest infestations, such as boll weevils, which can require the use of pesticides that can double production costs.[35] Other factors contributing to production and market inefficiencies include the small size of farm production units, low yields resulting from poor production practices and low seed quality, the lack of technical assistance to improve production practices, and the lack of agricultural credit.[36]

In addition, in response to cotton growers' protests against the TPA, Peru instituted a $4.30 per hundredweight cotton subsidy,[37] which is equivalent to about $95 per metric ton,[38] but only offsets about 57 percent of the likely price effect of immediate duty-free treatment for U.S. cotton exports to Peru. While the subsidy may stabilize or even stimulate increased Peruvian cotton production in the short run, without improvements in those conditions that result in low productivity and high costs among Peruvian cotton growers, Peru's cotton production sector is likely to decrease in size, resulting in lower production and increased demand for cotton imports in the long run.

However, the TPA may indirectly result in some increased production of Pima cotton as growers respond to the phase-out of duties on rice. Production of Pima cotton, the second most popular variety accounting for about 18 percent of production, has been unstable and insufficient to supply local demand for extra-long-staple fiber because Pima cotton producers

[33] USDA, FAS, "Peru Cotton and Products, Update 2005."
[34] Ibid.
[35] Ibid.
[36] Ibid.
[37] Ibid.
[38] The average unit value of Peru's cotton imports from 2000 to 2005 was $1,382 per MT. The applied duty of 12 percent translates into protection of about $166 per MT.

choose to grow cotton only if there is insufficient water to grow rice.[39] Because the Peruvian rice market has been more highly protected than the cotton market,[40] the TPA may alter the relative domestic prices of rice and Pima cotton so Pima cotton production becomes more consistently attractive in the future.

U. S. cotton exporters' ability to take advantage of increased market access may be mitigated by increasing international competition. As indicated, the United States has been the dominant supplier of cotton to Peru, holding a 68.5 percent import market share from 2000 to 2005. However, Peru's import market share composition has changed in the last 5 years as new competitors have entered the market. Brazil entered the Peruvian market in 2002 and has become a primary competitor for U.S. cotton exports. Peruvian imports of cotton from Brazil began with 367 MT in 2004 rising to an average of 8,112 MT in 2005. Peruvian cotton imports from Bolivia have been fairly stable throughout this period, accounting for nearly 7 percent of the import market share, while cotton imports from Argentina dropped from 12,800 MT and a 32.3 percent share in 2001 to zero in 2005.[41]

The TPA does not provide U.S. cotton a competitive advantage relative to Bolivian cotton in the Peruvian market because, as a member of the Andean community, Bolivian cotton receives duty-free treatment. The agreement does, however, provide U.S. cotton a price advantage over Brazilian and Argentinian cotton in the Peruvian market for 12 years. All cotton imports from Brazil, and cotton imports with a staple length greater than 27.8 mm from Argentina, currently receive a 30 percent margin of preference in the Peruvian market.[42] However, under the Peru-Mercosur trade agreement, cotton imports from Argentina and Brazil do not receive duty-free treatment until January 1, 2019.[43] If U.S., Argentinian, and Brazilian cotton are highly substitutable, the near-term increase in U.S. cotton exports to Peru could be significant. Recently, Argentinian cotton has become less competitive because increased domestic demand has resulted in low volumes available for export, and because of contamination problems.[44] On the other hand, the Brazilian cotton industry is rapidly becoming a highly competitive export supplier, with Brazilian industry leaders believing that Brazilian cotton exports may significantly replace U.S. cotton exports as U.S. cotton support programs are adjusted to comply with the WTO "Subsidies on Upland Cotton" ruling.[45]

Views of Interested Parties

The U.S. cotton industry supports the U.S.-Peru TPA because it believes that the cotton provisions of the agreement will be strongly beneficial to both the United States and Peru, given the characteristics of cotton, textile, and apparel trade between the two countries. The cotton industry also notes that the agreement contains acceptable rules of origin for cotton-based textiles with fewer exceptions than other U.S. free trade agreements.[46]

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[39] USDA, FAS, "Peru Cotton and Products, Update 2005."

[40] Rice has been subject to the Andean price band with AVE duties ranging from 40 percent to 120 percent from 2001 to 2004.

[41] *Global Trade Atlas.*

[42] The margin of preference represents the percentage discount off the MFN duty rate, e.g., a 30 percent margin of preference on the 12 percent cotton duty represents a discount of 3.6 percentage points, resulting in an applied duty of 8.4 percent. ALADI, *Acuerdo de Complementación Económica.*

[43] Ibid., AAP.CEN.58, apéndice 1-A.

[44] USDA, FAS, "Argentina Cotton and Products, Update 2005."

[45] USDA, FAS, "Brazil Cotton and Products, Update 2005"; and WTO, *United States – Subsidies on Upland Cotton*.

[46] ATAC for Tobacco, Cotton, Peanuts and Planting Seeds, *Advisory Committee Report*.

Sugar and Sugar-containing Products[47]

Assessment

The U.S.-Peru TPA provisions concerning sugar and sugar-containing products (SCP) are unlikely to have a significant effect on the U.S. sugar market for either producers or users.[48] Historic production, consumption, and trade patterns suggest that Peru may not be able to consistently meet the TPA's net-exporter provision.[49] Moreover, even when Peru is able to meet the net-exporter provision, Peru's duty-free access to the U.S. market under the TPA is limited to the initial size (9,000 MT) and growth rate (180 MT annually) of the TRQ in-quota quantity, which is small relative to the size and growth of the U.S. sugar market. Furthermore, U.S. over-quota tariff rates are not affected by this agreement. Although U.S. market access commitments above the WTO minimum have been increasing as a result of NAFTA and CAFTA-DR, the increase proposed under the U.S.-Peru TPA is relatively minor and likely would not result in import levels that would trigger the suspension of domestic marketing allotments. In addition, the U.S.-Peru TPA contains a compensation mechanism whereby the United States could limit sugar imports under the agreement in exchange for compensation (amount not specified in the TPA). Although the provisions of the TPA are unlikely to have an effect on U.S. exports of raw cane and beet sugar, the TPA may affect the exports of other sweeteners and syrups and sugar-containing confectionery to Peru. These results are consistent with the economy-wide simulation results that show a small increase in the value of sugar trade between the United States and Peru.

Peru is unlikely to meet the net exporter provision of the TPA, which limits Peru's sugar exports to the United States (beyond those allocated by the U.S. WTO TRQs) to the lesser of the specified TRQ quantity or the amount by which Peru's total imports exceed its total exports, excluding sugar trade with the United States. Peru would not have met the net-exporter provision of the agreement in 5 of the past 6 years (2000–2005).[50] Peru has generally been a net importer of sugar as domestic production has fallen short of domestic consumption by an average of 153,000 MT annually since 1983.[51] Furthermore, sugar

[47] The discussion of U.S. imports in this sector includes raw sugar, refined sugar, sugar syrups, and sugar-containing products classified in chaps. 17, 18, 19, and 21 of the HTS that are subject to TRQs, and all items that are covered by the sugar provision of the TPA. The discussion of U.S. exports in this section is limited to raw sugar, refined sugar, sugar syrups, and sugar-containing products classified in chap. 17.

[48] The U.S. sugar-producing sector addressed in this section of the report primarily consists of sugarcane growers, sugarcane millers, raw cane sugar refiners, sugar beet growers, and sugar beet refiners. This section of the report does not generally address producers of corn-based sweeteners, e.g., high-fructose corn syrup. The U.S. sugar-using sector generally consists of a wide range of food and beverage manufacturers, though the three largest sugar-consuming sectors in the United States are nonchocolate confectionery, chocolate and chocolate confectionery, and breakfast cereal.

[49] The net-exporter provision of the TPA reads as follows: "In any year, duty free tariff treatment under subparagraph (a) for Peru shall be accorded to the lesser of (i) the aggregate quantity set out in subparagraph (a) for Peru, or (ii) a quantity equal to the amount by which Peru's exports to all destinations exceeds its imports from all sources ("trade surplus") for goods classified under the following subheadings: HS 1701.11, HS 1701.12, HS 1701.91, HS 1701.99, HS 1702.40, and HS 1702.60, except that Peru's exports to the United States of goods classified under subheadings HS 1701.11, HS 1701.12, HS 1701.91, and HS 1701.99 and its imports of originating goods of the United States classified under HS 1702.40 and HS 1702.60 shall not be included in the calculation of its trade surplus. Peru's trade surplus shall be calculated using the most recent annual data available." (*U.S.-Peru TPA*, annex 2.3, I4–I5.)

[50] Based on USITC staff estimates using *Global Trade Atlas*.

[51] USDA, FAS, "Dataset for centrifugal sugar."

exported to the United States to obtain quota rents[52] under the U.S. WTO sugar TRQs has been replaced by imports over this period.[53] Therefore, to fully supply the average domestic shortfall since 1983 and the minimum U.S. WTO TRQ access allotment of 43,174 MT, Peru's average production would have needed to be 196,000 MT greater, or 26 percent greater than the average production of 752,000 MT over this period.[54]

Recent changes in the structure of Peru's sugar industry, however, may affect Peru's ability to achieve net-exporter status in the future. Much of the historic shortfall in domestic sugar production has been attributed to a 1968 land reform in which expropriated assets of private sugar companies were distributed to workers' cooperatives, resulting in production inefficiencies and lack of investment to upgrade cane fields and sugar mills.[55] Sugar production fell from a 1974 peak of more than 1 million MT to 415,000 MT by 1993.[56] Peruvian laws were changed in 1996 to encourage private investment in the sugar cooperatives. These changes increased private investment in the sugar industry, resulting in increased production. By 2004, Peru had its first sugar surplus since 1985.[57] The 2005 shortfall has been attributed to drought conditions, and production is expected to recover in 2006.[58] Furthermore, in January 2006, the Peruvian government sold the 31 percent share it had acquired to support Peru's largest sugar cooperative, Casa Grande, to a private conglomerate, Grupo Gloria.[59] Grupo Gloria is expected to increase investment in cane fields and milling technology. The Casa Grande mill is currently operating at one-third of its 300,000 MT capacity.[60] USDA estimates that increased investment in the Casa Grande mill and sugar fields that supply it can increase Peru's total sugar production to 1.2 million MT,[61] sufficient to make Peru a net sugar exporter based on current domestic demand. In addition, Peru's cost of production is significantly lower than the typical U.S. market price and the loan forfeiture price administered in the U.S. sugar program.[62]

Other factors, however, can offset the potential for increased sugar exports. First, general economic growth could increase the domestic demand for sugar in Peru. Second, high oil prices and recent Peruvian legislation to increase the use of biofuels have induced sugar mills to consider ethanol as an alternative to sugar production.[63] Third, dependence on irrigation makes Peruvian sugar production susceptible to drought, which can make production variable from year to year.

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[52] U.S. border protection measures (TRQs) help maintain an internal price that is typically greater than the price available on the world market. Therefore, allocation of licenses to quota holders for sugar imports creates quota rents.

[53] Peru's basic WTO TRQ allocation of 43,174 MT of raw cane sugar is among the largest allocations, ranking sixth, and accounting for nearly 3.9 percent among the U.S. WTO minimum market access commitment of 1,117,195 MT. Furthermore, during FY2005, Peru received an additional allocation of 8,476 MT for a total of 51,651 MT; and for FY2006, Peru has been allocated up to 73,664 MT of duty-free access for raw cane sugar.

[54] USDA, FAS, "Dataset for centrifugal sugar."

[55] USDA, FAS, "Peru Sugar Annual, 2005."

[56] USDA, FAS, "Dataset for centrifugal sugar."

[57] Ibid.

[58] USDA, FAS, "Peru Sugar Annual, 2005."

[59] Reuters, "Gloria Takes Over Peru Sugar Mill."

[60] Ibid.

[61] USDA, FAS, "Peru Sugar Annual, 2005."

[62] The current U.S. raw sugar price is about 24 cents per pound. USDA, ERS, "Table 4—U.S. raw sugar price." The current loan forfeiture price under the U.S. sugar program is 18 cents per pound for raw cane sugar and 22.9 cents per pound for refined sugar. USDA, ERS, "Sugar and Sweeteners: Policy." Data on Peru's cost of production are proprietary and are from LMC, *LMC Worldwide Survey*.

[63] USDA, FAS, "Peru Sugar Annual, 2005."

If in the future, Peru is able to meet the net exporter provisions of the agreement, the TPA is still unlikely to have a significant effect on the U.S. domestic sugar market. Additional duty-free access for Peruvian sugar and SCPs in the U.S. market is initially limited to 9,000 MT, which grows by 180 MT annually, plus 2,000 MT of specialty sugar.[64] These provisions will limit Peruvian sugar exports to the U.S. market because current MFN over-quota duty rates associated with WTO TRQs for sugar and SCP are generally prohibitive and not affected by the TPA. The initial additional in-quota quantity of 9,000 MT represents less than one-tenth of 1 percent of the 9.7 million MT of sugar expected to be consumed in the United States during FY2006.[65] Furthermore, comparing U.S. sugar consumption at the average annual growth rate of 1.3 percent (1994–2005) with the TPA duty-free in-quota quantities over the same period of time indicates that the TPA in-quota quantity is unlikely to ever exceed more than one-tenth of 1 percent of U.S. domestic sugar consumption, nor is it likely to exceed a nearly-insignificant amount in terms of the total U.S. domestic market for sweeteners.

Furthermore, any potential effect of increased duty-free access for sugar and SCP imports from Peru depends on the potential effect of imports from other trading partners subject to bilateral or regional trade agreements with the United States that have yet to be fully implemented or phased in. Under NAFTA provisions, Mexico has been allocated more than 250,000 MT (about 2.6 percent of U.S. domestic consumption) of sugar exports to the U.S. market during FY2006 subject to a net-exporter provision, and, as of January 2008, Mexico will have unlimited duty-free access to the U.S. sugar market. Under the provisions of the as yet not fully implemented CAFTA-DR, the Dominican Republic and other Central American countries will have additional duty-free access of 109,000 MT (about 1.19 percent of U.S. domestic consumption) initially, growing at 2 percent of the initial amount annually. Imports of sugar and SCP resulting from these agreements are far more likely to affect the U.S. market than the relatively small amount of additional duty-free access in the U.S.-Peru TPA, particularly with respect to the potential to trigger the suspension of U.S. marketing allotments.

The TPA is unlikely to have a significant effect on U.S. exports of raw cane and beet sugar because the United States is primarily an importer of these products. Furthermore, though the TPA may result in increased exports of other sweeteners and SCP classified in HS chapter 17, it is unlikely to have an effect on the total exports of sugar, other sweeteners, and SCP classified in that chapter because Peru is a small market relative to total U.S. exports of these products. From 2001 to 2005, U.S. exports to Peru were less than 0.5 percent of total U.S. chapter 17 exports, averaging $3 million to Peru compared with a world total U.S. exports of $697 million.[66] The United States is a competitive producer of alternative sweeteners, including lactose and high-fructose corn syrup (HFCS). Without the benefits of the TPA, U.S. lactose exports to Peru have grown from less than $4,000 in 2000 to more than $1 million in 2005.[67] Duty-free treatment of U.S. lactose exports upon implementation of the TPA should continue to facilitate the growth of U.S. lactose exports to Peru. High fructose syrups (those with 50 percent or more fructose by weight on a dry matter basis) were subject to a high and unpredictable price band. Consequently, U.S. exports of these

[64] Peru has been given an allocation of 2,000 MT of specialty sugar, which represents a country-specific allocation within the current chap. 7, note 5, TRQ which was allocated on a first-come, first-served basis. *U.S.-Peru TPA,* annex 2.3, I4–I5.

[65] USDA, ERS, *Sugar and Sweeteners Outlook,* Table 4, 10; converted to MT at rate of 1 metric ton = 1.10231123 short tons.

[66] USITC, *Dataweb*.

[67] Ibid.

products were highly variable, recently ranging from $100,780 in 2003 to $704,102 in 2005.[68] Elimination of the price band and a 5-year phase-out of the remaining duties on high fructose syrups should make U.S. exports of HFCS more competitive in the Peruvian sweetener market, especially as an input into soft drink production.

Views of Interested Parties

Both U.S. sugar producers and U.S. sugar consumers agree that the U.S.-Peru TPA is unlikely to negatively affect the U.S. sugar-producing industry.[69] However, U.S. sugar producers believe that including sugar in bilateral FTAs does not promote the objectives of the U.S. sugar-producing sector.[70] The American Sugar Alliance (ASA), representing U.S. sugar beet and sugar cane growers, prefers that U.S. sugar market access is negotiated in the multilateral WTO context in which foreign subsidies to sugar production can be addressed.[71] Sugar producers on the ATAC characterized that the additional market access extended to Peru as considerably more reasonable than the additional access extended in CAFTA-DR.[72] Sugar producers on the sweeteners ATAC also noted that, as a large net importer, the United States has no prospects for exporting sugar to Peru.

U.S. sugar consumers also believe that the TPA is unlikely to have negative effects on U.S. sugar producers; moreover, sugar users believe that the agreement will promote fair competition and help ensure an ample supply of sugar in the U.S. market.[73] U.S. sugar consumers support comprehensive product coverage, including sugar, in U.S. regional and bilateral FTAs. In addition, sugar consumers expressed their view that the increased access extended to Peru was extremely modest and that maintaining over-quota rates indefinitely was a substantial compromise from the goal of fully liberalized trade.[74] The Grocery Manufacturers Association, representing many sugar-consuming food manufacturers, stated that the agreement will stimulate increased manufactured food exports to Peru, helping balance the exchange of goods between the two countries, and will stimulate U.S. job growth in food manufacturing.[75]

Asparagus[76]

Assessment

The U.S.-Peru TPA is likely to maintain and potentially expand the positive effects of ATPA on U.S. consumers, importers, and distributors of asparagus. The TPA is unlikely to have additional negative effects on U.S. growers of fresh asparagus, though continued consolidation, rationalization, and relocation in the processing industry is likely to effect

[68] Ibid.
[69] ATAC for Sweeteners and Sweetener Products, *Advisory Committee Report*.
[70] Ibid., majority view, 5–7. In addition to representatives of cane and beet producers, the American Beekeeping Federation participated in the majority view.
[71] American Sugar Alliance, *Statement from U.S. Sugar Producers*.
[72] ATAC for Sweeteners and Sweetener Products, *Advisory Committee Report*.
[73] Ibid., minority view, 7–8.
[74] ATAC for Sweeteners and Sweetener Products, *Advisory Committee Report*.
[75] Grocery Manufacturers Association, "News Release: GMA Commends the Conclusion of Successful Trade Negotiations."
[76] This section considers imports of fresh, frozen, and processed asparagus classified under HTS tariff lines 0709.20.1000, 0709.20.9000, 0710.80.7060, 0710.80.9710, and 2005.60.0000.

growers in Michigan and Washington that historically had grown asparagus primarily for processing. Increases in current import growth rates of fresh asparagus may be stimulated by increased demand through expansion of seasonal availability and increased U.S. grower-shipper investment in the Peruvian industry. Furthermore, increased investment by U.S. processors in the Peruvian industry, which has been linked to divestment in U.S. asparagus processing capacity, may push additional domestic production in Washington and Michigan into the fresh market and increase U.S. imports of canned and frozen asparagus. ATPA preferences have provided Peru with duty-free treatment for fresh, frozen, and processed asparagus since 1991. These preferences are scheduled to expire at the end of 2006. Without renewal, duties would increase to between 5.0 and 21.3 percent, because Peruvian asparagus is not eligible for GSP treatment.[77] Under the terms of the TPA, Peru's duty-free access to the U.S. asparagus market is made permanent. The results discussed in this section are not comparable to the economy-wide simulation results because asparagus trade makes up a small portion of the GTAP food products n.e.c. and vegetables, fruits, and nuts sectors, and thus its individual effect is not measurable.

Since implementation of ATPA preferences in 1991, U.S. asparagus imports from Peru have increased at an average annual rate of 157.4 percent, compared with an average annual rate of 10.8 percent for U.S. asparagus imports from Mexico, and an average annual rate of 27.4 percent for total U.S. asparagus imports. By comparison, U.S. asparagus production has declined at an average annual rate of 1.9 percent over the same period. By 2001, asparagus imports from Peru exceeded asparagus imports from Mexico, making Peru the largest foreign supplier of asparagus to the U.S. market. In 1991, Mexico held a 75 percent share of U.S. asparagus imports versus 12 percent for Peru; by 2005 Peru held 59 percent versus 39 percent for Mexico.[78] Historically, more than 90 percent of U.S. asparagus imports from Peru were fresh. More recently, however, canned asparagus imports from Peru have increased from 401 MT in 2001 to more than 7,219 MT in 2005. As a result, fresh asparagus imports from Peru decreased to 86 percent of the total asparagus imports from Peru in 2005.[79]

Initially, fresh asparagus imports from Peru were seasonal and declined beginning in January, lessening the effect on U.S. producers. Over time, as Peru became a year-round producer and shipper, the effect on U.S. producers increased. Peru now supplies fresh asparagus to the U.S. market year round, including February and March,[80] which coincides with the beginning of the California production season. California is the primary U.S. supplier of fresh asparagus, providing about 74 percent of U.S. fresh asparagus production in 2005; California is the only U.S. supplier from January to March. Some growers report that prices are lower when imported supplies overlap with their normal shipping season. For example, even though prices for fresh asparagus from California are lower in late January, some U.S. retailers in the Southeast continue to purchase Peruvian asparagus as long as supplies are available.[81] Other grower-shippers suggest that rising imports have forced them to become more efficient in their overall operations. Some larger-volume U.S. grower-shippers are investing in operations in California, Mexico, and Peru in an effort to supply

[77] Imports of asparagus from Peru under HTS 0709.20.10, which are limited to the period between Sept. 15 and Nov. 15, are GSP eligible; however, imports from Peru exceed the competitive-need limit.
[78] USITC, *Dataweb*.
[79] Ibid.
[80] Vance Publishing, "Peru Leads Growth in Asparagus," C2.
[81] Ibid.

asparagus to their customers year round.[82] Two major U.S. asparagus shippers merged into a new company in late 2003 to improve their ability to ship fresh asparagus year round by combining product from California, Mexico, and Peru.[83]

California asparagus acreage has declined, falling from a recent high of 40,900 acres in 2000 to 30,000 acres in 2005, a 27 percent decrease; acreage totaled 35,500 acres in 1991.[84] Despite this acreage reduction, California produced more asparagus in 2005 than it did in 1991; yields have increased from 2,800 pounds per acre to 3,600 pounds per acre, and production has increased from 93.8 million pounds to 104.4 million pounds.[85] In 1991, the California asparagus crop was valued at more than $73 million, and in 2005, it was valued at more than $119 million.[86] The competition for fresh California asparagus is not limited to fresh asparagus imports from Peru. From 2001 to 2005, 70 percent of fresh asparagus imports from Mexico entered from January through June in direct competition with most U.S. domestic producers.[87] By contrast, 81 percent of fresh asparagus imports from Peru entered the United States from July to December, when fresh domestic asparagus is generally not available.[88]

Peru's ability to ship fresh asparagus year round has provided positive benefits to U.S. consumers of fresh asparagus. U.S. consumption of fresh asparagus has increased as imports from Peru and Mexico have extended the season of availability to year round. The Peruvian Asparagus Importers Association (PAIA) directly attributes the near doubling of U.S. consumption, from 0.6 pounds per capita in 1995 to 1.1 pounds per capita in 2003, to the year-round availability associated with imports of fresh asparagus from Peru.[89]

Peru's ability to grow asparagus year round has also affected the U.S. market for processing asparagus. Asparagus produced in Michigan and Washington has been used primarily for processing. In 2003, Del Monte Foods moved its asparagus processing operations from its plant in Toppenish, Washington, to Peru.[90] Also around this time, Green Giant announced that it would also end asparagus processing at its Walla Walla, Washington, facility. Those asparagus processing operations were closed at the end of the 2005 growing season before the TPA negotiations were complete, leaving Washington growers to find other processing options or compete in the fresh market.[91] Even without the TPA, it is unlikely that processing capacity will return to Washington; Green Giant has stated that domestically canned asparagus is not a financially viable alternative to supplies of canned asparagus from Peru, China, or Mexico.[92]

As a result of losing processing capacity, the Washington asparagus industry has declined sharply in recent years. Washington State asparagus acreage has dropped from a peak of

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[82] Vance Publishing, "Imports Help Lift Yearly Sales," C7.
[83] Vance Publishing, "Alpine Deals To Increase Asparagus From Peru," A2.
[84] USDA, NASS, *QuickStats Database*.
[85] Ibid.
[86] Not adjusted for inflation; adjustment using the CPI for food and beverages suggests that 1991 production would have been equivalently valued at about $103 million in 2005.
[87] Ibid.
[88] USITC staff estimates from *Dataweb* data.
[89] USITC, hearing transcript, Mar. 15, 2006, 29–36.
[90] Egan, "War On Peruvian Drugs Takes a Victim: U.S. Asparagus."
[91] Milkovich, "Asparagus Growers Prepare for Processing Plant Loss."
[92] Shapiro, written submission.

approximately 32,000 acres in the late 1980s[93] to the current 12,000 acres. Washington growers expect to lose an additional 3,000 acres as processing asparagus acreage is eliminated from production; nonetheless, some Washington growers believe that prospects to supply the fresh market are good.[94] During 2003 to 2005, prices for fresh-market asparagus averaged $2,163 per ton versus $426 per ton for asparagus used for processing.[95] As a result, growers expect more supplies to enter the fresh market inducing lower prices and lost revenue. Furthermore, without access to processing capacity, growers also lose revenue from the sale of asparagus that does not meet fresh-market grading standards.

Peruvian asparagus production was estimated to be 196,000 MT in 2005 and is expected to increase to 200,00 MT in 2006.[96] Recent increases in production have been facilitated by replacement of older, less productive plants with new ones to improve yields.[97] Land tenure changes also facilitated continued growth in the Peruvian asparagus industry, which has averaged 5.4 percent annually since 1994. In the mid 1990s, small producers with low levels of production technology found themselves squeezed by an inability to access credit, high taxes on inputs, and increasing labor costs.[98] Land tenure reforms facilitated the consolidation of small holdings and attracted local as well as foreign investment into the Peruvian asparagus industry.[99] Despite lower prices and the belief by Peruvian exporters that the world asparagus market has matured, continued new investment and increased production[100] suggest that, under the TPA, Peruvian asparagus will continue to be highly competitive in the U.S. market relative to domestic production and imports from other sources, including fresh asparagus from Mexico and canned asparagus from China.

Views of Interested Parties

The Agricultural Technical Advisory Committee (ATAC) on Trade in Fruits and Vegetables does not believe that the duty-free treatment afforded to asparagus under ATPA should have been made immediately permanent in the TPA.[101] Rather, ATAC believes that the duties on Peruvian asparagus should be phased out slowly over time from MFN duty rates. A representative of the Michigan Asparagus Advisory Board states that the industry was disappointed but not surprised that asparagus imports from Peru will receive immediate duty-free treatment under the terms of the agreement.[102] This representative acknowledged that ATPA was not intended to negatively affect the U.S. asparagus industry; however it provided the Peruvian industry the opportunity to expand and become a year-round shipper of fresh asparagus, and then move into the processed sector in competition with domestic producers.[103] Despite the negative reaction from most producers, one industry source reported that the TPA would not cause any additional negative effect than was already done by ATPA.[104]

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[93] USDA, NASS, "Vegetables, Final Estimates 1987–1992."
[94] Milkovich, "Asparagus Growers Prepare for Processing Plant Loss."
[95] USDA, NASS, *Crop Values 2005 Summary.*
[96] USDA, FAS, "Peru Asparagus Annual 2005," 4.
[97] USDA, FAS, "Peru Asparagus Annual 2003," 3.
[98] USDA, FAS, "Peru Asparagus Annual 1995," 4.
[99] USDA, FAS, "Peru Asparagus Annual," various issues.
[100] USDA, FAS, "Peru Asparagus Annual 2005," 5.
[101] ATAC on Trade in Fruits and Vegetables, *Advisory Committee Report*.
[102] Lehnert, "No Relief Yet for U.S. Asparagus Producers."
[103] Ibid.
[104] Jackson, "Globalization Hits Michigan's Asparagus Industry."

The National Asparagus Council (NAC) believes that U.S. asparagus growers have been economically injured by the growth of the Peruvian asparagus industry as a result of ATPA duty-free access for fresh, chilled, and preserved asparagus.[105] U.S. asparagus planted acreage has fallen from 93,000 acres before ATPA to fewer than 53,000 acres today. Processors that used to can 55 million pounds of asparagus have left Washington State and moved to Peru. The NAC believes that this reduced U.S. asparagus acreage and the loss of U.S. asparagus processing capacity to Peru has resulted in lost income for U.S. asparagus growers and lost jobs in rural communities in California, Washington, and Michigan.

PAIA strongly supports the TPA, believing it will provide tangible and significant economic benefits for both the United States and Peru.[106] PAIA believes that the TPA will continue to provide economic benefits to U.S. consumers, U.S. importing companies, U.S. distributors, and other companies involved in the distribution of fresh asparagus in the United States. Furthermore, PAIA states that, without the TPA, the loss of duty-free treatment associated with the possible expiration of ATPA would have resulted in discernable economic harm to these parties. Furthermore, a PAIA representative estimates that imports of Peruvian fresh asparagus directly and indirectly generate 5,000 jobs in the United States. Moreover, of the $300 million of revenue generated by fresh asparagus imports from Peru in 2003, PAIA estimates that 70 percent, or $210 million, accrued to U.S. companies. PAIA also believes that imports of fresh Peruvian asparagus are largely countercyclical to U.S. production, and benefit U.S. consumers by providing year-round availability.

The Peruvian Asparagus and Vegetables Institute (IPEH) supports the TPA and believes that it will continue to provide substantial economic benefits to both Peru and the United States.[107] The IPEH represents growers and exporters that accounted for $183 million of U.S. imports of asparagus, artichokes, chile peppers, paprika, and pimientos in 2005. The IPEH states that the Peruvian asparagus industry, which accounted for 71 percent of these U.S. imports in 2005, has grown into a mature industry that achieved the objectives of ATPA, and spurred economic development as an alternative to the production of illegal narcotics. The IPEH members believe the production and export of artichokes and paprika, which are expected to account for total world exports of more than $165 million in 2006, to further contribute to economic development and provide alternatives to the production of illegal narcotics. The IPEH believes that the TPA will expand and increase these benefits.

General Mills, the owner of Green Giant vegetables, states that the TPA will provide long-term economic benefits to consumers, manufacturers, and producers in both the United States and Peru, particularly with respect to trade in prepared and preserved asparagus.[108] Green Giant stated that, to provide the best-valued product to consumers, the company began sourcing canned asparagus from Peru in June 2005. Green Giant states that it is unable to supply canned asparagus from U.S. sources in a financially viable manner. Furthermore, even if Peruvian canned asparagus were not afforded continued duty-free treatment under the TPA, Green Giant states that it would not source canned asparagus from domestic sources, but would consider Mexico or China as viable alternatives.

[105] Bakker, written submission.
[106] USITC, hearing transcript, Mar. 15, 2006, 29–36.
[107] Paz-Soldan on behalf of the Peruvian Asparagus and Vegetables Institute, written submission.
[108] General Mills, written submission.

Meat[109]

Assessment

The provisions of the U.S.-Peru TPA will likely have a significant, positive effect on total U.S. exports of beef and pork to Peru. However, increased exports may not have a significant effect on the total U.S. industry because of the relatively small size of the Peruvian market. Peru is currently a large importer of beef variety meats, and the TPA will give U.S. exporters of directly competing products a competitive advantage over other suppliers in the Peruvian market, primarily Mercosur countries.[110] USDA prime and choice beef, which tends not to compete directly with local production and imports from the region,[111] will receive immediate duty-free treatment, while beef other than USDA prime and choice will receive duty-free treatment within an 800 MT TRQ, with all duties to be phased out within 12 years. U.S. pork and pork variety meat exports are likely to increase because the TPA will enhance the competitiveness of pork vis-à-vis other domestic protein sources (primarily fish and poultry), as well as pork imports from Chile that currently receive duty-free treatment. Furthermore, U.S. beef and pork exports will benefit from an exchange of letters that address outstanding SPS issues have limited U.S. meat exports in the past. This analysis is generally consistent with the economy-wide simulation results that show significant increases in Peruvian imports of U.S. bovine and other meat products, and small changes in the volume of U.S. imports of Peruvian meat products.

The provisions of the U.S.-Peru TPA are unlikely to cause an increase in U.S. beef and pork imports from Peru, because the Peruvian beef and pork industries primarily consist of small and indigenous producers that produce for household and local consumption.[112] Furthermore, Peru does not currently have any slaughter or processing facilities that are eligible to export meat to the United States.[113] Therefore, it is unlikely that the TPA will have a significant, negative effect on U.S. cattle and beef producers or U.S. swine and pork producers.

Provisions of the TPA include a TRQ for beef variety meats[114] that provide U.S. suppliers with up to 10,000 MT of immediate duty-free access, thereafter growing at the rate of 6 percent annually until all imports of the identified products are duty free by year 10 of the agreement.[115] Peruvian imports of beef variety meats averaged 19,268 MT, valued at more than $15 million from 2001 to 2005.[116] The United States supplied less than 5 percent of this total. Furthermore, U.S. suppliers shipped nothing in 2004 and 2005 because of an import

[109] This section primarily covers beef, beef variety meats, pork, and pork variety meats classified in chaps. 2, 5, and 16 of the HTS.

[110] This group includes Argentina, Brazil, Paraguay, and Uruguay.

[111] U.S. prime and choice beef is typically produced from young animals fed a high energy ration, i.e., grain-fed beef; local and regional production tends to be produced from animals of varying ages fed primarily forages, i.e., grass-fed beef.

[112] Sallyards, informal written industry description – Beef, Pork, Bovine Offal.

[113] USDA, FSIS, "Import Information."

[114] This TRQ covers items classified under Peru HTS items 0206.21.00, 0206.22.00, 0206.29.00, and 0504.00.10, and includes items such as livers, hearts, tongues, and tripe.

[115] *U.S.-Peru TPA*.

[116] *Global Trade Atlas*. This total includes Peru HTS items imported under subheadings 0202.21, 0206.22, 0206.29, and heading 0504. Under heading 0504, item 0504.00.10 accounted for more than 99 percent of imports; this item may include items from all species though, according to industry sources, imports are primarily bovine items. The beef variety meat TRQ includes items classified under HTS subheadings 0202.21, 0206.22, 0206.29, and 0504.00.10.

ban related to bovine spongiform encephalopathy (BSE).[117] The primary suppliers of these products to the Peruvian market are the Mercosur countries. These countries have preferential trade agreements with Peru; however, duties on most of these items for Mercosur countries will not be completely phased out until 2014 or 2016.[118] Until that time, U.S. suppliers will enjoy preferential access to the highly price sensitive Peruvian beef variety meat market. The United States should be able to be price competitive in the variety meat market because, if not exported, these items have very low U.S. domestic demand for consumption, and have much lower values in alternative domestic uses such as pet food.

The provisions of the TPA provide U.S. suppliers with immediate duty-free access for beef that is graded USDA prime or choice. The TPA also provides U.S. suppliers with a TRQ that provides immediate duty-free access for up to 800 MT of beef that does not grade prime or choice, growing at 6 percent annually, until all imports of these products are duty free by year 12 of the agreement.[119] Peruvian imports of beef averaged 3,750 MT valued at $8 million from 2001 to 2005; the U.S. share of this market was only approximately 1 percent, and no imports came from the United States in 2004 and 2005 because of the BSE ban.[120] Peru's primary suppliers are the Mercosur countries. Peru's trade agreements with these countries do not completely phase out tariffs on beef until 2019,[121] meaning that U.S. suppliers will have preferential access relative to Mercosur suppliers to the Peruvian market for beef.

The degree to which U.S. beef, which is primarily grain fed, and Mercosur beef, which is primarily grass fed, will compete in the Peruvian market depends on tastes, preferences, and price. Historically, Peruvian consumers have had limited access to U.S. grain-fed beef, but are familiar with grass-fed beef from local production and imports, which have been dominated by the Mercosur countries. U.S. beef exports graded USDA prime and choice are likely to be initially targeted at the hotel and restaurant segment, as well as the high-end retail segment.[122] Although this initially creates a market that may depend on tourist trade, it is also expected to create a market opening among upper- and middle-income Peruvian consumers, creating local demand for grain-fed beef that is expected to expand as local incomes increase. The TPA affords U.S. beef the ability to be price competitive with comparable cuts of beef from Mercosur countries while a local market for grain-fed beef is developed.

The provisions of the TPA provide U.S. pork with duty-free access for most muscle cuts and variety meat items by year 5 of the agreement, with duty-free treatment for all pork items by year 10, putting U.S. pork in a better competitive position in this growing market. Peruvians have not historically been large pork consumers; per capita consumption of pork is about

[117] Upon discovery of a BSE-infected cow in the U.S. cattle herd in Dec. 2003, 72 of 133 countries that had imported U.S. beef during 2003 banned imports of U.S. beef and beef variety meats. Most of these countries have since reopened their markets to U.S. beef, though access may be limited, typically to boneless beef from animals fewer than 30 months of age. As of Feb. 17, 2006, 27 countries, including Peru, were still closed to U.S. beef and beef variety meats. The Letter Exchange on SPS/TBT Issues for U.S.-Peru TPA set as Mar. 1, 2006, the date by which Peru would permit imports of U.S. beef and beef products accompanied by an FSIS Export Certificate of Wholesomeness. As of this writing, the Peruvian market had not been opened to U.S. beef shipments.

[118] ALADI, *Acuerdo de Complementación Económica*.

[119] The beef TRQ includes items classified under HTS items 0201.30.00, 0202.20.00, and 0202.30.00 not graded USDA prime or choice.

[120] *Global Trade Atlas*.

[121] ALADI, *Acuerdo de Complementación Económica*.

[122] USMEF, "USMEF Strategic Market Profile."

2.6 kg (5.7 pounds) annually, compared with 20.7 kg (45.5 pounds) of fish and seafood and 13.0 kg (28.6 pounds) of chicken.[123] Low consumption has been attributed to Peruvian perception of pork as a less healthy alternative to fish or chicken and the conditions under which most animals are raised (backyard production).[124] Though imports of pork products have been small, they are increasing. The value of fresh, chilled, and frozen pork imports has increased from less than $2,000 in 2001 to more than $1 million in 2005. Imports of processed pork items increased in value from approximately $80,000 to nearly $240,000 from 2001 to 2005; and imports of pork variety meats increased in value from approximately $72,000 in 2001 to nearly $257,000 in 2005. Most of this increase, however, benefited Chilean pork producers. Chile was the only supplier of fresh, chilled, and frozen pork and pork variety meats in 2004 and 2005. This predominance can be attributed to an FTA reached between Chile and Peru in 1998 that now provides Chile with duty-free access for most pork and pork variety meats.

Peru's commitments with respect to sanitary issues[125] are also likely to enhance the market access of U.S. beef and pork exports. In an exchange of letters in connection with the TPA, the Peruvian government has committed (1) to continue to recognize the U.S. meat and poultry inspection system as equivalent to Peru's inspection system and not require individual plant approval; (2) to continue to accept meat and poultry shipments accompanied by USDA Food Safety and Inspection Service (FSIS) Certificates of Wholesomeness; (3) to recognize FSIS certification statements as meeting import requirements for pork and pork products, and poultry and poultry products; and (4) to recognize that U.S. measures regarding BSE meet World Organization of Animal Health (also known as OIE) guidelines and to complete the verification process that will allow resumption of U.S. beef imports. Furthermore, these provisions should enhance future market access for U.S. beef and pork exports by assuring exporters and importers that sound scientific principles for food safety and wholesomeness will be transparently applied to U.S. beef and pork exports.

Views of Interested Parties

The ATAC for Trade in Animals and Animal products praises the U.S.-Peru TPA as an excellent example of the type of agreement that is in the best interest of the United States because it expands trading opportunities to the benefit of U.S. agriculture.[126] Nonetheless, the ATAC is disappointed with the 12-year phase-out on over-quota duties on beef not grading USDA prime or choice. Despite immediate duty-free access for all USDA prime and choice beef, 10,000 MT of beef variety meats, and 800 MT of beef not grading USDA prime or choice, and the 5-year phase-out of most duties on pork and pork variety meats, the ATAC believes that failure to secure the same preferential duties that Peru provides to parties subject to agreements concluded before December 7, 2005—this would appear to be directed at Peru's preferential trade agreements with Chile and the Mercosur countries—disadvantages U.S. livestock industries vis-à-vis these parties.

The National Cattlemen's Beef Association (NCBA) views the U.S.-Peru TPA as a great opportunity for the U.S. cattle and beef industry. The NCBA indicates that Peruvian beef consumers are very price sensitive and that immediate elimination of the 25 percent duty will allow U.S. suppliers to provide products at a lower price. This advantage is very important

[123] FAOSTAT data.
[124] Sallyards, informal written industry description – Beef, Pork, Bovine Offal.
[125] See chap. 5 of this report for a discussion of the TPA's SPS chapter.
[126] ATAC for Trade in Animals and Animal Products, *Advisory Committee Report*.

to both Peruvian consumers and U.S. producers. The NCBA also believes that the TPA sets a critical precedent for future FTA negotiations.[127]

The Ranchers-Cattlemen Action Legal Fund, United Stockgrowers of America (R-CALF USA, hereafter R-CALF), states that it assesses each FTA on a case-by-case basis subject to four criteria: (1) reduction of global market distortions, such as high tariffs; (2) application of a born, raised, and slaughtered beef rule of origin; (3) creation of special safeguards to protect against import surges and excess price volatility; and (4) upward harmonization of health and safety standards. On the basis of these criteria, R-CALF has concerns about the U.S.-Peru TPA. Specifically, R-CALF points out that the TPA does not include a special safeguard, nor does it apply a born, raised, and slaughtered beef rule of origin, which will allow beef from Argentinian and Brazilian cattle that is shipped to Peru to qualify for preferential access to the U.S. market.[128]

The National Pork Producers Council (NPPC) expresses strong support for the U.S.-Peru TPA. Analysis conducted for the NPPC found that the agreement, when fully implemented, will be extremely beneficial to U.S. pork producers; U.S. pork exports to Peru will increase U.S. hog prices by 83 cents per head, and producer profits by 7 percent.[129]

Textiles and Apparel

Assessment

Tariff liberalization under the U.S.-Peru TPA will likely result in a small increase in U.S. imports of textiles and apparel from Peru. The textile and apparel sector in Peru is an important sector, but is comparatively small, even though it is integrated from the production of raw materials (mainly cotton) to the manufacture of intermediate goods (yarn and fabric) and finished goods (mainly apparel).[130] Because almost all imports of such goods from Peru already enter free of duty under ATPA (96 percent in 2005) and because the rules of origin under the TPA for apparel are similar to those under ATPA, the principal benefit of the TPA is to make the trade preferences permanent and reciprocal. ATPA benefits have enabled Peru to expand its shipments of textiles and apparel to the United States by 108 percent since 2002, to $821 million in 2005.[131] The TPA can further boost U.S. apparel imports from Peru to the extent that it spurs foreign investment in Peru's textile and apparel sector[132] to increase its capacity and its competitiveness in the face of greater competition in the U.S. market from lower-cost exporting countries[133] following the elimination of U.S. import quotas on textiles

[127] NCBA, "Peru to Lower Beef Tariffs."

[128] R-CALF, *2006 Position Paper: International Trade in Cattle and Beef.*

[129] NPPC, "NPPC to Champion U.S.-Peru Trade Agreement."

[130] The textile and apparel sector is a leading source of economic activity in Peru, representing approximately 10 percent of the country's exports and reportedly accounting for 14 percent of industrial production and directly employing 150,000 workers. Italo Acha, counselor, Embassy of Peru, e-mail message to Commission staff, Mar. 23, 2006; and Paz-Soldan on behalf of Exporamerica, written submission.

[131] Import data are from the U.S. Department of Commerce, Office of Textiles and Apparel (OTEXA).

[132] The "relatively short life span" of ATPA preferences for apparel has reportedly deterred foreign investment in Peru's textile and apparel sector. U.S. Department of State, "USITC 2004 Annual Andean Investment and Drug Crop Survey."

[133] A trade report stated that production costs in Peru are estimated to be as much as 50 percent higher than those in China. "Peru Textile Trade."

and apparel in 2005.[134] The results of the economy-wide analysis indicate that tariff liberalization will result primarily in a small increase in U.S. imports of apparel from Peru, which accounted for 97 percent (or $800 million) of U.S. textile and apparel imports from Peru in 2005. Although Peru supplied just 1 percent of total U.S. apparel imports in 2005, it was the fifth-largest source of knit cotton shirts and blouses, with shipments of $644 million and a 5 percent import market share. The expected increase in apparel imports from Peru will likely displace U.S. apparel imports from other countries, rather than domestic production, which generally consists of time-sensitive and niche market goods.

The expected increase in U.S. apparel imports from Peru under the TPA will likely not change appreciably if ATPA preferences for the other three Andean countries (Bolivia, Colombia, and Ecuador) are extended beyond their current expiration date of December 31, 2006.[135] If ATPA preferences expire, the expected increase in U.S. apparel imports from Peru under the TPA also will likely not change appreciably in the short or long term, because U.S. textile and apparel imports from Bolivia ($37 million in 2005), Colombia ($618 million), and Ecuador ($19 million) are small. Although Colombia was the second-leading Andean supplier of textiles and apparel to the United States after Peru, with 41 percent of total Andean shipments in 2005, the import product mix differs between Colombia and Peru. Cotton trousers and wool trousers, suits, and sport coats accounted for 37 percent and 14 percent, respectively, of total U.S. textile and apparel imports from Colombia in 2005, while cotton knit shirts and blouses accounted for 78 percent of U.S. textile and apparel imports from Peru. In the long term, the growth in U.S. apparel trade with Peru will likely be moderated by the expected growth in imports from lower-cost exporting countries previously constrained by U.S. import quotas, particularly China, whose shipments of knit shirts, blouses, and other textile and apparel articles are now subject to U.S. safeguards through 2008.[136]

Although the results of the economy-wide analysis indicate that tariff liberalization under the TPA will likely result in a small value, but large percentage, increase in U.S. exports of textiles and apparel to Peru, this potential effect is unlikely largely because most U.S. exports of textiles to Peru are believed to be already eligible for duty savings in the form of duty drawback, a factor not accounted for in the economy-wide model, and local demand for U.S. apparel is limited by income.[137] U.S. exports of textiles and apparel to Peru are small ($21 million in 2005) and likely consist mostly of inputs (yarns, fabrics, and garment parts) used in the production of apparel for export to the United States. In addition, the low level of per capita income in Peru will likely dampen Peruvian demand for U.S. exports of finished goods, which tend to be more costly than the locally-produced apparel products.

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[134] The WTO Agreement on Textiles and Clothing (ATC) obligated the United States, the EU, and Canada to phase out their import quotas on textiles and apparel from WTO member countries over 10 years ending on Jan. 1, 2005. The United States did not maintain import quotas under the ATC on such goods from Peru.

[135] U.S. imports of textiles and apparel from Colombia, Bolivia, and Ecuador totaled $674 million, or less than 1 percent of total U.S. imports of such goods in 2005.

[136] U.S. imports of knit cotton shirts and blouses from China in 2005 increased 194 percent over the 2004 level to $636 million. Imports of these and certain other textile and apparel articles from China are now subject to safeguards (or quotas), as provided for under the terms of China's Protocol of Accession to the WTO, through 2008. U.S. imports of textiles and apparel from China totaled more than $22.4 billion, or 25 percent of total U.S. textile and apparel imports in 2005.

[137] Duty drawback is a refund of duties paid on inputs imported into a country and incorporated into goods for export. Peru's imports of U.S. materials are currently eligible for duty drawback upon exportation of the finished goods from Peru to the United States. Although duty drawback and rules of origin requirements are important in estimating the potential effect of the TPA on U.S. bilateral textile and apparel trade with Peru, they are not comprehensively incorporated into the CGE model (GTAP), resulting in a possible overestimation of the marginal tariff effects in this sector by the model.

Views of Interested Parties

U.S. textile firms[138] generally support the rules of origin for textiles and apparel under the TPA because the rules "will ensure [that] the benefits of the agreement flow mainly to the signatory parties" and that the yarn-forward rule will advance regional integration goals. They support the requirement in the TPA that pocketing fabrics be made and finished in the parties, as well as the exclusion from the TPA of certain provisions found in other U.S. FTAs that permit the use of third-country inputs such as cumulation provisions, TPLs, and a single-transformation rule. By contrast, U.S. apparel firms that source and market globally generally oppose the yarn-forward rule of origin; they state that this origin rule will be burdensome to administer and, in turn, prevent expansion of trade and investment in textiles and apparel. The apparel firms oppose the exclusion of TPLs, cumulation provisions, and a single-transformation rule from the TPA, stating that it will limit the built-in flexibility of CAFTA-DR. The apparel firms also oppose the added requirements that sewing thread, elastomeric yarns, certain narrow fabrics, and pocketing fabrics be made in the TPA region. Textile and apparel firms support the expedited "commercial availability" process under the TPA, although some apparel firms support the inclusion of more apparel inputs on the initial short-supply list. The apparel firms also support the continuation of the existing customs duty drawback program under the TPA that provides important cost savings.

U.S. retailers and distributors of textile and apparel goods[139] oppose the TPA rules of origin for textiles and apparel, stating that the yarn-forward rule is not commercially viable because it is overly restrictive and fails to reflect the realities of global production and sourcing. They state that the yarn-forward rule imposes a value-added requirement that is higher for apparel than for other goods and that the absence of certain exceptions to the yarn-forward rule, such as TPLs and cumulation provisions, will limit production flexibility, increase costs for apparel producers in Peru, and prevent the integration of hemispheric-wide production. The retailers and distributors state that, although Peru has an integrated textile and apparel sector producing fibers, yarns, fabrics, and apparel, the Peruvian sector is comparatively small and unable to compete effectively with "full-package" suppliers in China. The retailers and distributors state that the TPA short-supply provisions are unclear and provide insufficient product coverage. They support provisions in the TPA that will grant immediate duty-free treatment to originating textile and apparel articles and permit the use of third-country inputs (the de minimis foreign content rule). The retailers and distributors also support the continued use of duty drawback following implementation of the TPA.

The American Apparel & Footwear Association (AAFA) stated that it is "extremely disappointed that the U.S./Peru TPA contains very restrictive and, in many cases, unworkable rules of origin for apparel and textiles. Because of the agreement's apparel and textile provisions, we believe the U.S./Peru Trade Promotion Agreement represents a missed opportunity to preserve and expand the region's apparel and textile industries."[140] The AAFA adds that it prefers provisions similar to those in CAFTA-DR, and would have preferred to see the inclusion of features such as cumulation, a larger short-supply list, single transformation for key products, and a yarn-forward rule on essential character.

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[138] ITAC 13, *The U.S./Peru Trade Promotion Agreement*.

[139] The industry views expressed in this paragraph are from ITAC 5, *The U.S./Peru Trade Promotion Agreement*.

[140] Burke, written submission.

Peruvian apparel exporters support the TPA, stating that it builds on the benefits of ATPA. They assert that the TPA will strengthen and expand the strategic alliance between Peru and the United States, thereby enabling both countries to compete more effectively against Chinese and other Asian suppliers.[141] Peruvian apparel exporters note that the TPA will benefit both Peru and United States by boosting U.S. exports of cotton, yarn, and fabrics to Peru and increasing Peru's exports of price-competitive apparel to the United States.

Leather Goods and Footwear[142]

Assessment

Tariff liberalization under the U.S.-Peru TPA for leather goods and footwear (including leather and leather articles as well as footwear, travel goods,[143] and other products characteristic of the leather trade but also made from materials such as textiles and plastics) will likely result in an increase in U.S. leather goods trade with Peru that is small in absolute value but large in percentage terms. Under the TPA, tariff liberalization, coupled with flexible rules of origin, can spur foreign producers to assemble certain leather goods in Peru from nonoriginating materials and export the goods to the United States for sale in niche market segments. However, despite the TPA, the leather goods sector in Peru reportedly lacks the economies of scale necessary to compete in the U.S. market with China, which supplied 69 percent, or $17.5 billion, of total U.S. imports of leather goods in 2005.[144]

The results of the economy-wide analysis indicate that tariff liberalization for leather goods will result in estimated increases of approximately $1 million (33 percent) in U.S. imports from Peru and $3 million (164 percent) in U.S. exports to Peru, and that these increases will likely have almost no effect on total U.S. trade or domestic production of leather goods.[145] The modeling results reflect the current small volume of U.S. leather goods trade with Peru (U.S. imports and U.S. exports each totaled less than $2 million in 2005);[146] the large share of U.S. leather goods imports from Peru already eligible for duty-free entry (75 percent in 2005); the domination of the U.S. footwear market by China and other, mostly Asian suppliers (import market share was 98 percent in 2004);[147] and the low level of per capita income in Peru, which dampens Peruvian demand for U.S. leather goods.

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[141] Paz-Soldan on behalf of Exporamerica, written submission.

[142] This product grouping covers leather and composition leather (HTS headings 4102-4115); saddlery and harness (4201); luggage, handbags, and similar goods (4202); articles of leather or composition leather used in machinery or mechanical appliances or for other technical uses (4204); other articles, except apparel, of leather or composition leather (4205); footwear and footwear parts (HTS chap. 64); watch straps of non-metallic materials (HTS subheading 9113.90); and personal travel sets (9605.00).

[143] Travel goods include luggage, brief cases, computer cases, handbags, purses, duffle bags, wallets, and related goods.

[144] Peru's exports of leather goods totaled $33 million in 2005 and consisted mostly of leather ($18 million) and footwear and travel goods ($14 million), according to data from Global Trade Atlas. Peru's exports of footwear are expected to grow 20–25 percent in 2006. *Latin America News Digest*, "Peru Forecasts up to 25 Pct Y/Y Rise."

[145] The modeling results apply to leather goods, whether or not ATPA preferences for the other Andean nations (Bolivia, Colombia, and Ecuador) are extended beyond their current expiration date of Dec. 31, 2006. U.S. leather goods imports from all four Andean nations totaled $46 million, or 0.2 percent of total U.S. imports of such goods in 2005.

[146] In 2005, total U.S. imports and total U.S. exports of leather goods were $25.2 billion and $2.7 billion, respectively.

[147] USTR, hearing transcript, 54–63; and Lamar, written submission.

The TPA will grant immediate duty-free market access for tariff lines covering almost all leather goods currently traded between the United States and Peru, with tariffs on all the remaining leather goods phased out within 10 years.[148] The only U.S. tariff lines subject to 10-year staging are the 17 lines covering "sensitive" rubber footwear; the NTR duty rates for such footwear range from 20 percent ad valorem to 55 percent AVE, based on 2005 trade.[149] Peru will phase out its uniform ad valorem tariff of 20 percent on rubber footwear and 12 percent on most tanned leather over 10 years, and its 12 percent tariff on personal travel sets over 5 years.[150] The rule of origin under the TPA for the 17 sensitive footwear articles will be similar to that under NAFTA, requiring a qualifying good to have a regional value content of not less than 55 percent of the appraised value of the article, which effectively restricts the use of nonoriginating uppers because of the high labor content associated with stitching. The TPA will apply a more flexible "substantial transformation" rule of origin to all other footwear, permitting the use of nonoriginating uppers and other materials in qualifying goods, subject to a 20 percent local value-added content requirement. The substantial-transformation rule will also apply to travel goods except those of textiles. Textile travel goods will be subject to a "fabric-forward" rule that requires qualifying goods to be made of originating fabrics.

Views of Interested Parties

U.S. footwear companies that source and market footwear globally generally support the U.S.-Peru TPA because footwear, other than the 17 sensitive rubber footwear articles, will receive immediate duty-free market access and a flexible rule of origin (albeit with a 20 percent local value-added content requirement).[151] U.S. producers of the 17 sensitive rubber footwear articles state that these goods were excluded from duty-free treatment under ATPA and should be excluded from any FTA with the Andean countries because duty-free treatment for such footwear made in the Andean region will pose a serious threat to the domestic industry.[152] The Travel Goods Association (TGA) does not support the U.S.-Peru TPA. TGA states that the TPA has highly restrictive provisions on textile travel goods that prevent U.S. travel goods companies from using the best available inputs.[153] Certain U.S. travel goods industry representatives support the TPA provisions for nontextile travel goods, but oppose the fabric-forward rule of origin for textile travel goods, stating that this rule is "so restrictive that it effectively renders the [TPA] useless" for the industry.[154] These representatives state that all travel goods (both textile and nontextile) should become duty free immediately under simple and flexible rules of origin. U.S. footwear retailers and distributors state that they support immediate tariff elimination and liberal rules of origin for all footwear under a U.S.-Andean FTA, and that the Andean region lacks the footwear

[148] The "baseline" trade-weighted average ad valorem tariff used in the Commission modeling for leather goods was 2.8 percent for U.S. imports from Peru and 16.6 percent for Peru's imports from the United States.

[149] There were no U.S. imports from Peru in 2005 under the 17 tariff lines, which cover rubber or plastic protective footwear and certain athletic and other footwear with rubber or plastic soles and fabric uppers (HTS items 6401.10.00, 6401.91.00, 6401.92.90, 6401.99.30, 6401.99.60, 6401.99.90, 6402.30.50, 6402.30.70, 6402.30.80, 6402.91.50, 6402.91.80, 6402.91.90, 6402.99.20, 6402.99.80, 6402.99.90, 6404.11.90, and 6404.19.20).

[150] Peru maintains a uniform MFN ad valorem tariff of 12 percent for all leather goods except footwear (subject to a uniform rate of 20 percent) and leather articles used in machinery or mechanical appliances or for other technical uses (4 percent).

[151] ITAC 13, *The U.S./Peru Trade Promotion Agreement*.

[152] Cooper, written submission.

[153] Pittenger, written submission.

[154] ITAC 13, *The U.S./Peru Trade Promotion Agreement*.

production capacity to affect the U.S. footwear market in any meaningful way.[155] Finally, the American Apparel & Footwear Association (AAFA) generally supports the TPA's provisions for footwear, stating that the provisions "will ensure that the growth in footwear trade between the United States and Peru started under the current Andean Trade Promotion & Drug Eradication Act (ATPDEA) will continue."[156] The AAFA notes, however, that it had hoped "for an even more liberal rule of origin for non-import-sensitive footwear articles along the lines of what was negotiated in [CAFTA-DR]."[157]

Pharmaceuticals

Assessment

The U.S.-Peru TPA is expected to have a positive effect on U.S. pharmaceutical exports to Peru. Pharmaceutical exports will benefit from the liberalization of government procurement in Peru, which currently gives preferential treatment to local manufacturers.[158] Stronger intellectual property laws, specifically those related to patent protection and confidential test data, should also assist U.S. suppliers in expanding exports to Peru.[159] Demand for health care in Peru is expected to rise as life expectancy and urbanization increase, further increasing possible long-term market opportunities for U.S. suppliers.[160] This analysis is not comparable to the economy-wide simulation results because pharmaceuticals trade makes up a very small portion of the GTAP chemical, rubber, and plastic products sector.

The TPA offers significant immediate duty reductions for U.S. pharmaceutical exports. Peruvian imports of all pharmaceuticals are taxed at 12 percent ad valorem. Of the 69 headings or subheadings in the Peruvian schedule for pharmaceutical products (chapter 30), 53 become duty free immediately with the enactment of the TPA, 15 become duty free after 5 years, and 1 heading (waste pharmaceuticals) becomes duty free after 10 years. The 16 items that do not immediately become duty free accounted for 18.7 percent of U.S. exports to Peru in 2005.[161]

The United States is one of the top suppliers of pharmaceuticals to Peru, exporting $14 million in 2005. Imports accounted for approximately 40 percent of the Peruvian market for pharmaceuticals; U.S. exports represent approximately 9 percent of Peruvian imports.[162] The largest U.S. exports of pharmaceuticals to Peru in 2005 were medicaments in measured doses ($6 million), vaccines for veterinary medicine ($4 million), and adhesive dressings ($1 million). The Peruvian market for pharmaceuticals was $544 million in 2004 and is expected to grow by 4 percent annually for the next few years, expanding long-term opportunities for U.S. suppliers.[163]

[155] USTR, hearing transcript, 54–63.
[156] Burke, written submission.
[157] Ibid.
[158] US&FCS and U.S. Department of State, "Drugs and Pharmaceuticals," 7.
[159] PhRMA, "Special 301 Submission: Peru," 251.
[160] EIU, *Industry Briefing, Peru: Healthcare and Pharmaceuticals Background*.
[161] *Global Trade Atlas*.
[162] US&FCS and U.S. Department of State, "Drugs and Pharmaceuticals," 7.
[163] Ibid., 2.

Views of Interested Parties

In general, the U.S. pharmaceutical industry favors the Peru TPA and supports "immediate tariff elimination in accordance with the multilateral understanding on elimination of pharmaceutical tariffs."[164] Industry representatives are pleased that all of the tariff lines eventually go to zero, but expressed disappointment with the number of lines in this sector subject to staged reduction of tariff rates.[165] A prominent industry group indicates that the TPA will increase legal certainty for U.S. companies and help create "an environment that helps to encourage the launch of new medicines."[166] Industry representatives are encouraged by the obligations to improve intellectual property protection. However, the industry notes the absence of explicit obligations for the protection of second-use patents and new clinical information, and restrictions on compulsory licensing, parallel imports, and pre-grant opposition.[167]

[164] ITAC 3, *The U.S.-Peru Trade Promotion Agreement*, 4.
[165] Ibid., 3.
[166] PhRMA, "PhRMA Welcomes Peru Free Trade Agreement."
[167] ITAC 15, *Report on the U.S.-Peru Trade Promotion Agreement*, 16.