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CENTRAL AMERICA: Trump may trigger trade opportunities

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Abstract

Outlook for Central American trade.

The election of Donald Trump as the next US president has created uncertainty over the outlook for trade in Central America. However, the region is open to international trade, and a recent trade deal with South Korea illustrates its attractions as a partner.

Full Text

SUBJECT:Outlook for Central American trade.

SIGNIFICANCE:The election of Donald Trump as the next US president has created uncertainty over the outlook for trade in Central America. However, the region is open to international trade, and a recent trade deal with South Korea illustrates its attractions as a partner.

ANALYSIS: Impacts.

The trade accord with South Korea is likely to come into force over the coming year.

Increased US protectionism would be felt in Central America.

Other Asian countries could show growing interest in negotiating trade deals with Central American countries.

For well over a decade, Central America has had open trading relationships with the rest of the world. This includes Nicaragua, whose left-of-centre government has been relatively pragmatic on the issue, despite periodic rhetorical hostility.

Two multilateral deals are key to the region's international trade relationships:

DR-CAFTA. The Dominican Republic-Central America Free Trade Agreement (DR-CAFTA) took effect in January 2009 and encompasses the United States, the Dominican Republic, Costa Rica, Nicaragua, El Salvador, Honduras and Guatemala. (Panama has a bilateral trade deal with the United States, which took effect in October 2012.) The deal has eliminated tariffs on consumer and industrial goods, with nearly all agricultural tariffs being phased out by 2020.

EU. The EU and Central America finalised an Association Agreement, which was signed in June 2012 and has three pillars -- political dialogue, cooperation and trade. The trade pillar came into force in 2013. Following a phase-out period, it will end tariffs on manufactured goods and fisheries, and eliminate most tariffs on agricultural products, except for 'sensitive areas' for local markets.

In addition, a bilateral free trade agreement (FTA) between China and Costa Rica took effect in August 2011. This eliminates tariffs on more than 90% of bilateral trade over 15 years, and opens a large number of Costa Rican service sectors to Chinese direct investment.

South Korea FTA.

Central America's latest bilateral trade deal is with South Korea. Seoul recently concluded talks with six Central American countries at a trade ministers' meeting in Managua. South Korea's exports to the region were worth 4.1 billion dollars in 2015, while imports from them were worth 784 million dollars.

The FTA aims to eliminate 95% of tariffs over ten years. Each country has negotiated a list of goods that the FTA will cover, as well the timing of import duty reductions. Following legal scrutiny and formal signature, it must be ratified by each country's legislature.

Key exports from all countries are part of the FTA, including cars, steel, cosmetics, pharmaceuticals and household goods on the South Korean side, and coffee, sugar and tropical fruits on the Central American side. The South Korean government was forced to make concessions on the agricultural exclusions that it was seeking, though tariff-free access will be phased in for several goods, such as bananas, pineapples and pork. Nonetheless, certain key South Korean crops will not be included, notably rice.

There are already signs that the deal will be controversial in Central America:

Guatemala's manufacturing chamber of commerce warned that it could lead to job losses and bankruptcies as a result of competition from South Korean imports, particularly among metal working and footwear manufacturers.

Costa Rican agricultural sector representatives expressed disappointment at their exports not receiving immediate tariff-free access.

Despite these objections, there will be significant political pressure for ratification during 2017. Indeed, this is extremely likely. However, there is some risk of Costa Rican opposition parties seeking to obstruct the FTA because of concern about delays in tariff-free agricultural access.

Trump uncertainty.

Trump's election has injected uncertainty throughout Latin America (*see LATIN AMERICA: US election will roil*

regional outlook - November 21, 2016). In his campaign, Trump repeatedly pledged to renegotiate, or even withdraw, from the North American Free Trade Agreement (NAFTA). He also pledged to impose a 35% tariff on imports from companies that move jobs abroad, which particularly would target Mexico.

After Trump reiterated his border tax warning in a tweet criticising General Motors for manufacturing cars in Mexico for the US market, on January 3, Ford announced that it would cancel plans for a 1.6-billion-dollar plant in Mexico and instead expand its Michigan operations. The move was described as motivated at least in part by a "vote of confidence" in Trump's policies.

Trump's transition team has already sought to manage down expectations over NAFTA, talking about unspecified adjustments and modifications. Moreover, the 35% tariff would require congressional approval, and there have already been signals, for example from House Majority Leader Kevin McCarthy, that the legislature might not support such a move.

While Central America has not been an explicit focus of his campaign, the Northern Triangle countries -- Guatemala, Honduras and El Salvador -- may well bear the brunt of any moves to deport undocumented migrants with criminal records (*see CENTRAL AMERICA/US: Washington will toughen policy - October 21, 2016*). This would potentially exacerbate insecurity in these countries, particularly as future US development assistance may also be in doubt.

Moreover, the resulting increased uncertainty and insecurity for undocumented migrants in the United States could affect the level of remittances sent back to Central America.

Limited trade impact.

The effect of Trump presidency on trade with Central America is likely to be relatively limited. While increased protectionism from Washington would have an impact on the Isthmus, the promised US withdrawal from the Trans-Pacific Partnership (TPP) trade deal involving twelve Pacific Rim countries could be beneficial to Central American textile producers because it would reduce the risk of competition from cheaper Vietnamese producers.

Moreover, a Trump administration focus on Mexico and NAFTA is likely to mean that DR-CAFTA, and trade relations with Central America more generally, are not a priority. This could create opportunity for Central American countries. A key motivation for the South Korean FTA was a desire to consolidate a first-mover advantage over its neighbours and use Central America as an entry point to North America and the rest of Latin America. Should it be successful, other countries, particularly in Asia, could seek to deepen trade relations with the region.

CONCLUSION: Reviewing its trade deal with Central America is unlikely to be a priority for the incoming US administration. Indeed, any increased protectionism towards Mexico could well increase Central America's attraction as a bridge to the US market.

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