Executive Memorandum

Published by The Heritage Foundation

No. 941
September 14, 2004

The U.S. Should Support Free Trade with Central America and the Dominican Republic

Brett D. Schaefer and Stephen Johnson

- DR-CAFTA represents a watershed moment for America's trade agenda.
- By approving the agreement, the U.S. would bolster political stability and encourage economic liberalization among close neighbors, supplying jobs to workers who would otherwise illegally migrate to the United States.

The Bush Administration has made great strides in opening foreign markets for American goods and services. Congress has already approved free trade agreements with Australia, Chile, Morocco, and Singapore—accords that will bring real benefits to producers and consumers in America and its trade partners. Congress now has an opportunity to extend free trade benefits to people closer to home by approving the Dominican Republic–Central American Free Trade Agreement (DR-CAFTA). Approval of DR-CAFTA is essential for both the long-term interests of the U.S. and maintaining America's commitment to free trade throughout the world.

This free trade agreement would enhance economic opportunities in the region and in America. It would also promote America's long-term national interests by bolstering political stability among close neighbors and encouraging economic liberalization in countries in which growth could supply jobs to workers who would otherwise migrate illegally to the United States. The U.S. should waste no time in approving DR-CAFTA, which will open overseas markets for American businesses, protect the homeland by reducing the flow of illegal immigrants, and help friendly countries by facilitating trade with America.

The Case for DR-CAFTA. Free trade negotiations with five Central American countries were concluded on March 15, and the agreement was signed in May 2004. Negotiations with the Dominican Republic were conducted separately. The DR-CAFTA agreement, which included all six countries, was signed on August 5, 2004.

Free trade with the Dominican Republic, Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua—the signatories of DR-CAFTA—is no small matter. Taken as a group, these six countries were America's 13th largest trading partner in 2003 with total trade of nearly $32 billion. Only Mexico was a larger U.S. trading partner in Latin America ($236 billion in 2003). Total trade with these nations outstrips that with Australia, Brazil, India, Russia, and many European nations.

Lowering barriers to trade with the Dominican Republic and Central America enhances opportunities for many American exporters and investors. According to the World Bank's *2004 World Development Indicators*, U.S. exports face tariffs of 10.1 percent in the Dominican Republic, 5.8 percent in

This paper, in its entirety, can be found at:
www.heritage.org/research/latinamerica/em941.cfm

Produced by the Center for International Trade and Economics (CITE)

Published by The Heritage Foundation
214 Massachusetts Avenue, NE
Washington, D.C. 20002–4999
(202) 546-4400 • heritage.org

Costa Rica, 6.1 percent in El Salvador, 5.8 percent in Guatemala, 7.3 percent in Honduras, and 2.3 percent in Nicaragua. According to the U.S. Trade Representative, DR-CAFTA would "eliminate eighty percent of the tariffs immediately, with the remaining tariffs phased out over 10 years." A free trade agreement would put U.S. exports on an equal footing by eliminating these tariff barriers and increasing access for agricultural, manufactured, and other products. The agreement would also change rules limiting U.S. investment in such sectors as energy, finance, insurance, telecommunications, transport, and tourism. Finally, DR-CAFTA includes a commitment to enhance protection for U.S. patents, trademarks, and other intellectual property.

In return, the Dominican Republic and the Central American countries would gain permanent tariff-free access to the $10.9 trillion U.S. economy, which is more than 145 times the size of their combined economies. This access would help the textile and garment sectors in the region—which draw on a wide range of U.S. manufactured goods—to compete with China and encourage new industries in those countries to take advantage of the U.S. market. The biggest winners, however, would be consumers and producers who would be able to purchase goods at cheaper prices—delivering an immediate improvement in the standard of living and production capabilities in DR-CAFTA countries.

Protecting America's Interests. Enhancing regional economic growth is key to improving long-term stability. As the Heritage Foundation's *Index of Economic Freedom* points out, countries that embrace economic freedom—including freedom of trade, labor, and capital—experience stronger growth than those that thwart commerce through regulatory hurdles and policy restrictions. By liberalizing rules and regulations constraining trade and investment, free trade sets these countries on a course toward greater prosperity that supports the democratic and free market evolution that has taken place in Central America over the last 20 years.

In the 1970s, nearly every Central American country (except Belize and Costa Rica) was ruled by a dictatorship bolstered by closed markets that protected state and family-owned monopolies. Limits on political and economic freedoms made the region vulnerable to Soviet-backed guerrilla movements. Today, the U.S-backed transformation to democracy and liberal markets is impressive, but by no means complete. DR-CAFTA would encourage further reform, offer market opportunities, and signal genuine U.S. interest in partnering with a region used to receiving development aid handouts.

Further progress is critical to provide jobs for Dominicans and Central Americans whose economies are struggling to become better integrated into the global system. Nearly 47 percent of these countries' citizens live below the poverty line, and these countries contribute a significant number of the illegal immigrants who enter the United States seeking employment.

Conclusion. This agreement represents a watershed moment for America's trade agenda. It will determine whether or not the U.S. will capitalize on recent gains in free trade and continue to push forward to help increase prosperity and security around the world. Free trade would expand markets for Central America, the Dominican Republic, and the United States. It would help to integrate these countries into the global economy and encourage needed economic reforms. Moreover, the agreement will signal the entire hemisphere that Washington is serious about market integration and helping its neighbors to develop.

The Bush Administration should submit the implementing legislation to Congress as soon as possible to enable Congress to approve DR-CAFTA this year.

—Brett D. Schaefer is Jay Kingham Fellow in International Regulatory Affairs in the Center for International Trade and Economics, and Stephen Johnson is Senior Policy Analyst for Latin America in the Kathryn and Shelby Cullom Davis Institute for International Studies at The Heritage Foundation.