

What does CAFTA mean for the Central American Garment Industry?

The US-Central America Free Trade Agreement (CAFTA) was signed on May 28, 2004 by the U.S., Costa Rica, El Salvador, Guatemala, Honduras and Nicaragua. On August 5, 2004 the Dominican Republic was incorporated into the agreement. If approved by signatory governments, CAFTA will allow for clothing from Central America to be exported to the United States without paying import taxes (called tariffs). Central America is currently able to ship clothes tariff-free under the US Caribbean Basin Trade Partnership Act (CBTPA).

There are three main differences between CBTPA and CAFTA relevant to *maquila* workers:

1 Migration and Wages

Under CBTPA, the United States gives tariff-free, called duty-free, access to its market for some Central American goods. Under CAFTA, Central America will receive more preferences but must also open its markets to the United States and accept US intellectual property and competition rules.

The sector most affected by CAFTA in Central America will be agriculture. It is likely that many small producers will be unable to compete with US imports of rice and corn. With a weakened rural sector, more people may look for work in cities, including in the *maquilas*. Increased competition for jobs in the *maquilas* will likely result in wages being pushed further down.

2 Labour Rights: Under CAFTA, labour rights are not a condition of receiving duty-

free access to the US market. With CBTPA and also the General System of Preferences (GSP), unions and labour rights organizations can petition the US Trade Representative to suspend trade preferences if a country fails to enforce labour laws.

Such petitions put limited pressure on Central American governments to respect freedom of association and collective bargaining. With CAFTA, each government, including the United States, pledges to enforce its own laws, no matter how weak. In addition, there is no effective penalty if the country fails to enforce its labour laws.

3 Rules of Origin: The *maquila* industry will have more favourable rules of origin under CAFTA. Clothes made from yarn spun in Central America or the US can be

exported duty-free to the US. With some exceptions, if the materials are from Asia, then the clothes do *NOT* qualify for duty-free treatment.

In most cases, under CBTPA, either the yarn or the cloth has to be from the US in order to qualify for duty-free access to the US market. Because materials from Asia are so much cheaper, many manufacturers use them anyway because the extra tariff they pay to get their clothes into the US is still less than the added cost of buying materials from the US.

Currently, 70% of all apparel products exported to the US from Nicaragua is made from cloth that is neither from Central America nor from the United States. The figures are lower for other Central American countries – 60% for Guatemala, between 35 and 40% for Costa Rica and El Salvador, and 25% for Honduras.

fact sheet

5 A series on
trade and
labour rights in
the garment
industry.

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● FOCUS: CAFTA and Workers' Rights

To participate in CAFTA, countries are only required to enforce their existing labour laws even though many of these laws are not in compliance with international standards. For example, in its December 2003 report on workers' rights in El Salvador, Human Rights Watch documents numerous legal loopholes that allow employers to circumvent freedom of association protections, through tactics such as forced resignations, anti-union suspensions, and blacklisting.

Also, CAFTA's definition of labour laws excludes "workplace discrimi-

nation," which means that a country's failure to enforce its own anti-discrimination labour laws cannot be addressed through CAFTA.

If a country fails to enforce its labour laws, another CAFTA country can file a request for a review of that country's compliance with the agreement. There are no provisions in the agreement for civil society organizations to launch formal complaints, nor does it require public reporting on the outcomes of a review. If a dispute cannot be settled, an arbitration panel can impose a fine *on the*

offending country. The country must pay the fine, a maximum of US\$15 million, into a fund that is to be used for "labour initiatives." The money put into the fund goes back to the country to carry out these labour initiatives, but there is no mechanism to ensure that the country addresses the problem. Only if the country fails to pay the fine, can tariffs be suspended up to the level of the fine assessed. So, the offending country could pay the fine, ignore the labour rights violation and still participate in CAFTA.

● FOCUS: CAFTA and Rules of Origin

The CAFTA rules of origin are similar to those of the North American Free Trade Agreement (NAFTA) between Canada, Mexico and the US, which came into effect January 1, 1994. Clothes made from yarn spun in the region or in the US qualify for preferences. This rule is called "yarn forward" because origin is determined by the fact that all the processes from yarn spinning onward take place in the CAFTA region (i.e., the US, Central America and the Dominican Republic). So, fibres can come from anywhere. Here's an example:

Cotton fibres from Egypt are spun and woven in Guatemala. The fabric is cut and assembled into shirts in El Salvador. With CAFTA, the shirt qualifies for duty-free treatment when exported to the US. Under CBTPA, it would not because there are no US components.

There are some important exceptions to the "yarn forward" rule, such as:

"Fabric forward"

For wool goods, origin will be determined from where the fabric is woven, called "fabric forward." The wool yarn can come from anywhere, but must be woven in the CAFTA region (except the Dominican Republic) in order to qualify for duty-free treatment.

"Cutting forward"

For certain goods, origin will be determined from the cutting stage onward. The goods that qualify are bras, men and boys' woven boxers and pyjamas, women and girls' woven pyjamas and negligees, and some dresses. Here's an example:

Cotton fibres from Indonesia are spun and woven in South Korea. The cloth is cut and sewn into boxer shorts in Honduras. With CAFTA, the boxers qualify for duty-free treatment when exported to the US. Under CBTPA, they would not because there are no US components.

"Short Supply"

In consultation with the US and Central American industries, the US created an expanded list of 43 fabrics

and yarns that can be brought in from Asian or other non-CAFTA countries, and still qualify for duty-free treatment, if they are unavailable in commercial quantities in the US or Central American countries.

Special Treatment for Nicaragua

CAFTA includes a provision allowing Nicaragua to export duty-free up to 100 million square metres equivalent (SME) of clothing assembled in Nicaragua made of cloth from countries outside the region. This applies only to cotton and man-made fibres and not to wool. After the first year of the agreement, this special exception will be reduced by 20 million every year for four years.

What about Canada and Mexico?

CAFTA preferences are limited to the CAFTA region for most clothing exports. The "cumulation" provision allows fabrics or yarn from all three NAFTA countries (the U.S., Canada and Mexico) to be used for garments made from woven materials. There is an annual cap on cumulation that may be increased or decreased depending on growth in CAFTA trade.