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Trade Policy Analyses

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The Cordell Hull Institute, in conjunction the International Food and Agricultural Trade Policy Council, held a half-day meeting on July 15, 2005, on the next U.S. farm bill and the Doha Round negotiations.

The meeting was held at Arnold & Porter, attorneys-at-law in, Washington, DC. Pictured above is the well of the firm's building.

Robert L. Thompson of the University of Illinois based discussion on a PowerPoint presentation.



Reproduced here is the revised text of the paper by **Robert L. Thompson** (above).

About the Author

Robert L. Thompson is the Gardner Professor of Agricultural Policy at the University of Illinois at Champaign-Urbana. As

NEXT U.S. FARM BILL...

Essentials for the 2007 Farm Bill in a Global Context

Robert L. Thompson

FROM the mid-1980s through the 1990s the United States played a major leadership role in promoting agricultural trade liberalization and policy reform. The 1996 Farm Bill, officially the Federal Agriculture Improvement and Reform Act of 1996, moved U.S. farm policy far in a market-oriented direction. During this period the United States was a strong advocate in the Uruguay Round of multi-lateral trade negotiations, the eighth and last round under the General Agreement on Tariffs and Trade (GATT), for bringing discipline to bear – through internationally agreed rules – on national agricultural policies that distort the locus of production and pattern of trade. But then the 2002 Farm Bill, officially the Farm Security and Rural Investment Act of 2002, reversed that course by increasing authorized spending, and levels of intervention, on U.S. farm subsidies.

In the next two years a new farm bill will be written in the United States and, at the same time, the Doha Round negotiations in the World Trade Organization (WTO) should be brought to a conclusion. These two activities, while proceeding in parallel, will each make a significant impact on the other. The purpose of this paper is to review and clarify the forces bearing on each of these activities and their interactions.¹

The paper begins by recalling the stated goals of U.S. farm policy and then turns to a brief historical review of the policy from its beginnings in the late 1920s through to the reforms embedded in the 1996 Farm Bill. After reviewing the progress achieved in the WTO Agreement on Agriculture reached in the Uruguay Round negotiations of 1986-94 (cited hereafter as the URAA), the paper turns to the 2002 Farm Bill, which reversed the course of American agricultural policy. The center section of the paper addresses the domestic forces that are conditioning the 2007 Farm Bill. The paper then examines the state of the Doha Round negotiations on agriculture, now entering a serious phase, as

the chairman, since 2002, of the International Food and Agricultural Trade Policy Council, Washington, DC, he has been active in the global debate on WTO agricultural trade issues.

In August 2005, Dr Thompson was appointed to the Agricultural Policy Advisory Committee for Trade, which works with the U.S. Department of Agriculture and the Office of the U.S. Trade Representative.

From 1998 through 2002, Dr Thompson was at the World Bank, where he served as the Director of Agriculture and Rural Development, then as the senior advisor for agricultural trade policy.

Earlier he served as the president and chief executive officer of the Winrock International Institute for Agricultural Development (1993-98), Merrillton, AK; as Dean of Agriculture (1987-93), and Professor of Agricultural Economics (1974-93), at Purdue University, West Lafayette, IN; as Assistant Secretary for Economics at the U.S. Department of Agriculture (1985-87); and as senior staff economist for food and agriculture at the President's Council of Economic Advisers (1983-85).

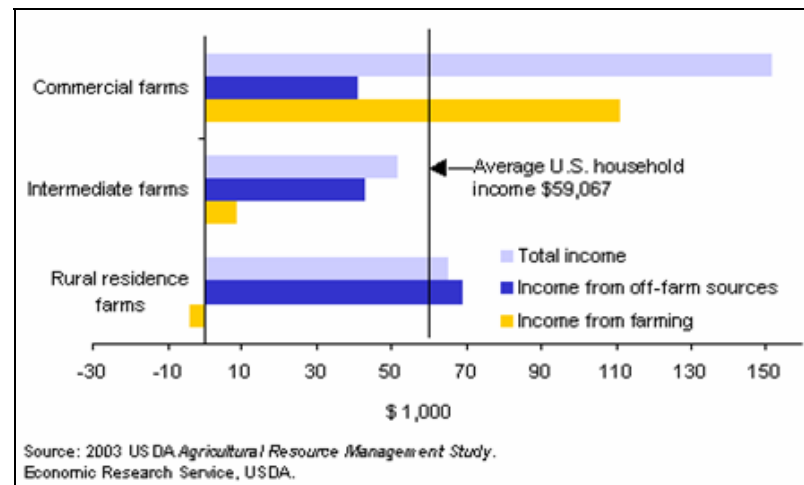
Dr Thompson is a past president of the International Association of Agricultural Economists. He is also a fellow of the American Agricultural Economics Association and of the American Association for the Advancement of Science; and a foreign member of the Royal Swedish Academy of Agriculture and Forestry and of the Ukrainian Academy of Agricultural Sciences. He is also a

preparations for writing the 2007 Farm Bill are getting under way. The paper concludes with some observations on the prospects for agricultural policy reform in both the Doha Round negotiations and the 2007 Farm Bill.

Objectives of Farm Policy at Odds with 21st Century Reality

The most common arguments in favor of government support for agriculture are low farm-family incomes and "excessive" variability in those incomes. Two-thirds of American farmers receive no farm-program benefits because they do not grow "program crops". There is no evidence that these farms are less profitable than those receiving farm-program benefits. Most program payments are distributed in proportion to past or present sales of "program commodities" and so the largest producers of those commodities get the largest benefits. Because most program payments get capitalized into the value of farmland, most of the benefits accrue ultimately to the largest owners of farmland, a group whose average wealth far exceeds the national average.

Chart 1: Sources of Operator Household Income by Typology Group, 2003



Misperceptions of Modern Farming

In the U.S. public at large there are many misperceptions of modern farming. Most Americans are too far removed from the farm to have much understanding of modern American agriculture. There is a nostalgic view of the small family farm that is way out-of-date. One source of the misperceptions is the outmoded definition of a "farm" that is used in official statistics on American agriculture. Any place that sells over \$1,000 worth of agricultural products a year is deemed to be a farm. The Economic Research Service of the U.S. Department of Agriculture (USDA) disaggregates these data into three broad groups: rural residence farms,

member of the Council on Foreign Relations, New York, and the Chicago Council on Foreign Relations.

Other Speakers

Besides Professor Thompson, the other main speaker was **Hugo Paemen**, a senior advisor at Hogan & Hartson, attorneys-at-law, who was previously the Permanent Representative of the European Commission in the United States.

The discussants at the meeting were: **Evandro Didonet**, Minister-Counselor for Economic Affairs and Trade Policy at the Brazilian Embassy, Washington, DC; **Frances Freeman**, Minister-Counselor (Agriculture) at the Australian Embassy, Washington, DC; and **James Grueff**, former U.S. agricultural trade negotiator, now a partner at Decision Leaders LLC, trade consultants, Washington, DC.

Trade Policy Roundtable

The Cordell Hull Institute's Trade Policy Roundtable is sponsored by eight international law firms in Washington, DC: Akin Gump Strauss Hauer & Feld, Arnold & Porter, Hogan & Hartson, Miller & Chevalier, O'Melveny & Myers, Sidley Austin Brown & Wood, Steptoe & Johnson and Wilmer Cutler Pickering Hale & Dorr.

intermediate farms and commercial farms (see Chart 1).² Over 1.2 million of the 2.1 million "farms", so defined, sell less than \$10,000 worth of product per year (as shown in Table 1).³

Table 1: Size Distribution of U.S. "Farms", 2003

Size in \$ thousand	Thousand Farms	% of all Farms	% with payment	Ave \$/pay farm (000)
<10	1,227	58	20	2
10-49	398	19	53	6
50-99	172	8	71	10
100-249	165	8	78	19
250-499	86	4	78	34
500-999	45	2	70	55
>1000	29	1	56	82
All	2,123	100	39	13

Source: Economic Research Service, U.S. Department of Agriculture, Washington, DC

In no sense are these so-called farms viable commercial businesses that can support a family. They are "rural residence farms" or "hobby farms" or both. In fact, 77 percent of the farms in the United States, by the official definition, collectively contribute only 14 percent of the country's production of food and fiber. On average, they earn more than the median family income from *non-agricultural* sources and lose money on their farming operations. The only group whose income averages less than the median U.S. household income is intermediate farms and they receive very little from farm programs.⁴

Another misperception is that corporate agri-businesses have taken over American farming and receive most of the farm-program benefits. This is false. Most commercially viable farms today are incorporated for tax and estate-planning purposes and ease of transfer of ownership between generations. Agri-businesses account for less than 10 percent of farm output and much of that is in the production of non-program commodities. The popular belief that corporate agri-businesses receive a lot of farm-program payments is simply wrong.

To stabilize their incomes farmers can buy price insurance (put options) and federally subsidized crop insurance. Farmers also have two other ways to smooth their incomes that are not available to other forms of business. First, farmers are allowed to use cash accounting, which facilitates shifting income and expenses between two tax years; and, secondly, farms are the only businesses allowed to use income averaging (over four years)

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when calculating their income tax. When one closely examines most arguments for stabilizing farm programs, what farmers are really seeking is "stabilization" around a higher average. It is therefore difficult to justify farm programs on the basis of either low farm-family incomes or income volatility.

The Environmental Working Group has posted on its website (www.ewg.org) data obtained through Freedom of Information Act requests on how much each individual farmer (by name) receives from USDA programs.⁵ The ready availability of this information spawned a flurry of anti-farm program editorials in newspapers throughout the country. The transparency which publicly posting these data has brought to farm programs has forever changed public discussion of the justification for, and benefits of, farm programs. The argument that farm programs help low-income family farmers is no longer persuasive.

Brief History of U.S. Farm Policy⁶

American agriculture prospered during World War I, but when European agriculture recovered after the war, U.S. exports collapsed. Farm production capacity in the United States was left well in excess of domestic demand; and in 1921, agriculture went into depression, almost a decade earlier than the rest of the economy. After several halting attempts to shore up farmers' incomes in the late 1920s, Congress passed the Agricultural Adjustment Act of 1933, which laid the foundation for U.S. farm policy for more than half a century – to this day, in some sense.

To raise the prices farmers got for their products, various acreage restrictions and marketing controls were introduced to constrain supply. Agricultural productivity, however, rose faster than domestic demand grew, making the "surpluses" even larger. Because U.S. commodity prices were being supported at levels well above world market prices, exports were possible only when subsidized or given away as food aid.

After the U.S. dollar was devalued in 1971 and 1973, U.S. farm products once again became internationally competitive; and exports grew rapidly through the 1970s until about one-third of production went into world markets. Weakness of the U.S. dollar in the late 1970s further facilitated exports. In 1981, however, the dollar appreciated significantly, while Congress wrote a new farm bill that prescribed minimum levels at which U.S. prices would be supported ("loan rates"). Once again U.S. farm policy undercut the inter-national competitiveness of U.S. farm products. Agricultural exports fell by over 40 percent in five years. This precipitated the worst financial crisis in rural America since the 1930s, exactly 60 years after U.S. agriculture went into depression, as U.S. exports collapsed with the recovery of West European agriculture after World War II – helped by subsidies and protection through the European Union.

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The 1985 Farm Bill, which was passed as the Food Security Act of 1985, had to deal with the financial crisis while restoring the international competitiveness of U.S. agriculture. To transfer income to farmers, the bill provided "deficiency payments" equal to the difference between a politically determined "target price" and the market price or the loan rate (price support), whichever was higher. To restore international competitiveness, the loan rates were reduced to 85 percent of a moving average world market price. "Marketing loans" were created for cotton and rice in which the USDA would pay farmers the difference (the "loan deficiency payment") between the loan rate and what it determined to be the world market price.

To prevent deficiency payments from inducing larger production than would otherwise have occurred, the 1985 Farm Bill began "decoupling" payments from production decisions. Deficiency payments were no longer based on actual production. Instead they were based on a fixed historical average yield and the number of acres planted to each program crop. The 1990 Farm Bill completed the decoupling of payments from production decisions by also fixing the acreage base for each crop at historical levels. Since planting and input decisions could no longer influence the deficiency payment a farmer received, the payment was fully decoupled from production decisions.

The 1996 Farm Bill gave farmers still greater planting flexibility by doing away with target prices, deficiency payments and acreage-reduction programs. The bill eliminated any link between income-support payments and market prices. To compensate for giving up deficiency payments, farmers were granted "production flexibility contract" payments, also known as Agricultural Market Transition Act (AMTA) payments, which were to be phased out over the seven-year life of the bill.

Advocacy of Freer Farm Trade

During this period the Uruguay Round negotiations were taking place. The United States and the Cairns Group of smaller agricultural-exporting countries, led by Australia, were advocating freer and more open international markets for agricultural products. At the insistence of both, domestic agricultural policies were on the negotiating table, which was the first time they were addressed systemically in GATT negotiations. In previous rounds, it was difficult to address domestic policies, for multilateral trade negotiations were considered to be about border measures – whereas the main instruments of farm-support policies were within borders.

The Tokyo Round negotiations of 1973-79 were substantially about tackling non-tariff measures within borders, including public subsidies to manufacturing industry and technical barriers to trade in manufactures. An effort was also made to address domestic farm-support measures, which negotiators realized in the earlier

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Kennedy Round negotiations of 1964-67 would have to be tackled for progress to be made in liberalizing trade in the agriculture sector. Towards the end of the negotiations, however, the United States and the European Union took agriculture off the table. There was no sign of an agreement being reached and they did not want to jeopardize an agreement on industrial products.⁷

While acknowledging that there are often exceptional occasions when, for political reasons, a government believes it has to provide support to farmers, the United States sold the notion that not all payments to farmers are equally distorting of agricultural production and trade. Support that is linked to the volume of production or the sales of specific commodities distorts farmers' production decisions more than direct payments.

This led to the division of farm-support measures into three categories or "boxes" for negotiating purposes:

(a) Support that is clearly linked to production was put into an "amber box" category. Each country accepted a maximum "aggregate measurement of support" (AMS) below which it agreed to keep its total amber box support.

(b) Countries were encouraged to "decouple" support from the production of specific commodities by also creating a "green box" category on which there would be no AMS cap. The green box includes direct payments that are not linked to present or future production of any specific product. These payments might be for "doing something", like conserving the soil or protecting the land-scape for tourism, or they could be direct income transfers to farmers calculated on some *fixed* historical base. Investments in public goods like agricultural research, extension and teaching, as well as collecting and diffusing agricultural statistics and market information, were also included in the green box.

(c) A third category of agricultural subsidies was the "blue box". Policies were categorized in the blue box if, although inducing larger production, they included a constraint such as a land set-aside program or a marketing quota on the volume of production or sales of the product in question.

In the Uruguay Round negotiations on agriculture, the United States also advocated the conversion of non-tariff barriers into tariffs, which could then be reduced by an agreed percentage over the implementation period. This was important because, in part, it is much harder for potential suppliers to compete for a country's purchases when imports are constrained by a quota, as opposed to a tariff.

But there is a more important economic argument for "tariffication" – as this conversion came to be known. A quota or some other non-tariff barrier (NTB) to imports, such as a variable import

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levy, cuts the link between the world market price and the domestic price of a product so that the domestic price no longer moves up and down with the world market price, which means domestic producers and consumers get no signal to adjust. All the adjusting has to be done by the producers and consumers in the countries whose domestic prices are linked to the world price (even when distorted by a tariff). When fewer than usual producers and consumers participate in the adjustment to any shock in the world market, the world market price has to adjust more than it would if all suppliers, everyone in all markets, shared in the adjustment. This causes world commodity prices to be more volatile than they would otherwise be and increases the price risk to producers and consumers in the rest of the world. If all countries were to reconnect domestic prices to world prices, the swings in world commodity prices would be dampened.

The United States and the Cairns Group both sought a ban on agricultural export subsidies. From the outset of the multilateral trading system, under the General Agreement on Tariffs and Trade (GATT), export subsidies to trade in non-agricultural products were banned under GATT Article XVI. In the URAA, agricultural export subsidies were frozen, in terms of both value and volume, and reduced (but not banned); and no country could start subsidizing exports of a commodity not previously subsidized.

The 2002 Farm Bill

Congress passed the 2002 Farm Bill early. Budget surpluses were coming to an end, but the "budget baseline", within which Congress had to draft the bill, had not yet been revised. A few years earlier, the Uruguay Round negotiators had agreed a \$19.1 billion AMS ceiling on amber-box subsidies to U.S. farmers. There was wide-spread "subsidy envy" among American farmers over the fact that the European Union had negotiated an AMS cap of \$67 billion, more than three times larger than theirs. Congress was in a mood for spending and looked at the AMS for the United States more as a target to be attained than as an upper binding on farm programs. Out of fairness to the Congress, they tried to design programs that would not exceed the AMS cap, but they didn't want actual subsidies to fall very far short of it either. The net result was to increase budget authority for its farm programs at a time when the United States was telling everybody else to cut theirs.

The 2002 Farm Bill raised (lowered) loan rates on grains (soybeans).⁸ The 1996 Farm Bill had provided an excessive incentive to produce soybeans relative to other crops that could be grown that year in the same places, and the 2002 bill corrected this market distortion. The 2002 Farm Bill reestablished a target-price system and created a new counter-cyclical payment (CCP). The CCP program institutionalized \$2 billion of *ad hoc* "emergency payments" that had been made each year on top of that authorized under the 1996 Farm Bill.

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The 2002 legislation watered down limitations on payments, allowing each farmer to get a larger total payment, and authorized updating the historical bases, meaning payments were no longer decoupled from production decisions. The bill also institutionalized fixed direct payments in place of the AMTA payments, which had been designed as transitional compensation that would be phased downwards. The 2002 Farm Bill (i) created new farm programs for commodities that had never before had them, such as small legumes, (ii) resurrected previously killed programs for wool, mohair and honey, (iii) increase-ed benefits to sugar producers and (iv) created another dairy pro-gram. It bought out the quotas in the old peanuts-support program and replaced it with a new support program.

In other countries, where hopes of progress in the Doha Round negotiations on agriculture were running high, the 2002 Farm Bill was seen as an abdication of U.S. leadership in reforming farm-support policies and liberalizing agricultural trade. The United States, which had led the global effort to reduce agricultural subsidies, appeared two-faced, telling the rest of the world to cut their farm subsidies while increasing its own. By allowing the bases for direct payments to be updated, the new farm bill was seen as a retreat from decoupling by the United States, its author and strongest advocate.

The United States had also been arguing that the prices to which farmers respond in making their production decisions should be linked to world market prices so that farmers everywhere adjust their planting up and down according to changing world market price signals. Counter-cyclical payments violate this principle. They reduce American farmers' responsiveness to falling prices, but not to rising prices. Furthermore, marketing loans, which were created originally for cotton and rice in the 1985 Farm Bill, are in effect export subsidies. While the U.S. negotiators argued against export subsidies, the 2002 Farm Bill broadened the role of marketing loans in U.S. agricultural policy.

Towards the 2007 Farm Bill

There are several points to keep in mind when identifying factors likely to influence the writing of the 2007 Farm Bill. First, a farm bill is much more than commodity programs. The 2002 Farm Bill had ten titles:

- I. Commodity Programs
- II. Conservation
- III. Agricultural Trade and Aid
- IV. Nutrition Programs
- V. Farm Credit
- VI. Rural Development
- VII. Research
- VIII. Forestry

- IX. Energy
- X. Miscellaneous

While two-thirds of American agriculture is not affected by commodity programs, most of it is affected by programs authorized under one or more titles.

Another important point to bear in mind about farm bills is that they are authorizing legislation. Implementation of most programs authorized in a farm bill (even when the authorization specifies an annual expenditure level) requires an appropriation each year. There is an important exception, however, that is unique to the USDA. Many of the farm commodity programs are authorized in farm bills as entitlements that can be run independently of annual appropriations. The Commodity Credit Corporation (CCC) has a standing line of credit at the U.S. Treasury of \$30 billion against which the USDA draws. Periodically, after enough money has been paid out to farmers, the USDA goes to Congress for a "replenishment" of its line of credit. (See Table 2.)

In the Administration's fiscal year 2006 budget proposal transmitted to Congress in February 2005, a modest reduction in farm programs was proposed - \$5 billion over five fiscal years. Farm organizations and commodity groups responded angrily.

Some members of the Congressional agriculture committees even proposed that the cuts be taken out of food stamps, which go to low-income people, instead of the farm programs.

Table 2: Commodity Credit Corporation's Outlays, by Commodity (\$ thousand)

Commodity	2002	2003	2004	2005E
Corn	2,959	1,415	2,504	7,683
Wheat	1,190	1,118	1,173	1,495
Rice	1,085	1,279	1,130	586
Upland cotton	3,307	2,889	1,372	4,721
Soybeans	3,447	907	595	1,563
Dairy	622	2,494	295	633
Total	15,680	17,425	10,575	24,065

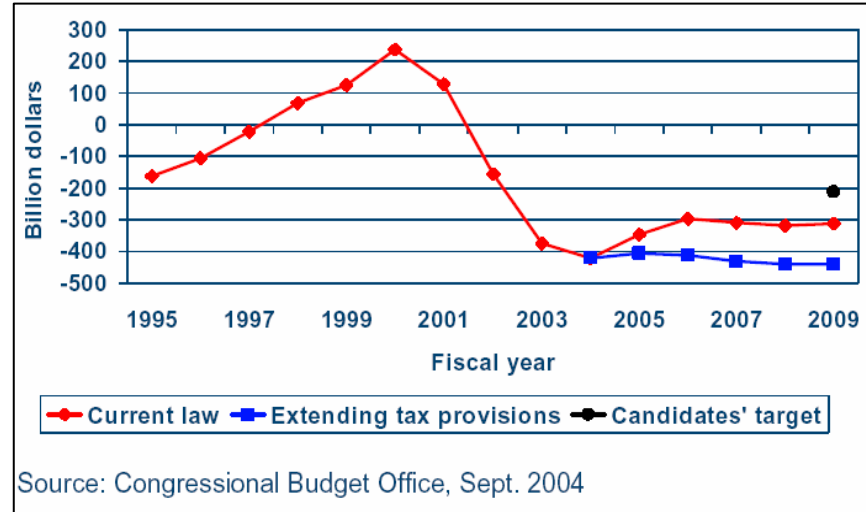
Source: Commodity Credit Corporation, U.S. Department of Agriculture, Washington, DC

Federal Budget Deficit

The 2002 Farm Bill was passed by Congress using a budget-baseline projection that everyone involved knew was wrong. That farm bill was rushed through Congress early in order to get as much money committed to farm programs as possible before the baseline was updated. The federal deficit returned and has run at about \$400 billion per year since 2003. Despite frequent calls to do something about the budget deficit, neither the White House nor the Congress appears to be very concerned. In 2004 both candidates for the presidency talked about reducing the annual deficit to about \$200 billion (see Graph 1). Many observers have argued that agriculture must participate in deficit reduction, particularly since there never would have been as much money

available for farm programs if the 2002 Farm Bill had not been taken up ahead of schedule.

Graph 1: U.S. Federal Budget Deficit, 1995-2003 and Projection to 2009



The budget resolution that Congress passed on April 28, 2005, authorized a \$2.6 trillion federal budget for fiscal year 2006. Exhibiting no apparent commitment to deficit reduction, this budget projects deficits of multi-hundred billion dollars a year for five years...

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In the Administration's fiscal year 2006 budget proposal transmitted to Congress in February 2005, a modest reduction in farm programs was proposed – \$5 billion over five fiscal years. Farm organizations and commodity groups responded angrily, arguing that the government was breaking faith (if not a legal contract) with farmers, who had made their five-year business plans assuming that the full anticipated benefits of the 2002 Farm Bill would remain intact for the full five-year life of the legislation. Some members of the Congressional agriculture committees even proposed that the cuts should be taken out of food stamps, which go to low-income people, instead of farm programs.

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U.S farm programs have never been subjected to a binding budget constraint. Even in 1985, when the Gramm-Rudman-Hollings Bill mandated across-the-board reductions in federal outlays to reduce the deficit, the Congress passed a farm bill that authorized the

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largest farm-program benefits ever. Whether the environment in 2007 will be any different remains to be seen.

Many budgetary commitments get made in the heat of Presidential election campaigns. For example, in the 2004 campaign in Wisconsin both candidates pledged to continue the Milk Income Loss Contract (MILC) program, a temporary additional dairy program created in the 2002 Farm Bill, which was slated to expire. The President's fiscal year 2006 budget proposal contained funds to continue this program for two more years. When all such commitments are added up, they also make it more difficult to reduce the federal budget deficit.

Breakdown in Inter-commodity Solidarity?

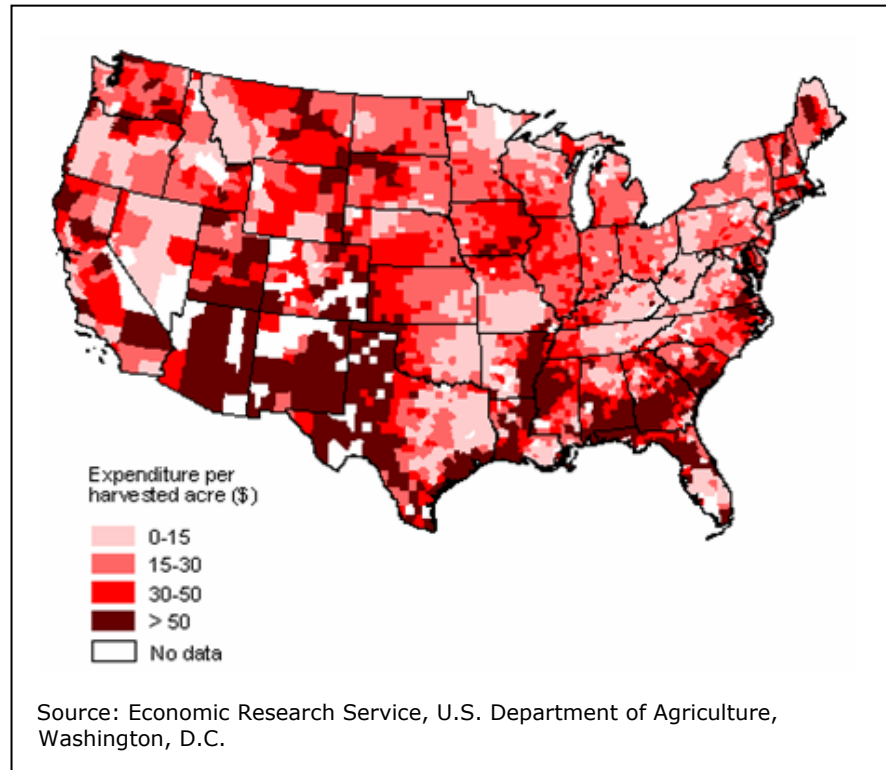
U.S. agriculture's political clout has been enhanced over the years by solidarity and the formation of coalitions among commodities. For many years dairy and tobacco interests formed a very effective coalition that resulted in each securing more farm program benefits than either could have secured if they had worked independently. Cotton has the most "vertically integrated" program of any commodity. Every phase of the industry gets something from the cotton program - from those who grow cotton to those who gin, ship, store, export or use it domestically. This has ensured cotton-industry solidarity in support of the program.

Agricultural commodity organizations have traditionally deferred to one another's interests, as have individual commodity groups within the general farm organizations. There has always been enough money to go around. Even when certain commodities or regions have seemed to get more benefits than others (see Map 1), amity and solidarity have generally prevailed.

In 2005 one observes cracks in this historical solidarity. Leaders in farm and commodity organizations are beginning to acknowledge that 2007 may be different, that Congress really is going to have to do something about the federal budget deficit and that agriculture will be forced to "participate" in deficit reduction. One hears suggestions that the inter-commodity and inter-region solidarity may break down in the face of a tight budget constraint. The large differences in Producer Support Estimates (PSEs)⁹ among commodities and among regions, and in payments per farmer, are starting to bring demands for greater "equity". For example, groups that earlier deferred to sugar were angry at the sugar industry's opposition to the Central American Free Trade Agreement, also embracing the Dominican Republic (CAFTA-DR), which was generally regarded as good for the agricultural sector as a whole.

Farm-program legislation bans the production of fruits and vegetables on land benefiting from commodity programs. A recent

Map 1: Distribution of Commodity Payments per Harvested Acre



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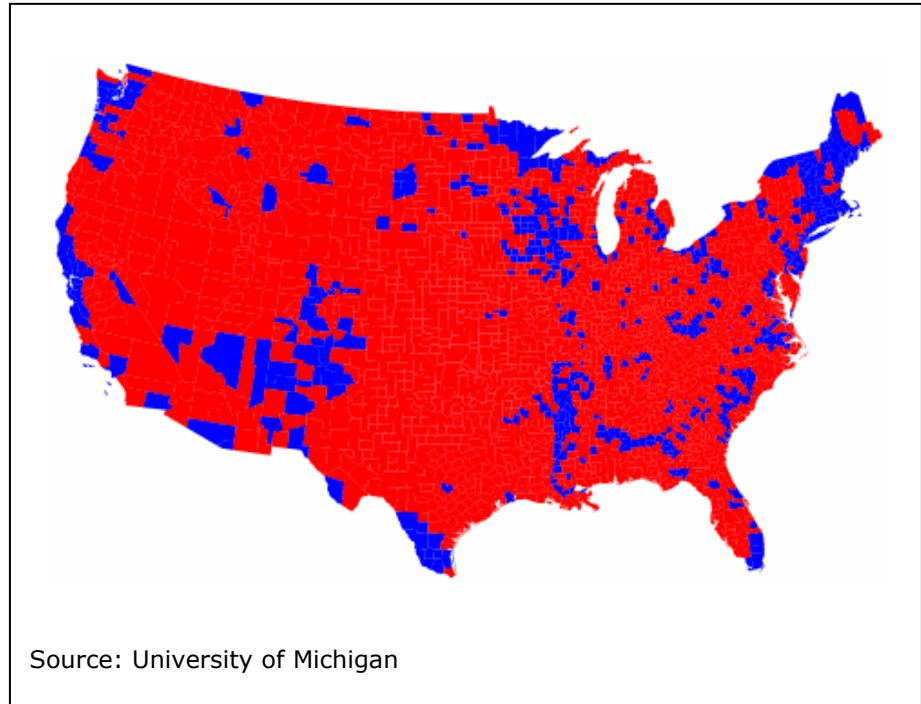
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decision by a WTO dispute-settlement panel (the *Brazil Cotton Case*, discussed in more detail below) ruled that that exclusion has to be removed if the United States wants to continue claiming its direct payments as green-box support, not subject to an AMS cap. Otherwise, those payments must be reported as amber-box support. Changing this exclusion could bring land that previously grew program commodities into fruit-and-vegetable production in competition with existing growers. This would certainly cause fragmentation between fruit-and-vegetable interests and the program commodities. On the other hand, if the United States does not remove the exclusion, it will violate its AMS cap.

Election Politics and the High Cost of Elections

Don't forget that rural America re-elected George Bush in 2004! If one overlays a map showing the "red" (Republican majority) and "blue" (Democratic) counties in the 2004 presidential election¹⁰ (Map 2) with a map showing where farm program payments go¹¹ (Map 1), the correlation is striking. One can understand that the President's fiscal-year 2006 budget proposal did not push very hard to reduce farm-program payments going to counties that so recently voted for the President's re-election. Congressional and Presidential elections are extremely expensive in the United States where little real campaign reform has occurred.

Map 2: Results of the 2004 U.S. Presidential Election by County (Red indicates Republican majority; Blue, Democratic majority)



In 2005 one observes cracks in the historical solidarity. Leaders in farm and commodity organizations are beginning to acknowledge that 2007 may be different, that Congress really is going to have to do something about the federal budget deficit and that agriculture will be forced to “participate” in deficit reduction.

Campaign contributions do buy access for a firm’s or an interest group’s position to be heard by the Executive Branch and the members of Congress involved in writing legislation of interest to them. Food and agri-business groups are generous contributors to both Congressional and Presidential election campaigns. Recent data on contributions by “political action committees” (PACs) to federal candidates in the 2004 election cycle list \$12.3 million in contributions from farm and commodity organizations and from food and agri-business companies (see Table 3).¹² When the data for agricultural commodity PAC contributions are examined (as shown in Table 4), one can see a positive correlation between the magnitude of campaign contributions and producer support for the corresponding crop. The four highest agricultural campaign contributors, namely the sugar, dairy, cotton and rice industries, are also the commodities with the highest PSEs (see Table 3).

Despite the shrunken size of the U.S. farm sector and its work force relative to the U.S. economy and population, respectively, its interest groups have effectively managed their campaign contributions and political influence to give them political clout far in excess of their numbers. Many more Americans are concerned about issues like Social Security reform, Alternative Minimum Tax relief, the funding of local schools and prescription drugs under Medicare than farm programs. There is little public goodwill towards farm programs that accord most of the benefits to the largest producers and farmland owners. Nevertheless, there was

sufficient political support for farm programs to avoid reductions in this year's budget process almost completely.

Table 3: U.S. Producer Support Estimates (PSEs), 2001-2003

Commodity	Percent
Sugar	58
Milk	44
Rice	44
Sorghum	37
Wheat	34
Barley	30
Corn	20
Soybean	19
Wool and lamb	17
Pork, beef and broilers	4
Overall	19

Source: PSE database, Organization for Economic Cooperation and Development, Paris

Table 4: Food & Agricultural PAC Contributions to Federal Candidates, 2004 Election Cycle

Sector	Contributions (\$ million)
Agric Inputs & Services*	3.2
Food Processing/ Sales	2.7
Sugar growers/ proc'ors	2.4
Tobacco companies	2.1
Crops other than sugar	2.0
Dairy	1.8
Other livestock & poultry	0.7
Vegetables, fruits & nuts	0.6

* Machinery, pharmaceuticals, credit, insurance, fertilizer, seeds, ag chems, etc.

Source: Center for Responsive Politics (Federal Election Commission data)

Three final points related to political influences on the 2007 Farm Bill merit mention here.

- The Congress and the White House are now extremely politicized. There is virtually no bipartisan cooperation among either of the Congressional agriculture committee

Congressional and Presidential elections are extremely expensive in the United States where little real campaign reform has occurred...

members or their staffs. This is very different from the traditional behavior of the agriculture committees. Today each party is attempting to make the other look as bad as possible – even if it means Congressional paralysis.

- Second, we will not know until November 2006 the Republican-Democrat split in the Senate and the House of Representatives that will write the next farm bill.
- Finally, the state of Iowa has the first Presidential primary, and no aspirant for the Presidency of the United States will utter a word against any farm program while campaigning in Iowa for fear of being an early casualty in the campaign. By the time a candidate is elected President, he has made so many commitments that it is hard to exercise leadership to change farm programs.

Table 5: PAC Contributions to Federal Candidates, 2004 Election Cycle

Commodity	Contributions (\$ 1,000)
Sugar	2,375
Dairy	1,757
Cotton	479
Rice	283
Peanuts	218
Citrus	17
Wheat	100
Potatoes	57
Corn	37
Soybeans	17

Source: Center for Responsive Politics (Federal Election Commission data)

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Role of Environmental Groups?

The first time that environmental groups played an active role in writing a U.S. farm bill was in 1985. That farm bill created the long-term conservation reserve program (CRP) under which farmers bid for annual compensation for idling erosion-prone land for ten years. The CRP was created by a coalition of environmental groups concerned about conservation and farm organizations that sought more supply control by the government. In addition, the 1985 Farm Bill introduced the so-called “sod-buster” and “swamp-buster” provisions. And it created “conservation compliance” requiring any farmer who receives benefits from any USDA program to have a farm conservation plan that meets specified environmental standards – failing which would cause that farmer to lose all USDA benefits. To add these measures to U.S.

agricultural legislation required an unprecedented degree of cooperation between agricultural and environmental groups.

I would characterize the relationship over the last 20 years between these two groups, environmentalist and farmers, as wary of one another. Farmers see many environmental regulations as overly restrictive, increasing their costs more than the expected benefits are worth. They see environmental organizations as too prone to use the stick instead of the carrot. Most farm organizations have not forgiven the Environmental Working Group for making transparent how much each individual farmer receives in farm-program payments.

Since 2002, every time Congress has authorized disaster payments, agricultural interests have successfully lobbied to have the cost subtracted from appropriations for conservation measures, not from commodity programs. Furthermore, neither the farm lobby nor the Bush Administration has supported funding of the new Environmental Conservation Security (ECS) program authorized in the 2002 Farm Bill, which has remained unfunded and unimplemented. Such actions have led the environmental organizations to doubt the sincerity of farm organizations' support for conservation programs. This behavior by farm groups, however, is not unique to environmental measures. Farm organizations support funding research, conservation, trade promotion and the like as long as the appropriations are additional to commodity programs. They have been unwilling to reduce near-term commodity-program benefits in exchange for federal investments in measures that would have longer-term payoffs for the sector as a whole.

In the Doha Round negotiations, European farm groups, who foresee lower traditional farm-program benefits, would like to see more direct payments to underwrite the cost of soil conservation, protection of the landscape and investments in other measures beneficial to the environment and, too, in rural development. It is likely to be easy to get agreement with the European Union for this kind of "doubly green"¹³ payments to be exempted from any "binding" or AMS cap in a Doha Round agreement on agriculture. The payments are "doubly green" in the sense that they are environmentally beneficial and would be categorized as "green box" payments – on which there are no limits.

Agriculture as Energy Supplier?

The Uruguay Round Agreement on Agriculture was oversold to American farmers. Agricultural economists did a great deal of analysis that showed large potential gains from agricultural policy reform and moving to *free* trade in agricultural products. In reality, despite some conceptual advances in the URAA, virtually no real agricultural trade liberalization resulted. When the anticipated gains failed to materialize and Brazil captured most of

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the growth in the world markets, many farmers became disenchanted with the WTO system and, too, with their ability to compete in export markets. They started casting about for alternative market-growth possibilities.

At the same time, as corn growers were looking for new markets, there was increasing concern about the growing dependence of the United States on imported oil. The resulting interest in renewable sources of energy sparked interest in using corn to make ethanol to blend with gasoline and, more recently, soybean oil to produce bio-diesel fuel. Even with today's high oil prices, this industry seems to be at best marginally profitable – requiring construction subsidies and mandated minimum use in gasoline/diesel blends – and then only with protection against imports from lower-cost suppliers, such as ethanol from sugar cane and bio-diesel from palm oil.

The petroleum companies, which control access to the service-station pumps and have deeper pockets to make political campaign contributions, oppose minimum-use mandates. Nevertheless, they did not have the political clout to stop the minimum-use mandate in the 2005 Energy Bill. Using corn and soybeans for renewable energy is extremely popular with the United States farm organizations and they can be counted on to advocate a yet larger role for agriculture in renewable fuels in the 2007 Farm Bill. Most farm organizations are currently more interested in this than in agricultural trade liberalization.

WORLD TRADE ORGANIZATION

There are two channels through which the WTO may affect the 2007 Farm Bill: the Doha Round negotiations and the recent loss in a case brought by Brazil against the U.S. cotton program. Before addressing either of these specifically, it is useful to review what the WTO is and what it isn't. There is such a vast amount of misinformation swirling through the media that we need to have a clear understanding of the institution before looking into how it may affect the 2007 Farm Bill.

The WTO is a voluntary association of 148 countries that, like the GATT forum before it, periodically conducts rounds of multilateral negotiations aimed at liberalizing international trade and reviewing and revising the "rules of the road" in the multilateral trading system. Decisions are taken by consensus among all participants. The WTO system has a Secretariat, located in Geneva, Switzerland, which organizes and staffs the meetings, reviews the trade policies of member countries (the Trade Policy Review Mechanism) and administers a dispute-settlement process to resolve differences among members over whether its internationally agreed rules are being broken.

When a case is brought by one country against another, a "dispute-settlement panel" is appointed, which functions as "a

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court of first instance” in trade disputes. If any party to a case is dissatisfied with the panel’s ruling, it can appeal the decision to the WTO’s Appellate Body, which, in effect, serves as the “supreme court of international trade”. The panels and the Appellate Body build up a body of case law which interprets and clarifies trade agreements. In past rounds, negotiators have often found it necessary to use fuzzy language to reach closure, allowing each party to declare victory on returning home. The cost of this is that panels and the Appellate Body may reach interpretations at odds with what the negotiators themselves thought they had agreed.

Perhaps the most widespread misunderstanding about the WTO is that it cannot make any country change its policies. But if a country that loses a case refuses to change the policy found to be in violation of an internationally agreed rule, the WTO can authorize the victims of the violation (i.e. the country that won the case) to collect a specified amount of compensation by levying import duties on the violator’s exports to that country. The goods on which the duties are levied need have no relationship to the sector found to have been hurt by the violation. This often leads to targeting with duties those goods produced by politically powerful non-agricultural sectors in order to get them to bring pressure on their governments to change the offending agricultural measure.

WTO Cotton Case

In February 2003, Brazil filed a case with the WTO against the United States, alleging that the U.S. cotton program violated the Uruguay Round Agreement on Agriculture, of which the United States was not only a signatory but also a principal author. (Brazil, along with Australia and Thailand, also brought a successful case against the other principal author of the URAA, the European Union, alleging that its sugar program violated that agreement.)

Brazil alleged that the various subsidies in U.S. cotton policy stimulated larger production and exports of cotton than would have been the case in the absence of those subsidies. Brazil further alleged that the additional exports depressed the world price of cotton, reducing the earnings of Brazilian cotton producers, who get their entire income from the marketplace. Brazil demanded that the United States change its cotton program to remove the offending subsidies or pay it damages.

When each country filed its new tariff schedule with the WTO following the Uruguay Round agreements, it was required to itemize those commodities for which export subsidies were being provided. The United States’ filing did not list cotton (or soybeans). Therefore, the ruling mandated that the Step 2 cotton payments, as well as export credit guarantees in excess of normal commercial terms, which it also found to be export subsidies,

should be changed by July 1, 2005. On July 1, 2005, the USDA administratively changed its export credit program to eliminate the offending subsidy element. To eliminate the Step 2 program requires Congressional action. On July 5, 2005, the USDA sent a request for its repeal to the Congress. The cotton industry has lobbied the Congressional agriculture committees hard not to eliminate the Step 2 program during the current marketing year. No date certain was specified by which the United States should change the other offending policies. Whether the "fix" can wait until the 2007 Farm Bill or the outcome of the Doha Round negotiations will be decided in talks between Brazil and the United States. It should be noted, however, that the United States cannot claim any "credit" in the Doha Round negotiations for changes it makes in policies that a WTO panel found to be in violation of the existing WTO agreement.

Fruit and Vegetable Exclusion

The WTO panel and Appellate Body made one other quite unanticipated ruling in the cotton case. When set-aside programs were designed, the fruit and vegetable industry (especially the California and Florida growers) lobbied successfully for a ban on the subsidy recipients growing fruits and vegetables on set-aside land. They argued that, if producers of program commodities planted set-aside land to fruits and vegetables, this would likely depress the prices of fruits and vegetables to the primary growers of those commodities who get their entire income from the marketplace. This fruit-and-vegetable exclusion rolled forward into the U.S. rules on direct payments.

The WTO cotton panel, which ruled that the United States direct payments had not contributed to the larger production and exports that had depressed the world cotton price, found that those direct payments did not meet the URAA definition of decoupled payments. To be decoupled, the definition – which the United States substantially wrote – requires that there should be no restrictions on what the payment-receiving producer grows (or doesn't grow). The fruit-and-vegetable exclusion violates the URAA definition. The panel concluded that the direct payments, therefore, should have been included in the total trade-distorting (the amber box) subsidies reported by the United States to the WTO and, if they had been, the United States would also have been in violation of the AMS cap on such support to which it had agreed in the Uruguay Round negotiations.

Doha Round of Agricultural Trade Negotiations

In July 2002, the United States submitted to the WTO an ambitious proposal for agricultural trade reform in the Doha Round negotiations, which was reiterated by President Bush at the Gleneagles G-8 Summit in early July 2005. The proposal stated

The next milestone in the Doha Round negotiations is the WTO Ministerial Conference in Hong Kong this December.

Negotiations have moved at a glacial pace because the negotiators have not had authority from their capitals to strike compromises, especially on agriculture, over which there are deep-seated differences not only between developed and developing countries but also among the members of the two groups.

Just think of the differences among Canada, the European Union, Japan and the United States.

In the Framework Agreement on Agriculture – part of the “July 2004 Package” – the negotiators agreed that each high-income country should make a “substantial reduction in the overall level of its trade-distorting support from bound levels”, with the highest levels of support being reduced the most.

In the U.S. case this would entail more than proportional reductions in commodity-specific support for rice, cotton, sugar, dairy, and peanuts.

that the United States is prepared to undertake significant reform of its domestic agricultural policies in exchange for significant increases in market access for U.S. agricultural products abroad.

After more than two years of little progress in the negotiations, the WTO General Council reached on August 1, 2004,¹⁴ a package of “framework agreements” (*without* modalities), known as the “July 2004 Package”, which promised to move the process forward. The Framework Agreement on Agriculture was substantially less ambitious than the initial proposal made by the United States, but it contained many provisions that the United States had proposed. The July 2004 Package left a lot of details to be resolved not only in the agriculture negotiations but also in those dealing with manufacturing and services, as well as WTO rules – covering subsidy-countervailing measures, anti-dumping actions, regional trade arrangements and development matters (such as special-and-differential treatment).

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There was some hope that an informal mini-ministerial meeting in Dalian, China, in July 2004 would impart renewed momentum to the process, but no agreement was reached before the negotiators left Geneva for their August 2005 recess. It is urgent that negotiators resolve most of the open issues between September and December so that few remain to be resolved at ministerial level in Hong Kong. If the modalities of an agreement can be defined by December, then the negotiators should be able to settle the specific details in each country’s bilateral requests and offers during 2006.

Before discussing the specific aspects of the WTO Framework Agreement on Agriculture – part of the July 2004 Package and referred to hereafter as the “Framework Agreement” – that have a bearing on the 2007 Farm Bill, one other point should be clarified. As in U.S. federal budgeting, a “cut” does not necessarily imply a reduction. It is essential to pay attention to what is the baseline from which “cuts” are to be made. This is particularly important with respect to agreed reductions in tariffs and trade-distorting domestic support. Many countries apply lower tariffs than the maximum rates they agreed to bind (“bound rates”) in the last round of trade negotiations. The difference between bound rates and “applied rates” is often referred to as “water” in the tariffs. When there is a lot of water in tariffs, it takes a very substantial

In response to insistence from the most protectionist agricultural importers – such as Japan, South Korea, Norway and Switzerland – the Framework Agreement provides an escape clause with respect to the principle that the highest tariffs should be reduced the most.

The Framework would allow all countries to designate an “appropriate number” of “sensitive products” to which the tariff-reduction formula will not apply.

The sensitive-product loophole provides a possible way for the most politically powerful commodities, which enjoy the largest subsidies and highest rates of import protection, to avoid as large reductions in tariff rates as other products.

reduction in a bound tariff before there is any reduction in the applied tariff, resulting in an actual increase in market access.

Similarly, in high-income countries the bound AMSs – the aggregate measurements of trade-distorting support – are in general higher than the total actual support provided. So, while the Framework Agreement calls for a 20 percent reduction in total trade-distorting domestic support in the first year of implementation of a Doha Round agreement on agriculture, this would require neither the United States nor the European Union to make any actual reductions. In both cases there is more than 20 percent unused capacity in their AMSs and the new lower maximum AMS would still exceed the levels that the United States and the European Union have been providing to their farmers.

(a) Domestic Support

In the Framework Agreement the negotiators agreed that each high-income country should make a “substantial reduction in the overall level of its trade-distorting support from bound levels”, with the highest levels of support being reduced the most. In the U.S. case this would entail more than proportional reductions in commodity-specific support for rice, cotton, sugar, dairy and peanuts. Product-specific AMS caps on support would be imposed in addition to the binding on the aggregate support provided to the agricultural sector. The size of these caps and what is meant by “substantial reduction” remain to be defined in the negotiations.

In the Framework Agreement, U.S. negotiators obtained agreement to broaden the definition of the blue box beyond policies that, while providing production- and trade-distorting support, also entail an offsetting supply constraint such as a marketing quota or a land set-aside provision. The broadened definition would also include “direct payments that do not require production” so that the United States could include its counter-cyclical payments in the blue box. Counter-cyclical payments do not qualify for inclusion in the green box because, while there is no link to the current volume of production, the payment is based on the current market price. In the URAA there was no cap on blue-box payments; in the Framework Agreement, blue-box payments (as redefined) are capped at less than 5 percent of a country’s total value of agricultural production (i.e., all commodities, not just those for which there are farm programs).

During the remaining negotiations there will probably be a further tightening of the definition of blue-box payments to ensure that such policies are less trade-distorting than the amber-box payments. There is widespread unhappiness in other countries with the redefinition of the blue box; and we can anticipate continued attempts to tighten the criteria as much as possible in the remainder of the negotiations.

It is widely recognized that high-income countries tend to be most protectionist in the sectors where low-income countries have a comparative advantage, particularly in labor-intensive manufactures and certain agricultural products that thrive in the tropics, such as sugar, cotton and rice.

The Framework Agreement would leave green-box payments unrestricted, but there is likely to be some further tightening of the green-box criteria to ensure that the support categorized there really is minimally trade-distorting in practice. Since the signing of the URAA, the United States, the European Union and Japan have made substantial shifts in agricultural subsidies from the amber-box category to specific commodities to direct (decoupled) payments. But there is a widespread perception in other countries that such large green-box payments cannot possibly be production- and trade-neutral.¹⁵

Particularly noteworthy in the Framework Agreement is a proposal to create a new cap on the sum of amber-box plus blue-box product-specific *de minimus* subsidies in place of the current AMS cap on the amber box. This would substantially *increase* the maximum allowable trade-distorting subsidies – in the United States to 250 percent of current spending and in the European Union to 170 percent of its current spending. If this proposed change is made, a reduction of 60 percent in this redefined cap would be required in U.S. farm-program payments before any actual reduction would occur.¹⁶

(b) Export Subsidies

The Framework Agreement contains a commitment to eliminate all export subsidies by a date yet to be determined. The elimination of direct export subsidies affects mainly the European Union. But to obtain its commitment on this issue, other countries will have to agree to discipline policies they employ that have an effect equivalent to an export subsidy. In the case of the United States, this involves subsidized export credits and export credit guarantees with a repayment period beyond normal commercial terms (180 days). (This issue was also flagged by the WTO cotton panel.) The United States also provides part of its food aid on other than a fully grant basis. For example, food aid is provided to private voluntary organizations and non-governmental organizations (NGOs), which sell the products in the recipient country markets in order to generate local currency that is used to support their development and humanitarian activities. While much good undoubtedly comes from these activities, it is hard to argue that they do not displace commercial sales (either from local farmers and/or commercial import suppliers).

Accepting greater discipline in these areas would be a small price for the United States to pay for a complete ban on agricultural export subsidies, which have caused significant distortions in world commodity markets. Parenthetically, eliminating export subsidies will force the European Union to make larger reforms in its domestic agricultural policies. For example, despite its milk marketing quotas, the European Union still has to buy dairy products (“intervention”) to support the internal price of milk. It gets rid of these “intervention stocks” by subsidizing their sale on the world market.

The European Union and the United States produced a proposal just before the WTO Ministerial Conference in Cancun in September 2003. But the document was seen to be so self-serving that it precipitated the emergence of an unlikely group of twenty odd developing countries led by Brazil and including India, China, South Africa and other agricultural-exporting developing countries.

The Group coalesced as the Group of 20 and has been an effective counter-weight to the European Union and the United States in the negotiations – ending the era when the two “majors” could go behind closed doors to hammer out the terms of a deal.

(c) Market Access

Market access, the most important of the three pillars in liberalizing trade, is the least well defined in the Framework Agreement. Beyond a general agreement that the highest tariffs should be reduced the most and that the negotiated reductions will be bound, not applied, tariff rates, not much has been agreed. Because there is so much “water” in tariff rates, in many cases it would take a substantial reduction in bound tariffs – more than 70 percent according to some studies – to bring about any reduction in applied rates and achieve, in turn, an increase in actual imports.

Moreover, in response to insistence from the most protectionist agricultural importers – such as Japan, South Korea, Norway and Switzerland – the Framework Agreement provides an escape clause with respect to the principle that the highest tariffs should be reduced the most. The Framework would allow all countries to designate an “appropriate number” of “sensitive products” to which the tariff-reduction formula will not apply. In exchange for a smaller tariff reduction on sensitive products, however, the Framework suggests that the minimum market access for the “sensitive products” be increased, but many details remain to be negotiated.

In many instances, tariff-rate quotas (TRQs) constrain access to highly protected markets. A relatively low tariff rate is charged on imports that enter within the quota, but a much higher, often prohibitively high, tariff is charged on imports in excess of the tariff-rate quota. For example, the United States maintains tariff-rate quotas for sugar, dairy, cotton, peanuts, tobacco and beef. In the cases of beef, sugar and butter, the United States would have to reduce its import tariffs by 77, 38 and 19 percent, respectively, before any increase in imports would occur.¹⁷

The sensitive-product loophole provides a possible way for the most politically powerful commodities, which enjoy the largest subsidies and highest rates of import protection, to avoid as large reductions in tariff rates as other products. Nevertheless, those commodities should anticipate having to allow foreign suppliers to compete for a larger fraction of domestic consumption. Larger imports might be enough to force more change in those commodities’ domestic farm programs.

(d) Developing-country Issues

There is another important way in which the Doha Round negotiations are likely to affect the 2007 Farm Bill. It relates to the strong development focus to the negotiations – dubbed the Doha Development Agenda. There are several reasons for this. One was that the WTO Ministerial Conference in Doha in November 9-13, 2001, which launched the negotiations, was exactly two months after the September 11 terrorist attacks in the United

States. Global poverty and the extent to which it facilitates recruitment by extremists were very much on delegates' minds.

Trade is widely acknowledged to be a powerful engine of economic growth, more so than financial aid. It was widely recognized that high-income countries tend to be most protectionist in the sectors where low-income countries have a comparative advantage, particularly in labor-intensive manufactures and certain agricultural products that thrive in the tropics, e.g. sugar, cotton and rice. It is also acknowledged that developing countries have gained little from previous rounds of multilateral trade negotiations and now that they represent the overwhelming majority of WTO members, there will be no overall Doha Round agreement until and unless they believe there will be a clear benefit in it for them.

Between 2001 and 2003, numerous proposals were introduced by individual countries and coalitions of countries, including several from groups of low-income countries, but little progress was made in the negotiations. Several attempts at outlining a framework for an agricultural agreement were made, but without success. In August 2003, in an attempt to advance the agricultural negotiations, the other members asked the European Union and the United States to advance a proposal that would be satisfactory to both of them.

The World Bank released estimates that the world market price of rice is depressed by 33-50 percent, sugar and dairy-products prices were 20-40 percent and for cotton and peanuts 10-20 percent relative to the level at which it would otherwise reside.

The European Union and the United States produced, following a mini-ministerial meeting in Montreal, a proposal just before the WTO Ministerial Conference in Cancun in September 2003, but the document was seen to be so self-serving (with neither having to make many concessions), and so out of keeping with the development spirit of the round that it precipitated the emergence of an unlikely group of twenty odd developing countries led by Brazil and including India, China, South Africa and other agricultural-exporting developing countries. The group coalesced as the Group of Twenty (G-20) and has been an effective counter-weight to the European Union and the United States in the negotiations – ending the era when the two “majors” could go behind closed doors to hammer out the terms of a deal. Unless the G-20 perceives the deal to be worthwhile to them there will be no deal.¹⁸

In the run-up to the Cancun ministerial meeting, Oxfam and other NGOs waged a high-profile publicity campaign against high-income countries' subsidies to agriculture. They focused on the adverse effects of subsidies that drive down world market prices and, hence, drive down the incomes of poor farmers in low-income countries who get their entire income from the market. Just before the Cancun ministerial the World Bank released estimates of the price-depressing effect in world markets of high-income countries' agricultural subsidies and protectionism. The World Bank analysts estimated that the world market price of rice is depressed by 33-50 percent relative to the level at which it would otherwise reside.¹⁹ The Bank's estimates for sugar and dairy-

product prices were 20-40 percent; and for cotton and peanuts, 10-20 percent.

Oxfam had built its campaign around U.S. cotton subsidies and how they hurt low-income cotton producers in four of the poorest countries in West Africa.²⁰ The campaign had been so effective that when delegates arrived in Cancun, cotton – specifically the U.S. cotton program – was on everyone’s mind. The U.S. negotiators were in an impossible situation, caught between one of the most powerful lobbies in Washington and virtually all the other delegations. When the United States advanced a proposal that assistance be provided to the West African countries – which have a lower cost of production – to help their farmers diversify out of cotton, the anger at the United States was palpable and the stage was set for the Cancun ministerial meeting to fail.²¹

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Because agriculture is so important in the economies of most low-income countries, it is viewed as *the* make-or-break issue in the Doha Round negotiations. The United States has said that it would reduce its trade-distorting agricultural subsidies if other countries will reduce tariffs and increase quotas to provide greater market access. The developing countries say they cannot open their borders to products whose world market prices are artificially depressed by the subsidies that high-income countries provide to their producers. The developing countries say, in effect, the high-income countries have to go first. The United States responds that it cannot sell subsidy reductions to the Congress without significant market opening abroad, including in developing countries. This led to a stalemate in the agricultural negotiations for more than a year up until the July 2004 Package and the issue continues to thwart progress.

There has been a practice in multilateral trade negotiations since the 1970s to allow developing countries special-and-differential treatment (S&DT), which translates into smaller reductions in protection, phased over a longer transition period. That this will once again be the case was confirmed in the July 2004 Package. U.S. agricultural interests have expressed significant concern about one aspect of S&DT. Most interests other than sugar have little argument with the 49 least-developed countries receiving special treatment. In the WTO, however, the next higher income category of countries, the “developing countries”, is a self-designating category and some countries’ self-designation seems to stretch the definition. Singapore and South Korea, for example, see themselves as developing countries. Moreover, there is a problem with certain countries that have highly competitive export sectors, but regional concentrations of poverty, like Brazil in soybeans and China in labor-intensive manufactured goods. This is a highly political issue in the WTO, but U.S. agricultural organizations are unlikely to go along with a Doha Round agreement in which they see their prime competitor, Brazil, claiming special privileges because it declares itself to be a developing country.

It is in the United States' economic self-interest for this to be a successful "development round". The (almost) three billion people to be added to the world's population in the first half of the twenty-first century, plus the three billion people (almost half the world's current population) who live on less than two dollars a day, are the only potential growth market for world agriculture. But their needs will be translated into market demand only if they experience broad-based economic growth that empowers them with the necessary purchasing power. Because many countries, especially in Asia, have a much larger fraction of the world's population than of the world's arable land, the growth in their food demand will quickly outstrip their production capacity and, consequently, they will need to import a larger part of their food supply. This will only happen, though, if they can export products in which they have a comparative advantage to earn the foreign exchange needed to buy goods, including part of their food supply, in which other countries have a comparative advantage.

Prospects for Reform

The 2007 Farm Bill and the Doha Round negotiations are progressing on the same timetable. Mike Johanns, the U.S. Secretary of Agriculture, began holding "listening sessions" on the 2007 Farm Bill around the country during the summer of 2005. The Congressional agriculture committees' "field hearings" will start in the fall of 2005, with hearings in Washington, DC, continuing through 2006, in anticipation of writing the next farm bill during 2007. The most likely time for the Doha Round negotiations to conclude is June 2007, when the current U.S. trade-negotiating authority expires. If history is any guide, this will be an effective decision-forcing date to bring the WTO negotiations to closure. Any changes in farm policy agreed in the Doha Round agreement on agriculture can then be implemented in the 2007 Farm Bill.

Within U.S. farm organizations there is little enthusiasm for trade negotiations or even for exports in general. Many American farmers are taking a defeatist attitude about their ability to compete internationally. They see the world market as a "zero sum game" and are betting their future on ethanol and bio-diesel instead. Unless farm organizations enthusiastically embrace whatever is coming out of the Doha Round negotiations, don't expect the Congressional agriculture committees to do so.

Many farm organizations and commodity groups organized task groups to work on future farm-policy options already in 2004. Their leaderships appear to believe that the probability of a binding budget constraint in 2007 is sufficiently high that they need to analyze other possibilities. Nevertheless, most farm organizations' first priority seems to be to preserve intact everything they got in the 2002 Farm Bill. There is likely to be a continuing stream of anti-farm program editorials in U.S. newspapers, but both political parties may view rural America as

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There are a number of other domestic issues that will influence the 2007 Farm Bill. Agricultural commodity programs are now acknowledged to be weak rural development policy. Will a coalition emerge that can secure support for investments in rural infrastructure, e.g. broadband internet and public goods such as education that are essential for successful rural development?

Many farmers perceive that the pendulum has swung too far in relying on the private sector for future agricultural technologies. Will the farm organizations that represent them be willing to support shifting some funds from commodity programs to public support for agricultural research?

Another issue that will play into the 2007 Farm Bill debate is the increasing size of farms and concentration in the agricultural marketing and input sectors. This will be manifested, among other ways, in advocacy for limits on the size of farm-program payments any one producer can receive. To be effective, payment limitations will have to constrain how many times a "farm" can be carved into smaller units, each of which can receive the payment limit.

Subsidized crop insurance and disaster payments have a tendency to induce larger production of certain crops in areas where there are sub-optimal growing conditions (higher risk) for those crops. Over the years Congress has regularly undermined the viability of the crop insurance program by providing disaster payments to farmers in bad crop years. Some farm organizations are studying alternative forms that a gross revenue assurance program could take to replace disaster payments, crop insurance, marketing loans, loan deficiency payments and counter-cyclical payments. This willingness of leaders of farm organizations to look at radical alternatives to present farm programs is encouraging for WTO prospects.

Every farm bill is influenced disproportionately by the current economic conditions in the farm sector and agricultural commodity markets *at the time* the farm bill is written. While no one can predict how crop conditions here and around the world will evolve between now and 2007, we can predict with some assurance that whatever they are will affect the content of the 2007 Farm Bill. The role government payments are playing in farmers' incomes in 2007 will also affect the outcome, but the direction of its influence is difficult to predict. If government programs are supplying a significant fraction of net farm income, farm organizations will lobby hard to keep what they are getting. On the other hand, if there should be a big jump in the magnitude of payments from 2004 to 2005²² (as can be seen in Table 6), budget hawks are likely to attack, demanding reductions.



The **mockingbird** is the state bird of Tennessee. Cordell Hull represented a district of Tennessee in the

Congress of the United States, and was elected a senator from there, before becoming U.S. Secretary of State (1933-44).

"The mockingbird is known for fighting for the protection of his home – falling, if need be, in its defense. Mockingbirds are not intimidated by animals larger than themselves and have been known to attack eagles"

– Diana Wells, *100 Birds and How They Got Their Names* (Chapel Hill, NC: Algonquin, 2002)

Trade Policy Analyses

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If one had to predict, the safest bet would be that the commodity programs in the 2007 Farm Bill will not look a lot different from those at present. With the definition of the special products and sensitive products, and the redefinition of the blue box to include counter-cyclical payments in the Framework Agreement, there is a significant possibility that the Doha Round negotiations will end with a minimalist agreement in agriculture that requires little change in U.S. farm programs. Based on their behavior in past rounds of multilateral trade negotiations, the United States and the European Union would probably go along with this.

Table 6: Role of Government Payments in U.S. Farm Income, 2001-2005

	2001	2002	2003	2004 (est)	2005 (est)
Total Cash Receipts	200	195	212	235	222
Net Cash Income	60	51	69	78	78
Net Farm Income	51	37	59	74	64
Total Government Payment	21	11	16	14	21

Source: Economic Research Service, U.S. Department of Agriculture, Washington, DC.

Agriculture, however, is central to the interests of least-developed and developing countries, which make up the majority of WTO members. The least-developed countries might be appeased with tariff preferences and special-and-differential treatment, but the G-20, led by Brazil, is likely to take the attitude that a bad agreement is worse than no agreement and they will view as a bad agreement any agreement that does little to reform agriculture. There will be no agreement until both the least-developed and the developing countries perceive there to be something of value in it for them. The ingredients are in place for at least one more high-profile failure at a WTO ministerial gathering. Finally, in the light of the difficulty the Bush Administration had in securing Congressional approval of the CAFTA-DR agreement, other countries' negotiators will doubt that the U.S. negotiators can deliver Congressional approval of any significant agricultural policy reforms to which they might agree in the Doha Round negotiations.

A betting person would have to wager that the 2007 Farm Bill will look a lot like to 2002 Farm Bill. But there is just enough of a higher likelihood of change – due to the federal budget deficit, the breadth of recognition that the programs are not achieving their stated objectives and the Doha Round negotiations – that some more fundamental change might be possible. Stay tuned.

¹ An earlier version of this paper was presented at the Second Annual North American Agrifood Market Integration Workshop, San Antonio, Texas, May 6, 2005. The author appreciates helpful suggestions from Hugh Corbet and Ann Tutwiler. Work on this paper was supported in part by a grant from the German Marshall Fund of the United States.

² “Farm and Commodity Policy: Government Payments and the Farm Sector”, U.S. Department of Agriculture, Washington, DC. Available at:
<<http://www.ers.usda.gov/Briefing/FarmPolicy/gov-pay.htm>>.

³ “ERS Typology for a Diverse Agricultural Sector”, *Agricultural Information Bulletin*, No. 759 (Washington, DC: U.S. Department of Agriculture, 2000).

⁴ James MacDonald, Robert Hoppe and David Banker, “Growing Farm Size and the Distribution of Commodity Program Payments”, *Amber Waves*, Washington, DC, 2005.

⁵ “What’s the Plan? U.S. Farm Subsidies, 1995 through 2003”, *Farm Subsidies Database*, Environmental Working Group, Washington, DC, 2005. Available at
<<http://www.ewg.org/farm/findings.php>>.

⁶ For a more detailed history, see Bruce L. Gardner, *American Agriculture in the Twentieth Century: How it Flourished and What it Cost* (Cambridge, MA: Harvard University Press, 2002).

⁷ See Clayton Yeutter, “Critical Role of the Cairns Group in the Uruguay Round Negotiations”, in Andrew Stoeckel and Hugh Corbet (eds), *Reason versus Emotion: Requirements for a Successful WTO Round* (Canberra: Rural Industries Research and Development Corporation, 1999).

⁸ Paul C. Wescott, C. Edwin Young and J. Michael Price, “The 2002 Farm Act: Provisions and Implications for Commodity Markets”, *USDA Agriculture Information Bulletin*, U.S. Department of Agriculture, Washington, DC, No. 778, November 2002). Available at:
<<http://www.ers.usda.gov/publications/aib778/aib778.pdf>>.

⁹ The PSE is the percentage of gross farm receipts attributable to government policy, including budgetary transfers financed by taxpayers, as well as the implicit tax on consumers that arises from interventions such as border protection that raise farm prices above the levels that would otherwise prevail.

¹⁰ Michael Gastner, Cosma Shalizi and Mark Newman, “Maps and Cartograms of the 2004 U.S. Presidential Election Results.” See: <www.personal.umich.edu/~mejn/election/countymappedblue.png>.

¹¹ “Farm and Commodity Policy: Government Payments and the Farm Sector,” *op. cit.*

¹² “Agribusiness: Long-Term Contribution Trends”, Center for Responsive Politics Available at:
<<http://www.opensecrets.org/industries/indus.asp?Ind=A>>.

¹³ To paraphrase Gordon Conway’s “doubly green revolution” in his book, *The Doubly Green Revolution: Food for All in the Twenty-first Century* (London: Penguin Books, 1997).

¹⁴ “Agricultural Negotiations at the WTO: The July Package and Beyond”, *Quarterly Intelligence Report*, No. 12 (Geneva: International Centre for Trade and Sustainable Development, April 2005). Available at: [http://www.agradepolicy.org/output/resource/agriculture negotiations12.pdf](http://www.agradepolicy.org/output/resource/agriculture%20negotiations12.pdf).

¹⁵ There can be little doubt that they induce larger investments in the agricultural sector as a whole relative to other sectors of an economy than would otherwise be the case. The issue here is whether they distort the mix of products produced. Some argue, for example, that in relatively specialized production regions, e.g. rice in Japan, the fact that support formerly distributed to Japanese rice growers via price supports, which it now distributes as direct payments based on historical production patterns, is still supporting rice production.

¹⁶ *Building on the July Framework: Advice and Cautions* (Washington, DC: International Food and Agricultural Trade Policy Council, 2005), available at www.agritrade.org.

¹⁷ Ann Tutwiler, “The July Framework Agreement: Nine Months Later”, International Food and Agricultural Trade Policy Council, Washington, DC, April 2005.

¹⁸ Brazil and other agricultural exporters in the G-20 will insist on real agricultural policy reform in the agreement, but India is less prepared to reform its own policies, and China perceives that it has already conceded enough in its WTO accession negotiations.

¹⁹ *Global Economic Perspectives and the Developing Countries 2003* (Washington, DC: World Bank, 2003), ch. 2.

²⁰ *Finding the Moral Fiber: Why Reform is Urgently Needed for a Fair Cotton Trade*, Briefing Paper No. 69 (Oxford: Oxfam International, 2004). Available at: http://www.oxfam.org.uk/what_we_do/issues/trade/downloads/bp69_cotton.pdf.

²¹ The Cancun Ministerial Conference nominally failed because of disagreement between the high- and low-income countries over whether to address national rules in four new areas on the Doha Round negotiating agenda: “trade facilitation” in customs procedures, investment regulations, competition laws and “transparency” in government procurement, but the United States’ inability to be forthcoming on cotton had already poisoned the well.

²² “ERS Typology for a Diverse Agricultural Sector”, *op. cit.*