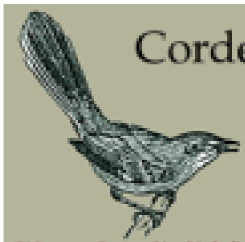

Cordell Hull Institute

Policy Forum

"Informed public opinion is a task of intensive study, hard thinking, broad vision and leadership, not for governments alone but for ... all those who provide spiritual, moral and intellectual guidance"

— CORDELL HULL, radio broadcast in 1944, cited in *Memoirs of Cordell Hull* (1949)

"Listen to the mockingbird..."

Moment of Truth on Liberalizing Agricultural Trade

Summary of a Presentation by

Robert L. Thompson

April 24, 2003

DEVELOPING COUNTRUES are the only potential growth market for agricultural exporters, said Robert Thompson, former Director of Agriculture and Rural Development at the World Bank, at a meeting of the Cordell Hull Institute in Washington on April 24.

That is one reason for the development focus in the Doha Round negotiations, he said, but there are other important reasons why agriculture has to be properly addressed in the negotiations. Apart from it being " the "right thing to do", there are the adverse geo-political effects of persistent poverty and, with developing countries now the majority in the WTO system, there will be no overall agreement until they perceive something of value to them in the negotiations.

World Agriculture in Disarray

Stressing how *World Agriculture is in Disarray* (the title of D. Gale Johnson's seminal work), Dr Thompson pointed out that most high-income countries subsidize their agriculture, which distorts relative returns to various outputs and induces larger total investment in agriculture relative to other sectors.

Many food policies in developing countries, however, turn the terms of trade against agriculture to keep urban food prices low. This reduces the incentive to invest and, as sa result, agriculture under-performs relative to its potential.

"Protectionist import policies and export subsidies further distort what is produced where," said Dr Thompson, chairman of the International Council on Food and Agricultural Trade Policy, based in Washington, DC.

"Farm-support policies are distorting domestic terms of trade in favor of politically powerful commodities," he explained. "Subsidies tied to the output of specific commodities stimulate larger production in less efficient locations.

"Subsidies are justified on the basis of low farm income, but they are distributed in proportion to sales and, in the end, are capitalized in land prices, benefiting large farmers and land owners.

Every year, the Organisation for Economic Cooperation and Development (OECD) assesses the "producer subsidy equivalent" (euphemistically called "producer support estimates) as a percentage of total costs. The assessments are made on both a country and a commodity basis.

In 2001, the figure for Switzerland was 69, while for Japan it was 59; for the European Union, 35. In North America, the figure for the United States was 21, for Mexico it was 19 and for Canada it was 17. These figures compare with 4 for Australia and 1 for New Zealand!

On a commodity basis, the producer subsidy equivalent in OECD countries in 2001 was 81 for rice, 45 for sugar, the same for milk, 36 for wheat, the same for beef and veal, 29 for corn, 28 for oilseeds and 6 for wool.

Agriculture's Role in Development

In low-income countries, agriculture is the largest sector in the gross domestic product, employment, export earnings and poverty. The employment multiplier is larger in agriculture than in manufacturing industry and so the failure to develop agriculture impedes national economic growth. Food is the largest item of expenditure in poor households.

Whereas development advocates often deplore the movement of people from rural to urban areas, Dr Thompson pointed out that "out-migration to non-farm employment, part-time or full-time, in far away cities and rural areas is a normal and necessary part of economic development".

Dr Thompson dwelt on how the policies of developing countries impede their agricultural development, resulting in a lack of technology adapted to local agro-ecological conditions (soils, climate, slopes). Cheap food policies keep urban consumers quiescent – often reinforced by food aid or subsidized (dumped) exports from OECD countries.

Current developing-country policies result in under-investment in Green Box measures, such as rural infrastructure and agricultural research. Lack of definition or enforcement of property rights and contract sanctity also undermines investment, as does corruption and/or macro-economic instability.

Effects of the Trade Environment

OECD protectionist barriers to developing-country goods reduces their foreign-exchange earning capacity and economic growth. Furthermore, OECD agricultural production and export subsidies depress world market prices below the long-term trend and increase variance around that trend. What's more, food aid is most available in years of OECD surplus, not in periods of developing-country deficit.

"Developing countries haven't got much out of past agricultural trade agreements," Dr Thompson concluded.

On how the Farm Act of 2002 hurts the interests of developing countries, Dr Thompson said: "Larger U.S. production depresses world market prices and in turn reduces the prices and revenue of developing-country producers, as with West African cotton.

Counter-cyclical payments, by smoothing expected returns, reduce the response by U.S. farmers to changes in prices. This forces adjustment onto the world market, increasing the volatility of "world" market prices.

Larger U.S. sugar production means less sugar imports from developing countries, which enjoy a comparative advantage in sugar production. Large food-aid shipments can, as mentioned, undercut developing-country farm prices.

"The net effect," Dr Thomson said, "is slower reduction in developing-country poverty and slower growth in this large potential export market."

Uruguay Round Achievements

In the preparations for the Uruguay Round negotiations, Dr Thomson was the U.S. Assistant Secretary of Agriculture for Economics. The agreement on agriculture reached in the negotiations, he said: (i) increased market access as a percentage of consumption, (ii) reduced export subsidies in terms of value and volume, (iii) converted all non-tariff barriers to tariffs and (iv) required a scientific basis for all sanitary and phyto-sanitary (SPS) barriers to trade.

Moreover, the agreement acknowledged that some domestic agricultural subsidies can distort trade and categorized them by degree of trade distortion:

- "Green box" = non-trade-distorting investments in public goods and decoupled income transfers;
- "Amber box" = trade-distorting (bound and reduced); and
- "Blue box" = trade-distorting, but offset by production controls or set-asides.

Thus the Uruguay Round negotiations brought agriculture under internationally agree trade rules. They established a useful framework in which to liberalize agricultural trade. But they did little to open markets and they contained a lot of loopholes.

“The Doha Round negotiations can and must be more ambitious,” Dr Thompson said. “In particular, the framework needs stronger controls and tighter disciplines.”

Obstacles and Opportunities

On the obstacles to progress, Dr Thompson said there is a lack of leadership at international level, the timing is too constrained, the bilateral and regional approach to trade liberalization is undermining the multilateral approach, there is not enough external pressures on the United States, the European Union and Japan and there are too many major areas of disagreement

On the other hand there are opportunities, Dr Thompson said. “Areas of agreement are emerging. The United States and the European Union are coming under pressure to re-engage internationally, U.S. farmers are reassessing budget outlook and there are internal pressures for reform in Europe and Japan.”

Abdication of U.S. Leadership

Unfortunately in the Farm Act of 2002, the United States abdicated leadership, Dr Thompson said, increasing agricultural subsidies while telling the world to cut them. “The United States, which has led global effort of “decouple” payment from production, appears two-faced,” he added.

“By allowing bases to be updated, farmers know that ‘fixed payments’ are not necessarily ‘fixed’. Marketing loans appear to have effect of export subsidies, as do some of our food aid and export credits. U.S. farmers have lost their enthusiasm for trade liberalization, appearing happy to live off government checks.”

Dr Thomson set out what he thought should be the objectives in the Doha Round negotiations:

- *Improve Market Access*: Expand minimum market-access quotas every year. Establish a maximum tariff rate, reduce all tariff peaks to the agreed maximum immediately, require minimum tariff cust per product and an average tariff cut over tariff chapters. And eliminate in-quota tariffs immediately.

- *Geographical Indications and SPS Barriers*: It is premature to extend geographic indications to foods. WTO should assess costs and benefits of GI’s to developing countries. The SPS agreement should not be reopened or reinterpreted.

- *Non-trade Concerns*: It is not WTO's role to question policy rationales, but to discipline policies. Non-trade concerns are best addressed through Green Box measures. If specific commodity support or on-going subsidies are needed, classify them as Amber Box.

- *Protect Importers' Concerns:* Ban export embargoes and restrictions. Institute a transparent safeguard mechanism with bound triggers and time-limits for developing as well as developed countries. Update the base for national consumption to more recent period.

- *Cut Trade Distorting Support*: Reclassify trade-distorting Green Box payments to Amber Box. Reduce Amber Box, Blue Box and product specific support. Make reductions commodity by commodity.

- *Discipline Export "Competition"*: Eliminate export subsidies by a date certain. Discipline export credits, food aid and state trading entities. Reduce and harmonize export taxes.

- *Developing-country Provisions*: Expand Green Box investments now (e.g. through foreign aid) to strengthen developing-country agriculture. Allow developing countries smaller tariff cuts, but on the same timetable as the rest of world. Eliminate tariffs for developing countries and also quotas for the poorest countries. Transform special preferences into general preferences.

Growing World Agricultural Trade

Dr Thompson summed up the situation thus:

The world's arable land is not distributed around in the world in the same proportions as its population. Agriculture in most developing countries is under-performing relative to its potential, thereby slowing national growth.

With population growth and urbanization in developing countries, a larger fraction of world food production is expected to move through world trade. Broad-based economic development in poor countries will accentuate this via growing commercial trade.

Greater trading opportunities will accelerate the rate of national economic growth and create larger market opportunities for exporters in high-income countries.

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