

**MULTILATERAL TRADE
NEGOTIATIONS
THE URUGUAY ROUND**

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Group of Negotiations on Goods (GATT)
Negotiating Group on Agriculture

SUMMARY OF STUDIES ON PROBLEMS AFFECTING TRADE
IN AGRICULTURE AND THEIR CAUSES

Note by the Secretariat

1. At the Group's first meeting from 16-18 February 1987 the secretariat was requested to prepare a brief summary of the studies undertaken in recent years by selected international organisations and other bodies on the problems affecting trade in agriculture and their causes.

2. In accordance with this instruction the secretariat has reviewed the following studies, of which brief summaries are attached:

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| World Bank | - "World Development Report 1986
Trade Pricing Policies in World Agriculture" |
| FAO | - "Impact on World Food Security of Agricultural
Policies in Industrialised Countries" (1987)
(CFS87/3) |
| Trilateral Commission
(authors Johnson,
Hemmi & Lardinois) | - "Agricultural Policy and Trade; Adjusting
Domestic Programmes in an International
Framework" (1985) |
| Department of Primary
Industry, Australia
(G. Miller) | - "The Political Economy of International
Agricultural Policy Reform" (1986) |
| US Department of
Agriculture | - "Government Intervention in Agriculture -
Measurement, Evaluation and Implications for
Trade Negotiations" (1987) |

Other studies can of course be included at the request of the Group. Work by other international organizations which is not yet de-restricted will be summarized as soon as possible.

3. The studies reviewed all reached broadly similar conclusions about the nature of the problems and their causes. Central to their analysis were the effects on trade of domestic agricultural policies, particularly in industrial countries. Failure in the past to give proper recognition to this linkage, especially in the GATT, and to negotiate limits on its operation, was generally identified as an important cause of the present crisis in agricultural trade.

Title: World Development Report 1986 - Trade and Pricing Policies in World Agriculture

Author: World Bank

4. The World Bank Report is the latest in an annual series dealing with development issues in the framework of trends in the world economy. It addresses the problems of agricultural trade in terms of macro-economic growth and efficiency, with emphasis on the interests of developing countries. Rather than being based on a specific mandate or investigation, it is a survey and synthesis of recent research from a large number of sources, concerning which it contains an extensive bibliography.

5. Looking at agricultural trade overall, the study notes depressed world prices for agricultural commodities and distorted price relativities among them. The instability of agricultural commodity markets has been increasing and supply/demand relationships becoming more disturbed. The balance of agricultural trade has shifted sharply against developing countries, with the bulk of food exports coming from high-cost industrial countries and the bulk of imports going to low-cost developing countries. The World Bank lists and discusses the policy measures through which industrial countries (in particular) have increasingly restricted and/or subsidized agricultural trade. These, it says, constitute a fundamental policy problem for the international community. Limitation of their export opportunities by import barriers and subsidized competition is a serious impediment to economic growth in developing countries. For the industrial countries, the problems are the high costs of present policies, their economic inefficiency, and the need to counter excessive production while maintaining farm income at politically acceptable levels. Attempts so far to deal with the imbalance of agricultural trade have mainly been palliatives rather than reforms. Some, like commodity agreements, have been ineffective; others, like special preferences for LDCs, and food aid, can in fact increase trade distortions.

6. The study concludes that, broadly speaking, developing countries discriminate against their agricultural sector and industrial countries discriminate in favour of theirs. The bias against agriculture in developing countries is exacerbated by the high levels of protection in the industrial ones. Policies which have held back agricultural growth in developing countries include overvalued exchange rates and discriminatory taxes. The industrial countries have increased their array of trade-distorting measures (using the relatively simple yardstick of Nominal Protection coefficients the World Bank shows how protection has increased since the 1950s) to protect domestic agricultural policies which generate

high-cost surplus production and subsidized exports. The World Bank dismisses justifications for agricultural protection based on concepts like self-sufficiency, and (drawing on recent studies) makes a case for the overall economic gains from liberalization. However, ad hoc modification of national policies is not enough - in looking ahead to the new GATT round the study concludes that governments must be willing to negotiate about the trade effects of their domestic programmes. Developing countries, too, could benefit by negotiating the liberalization of some of their own restrictive policies.

Title: Impact on World Food Security of Agricultural Policies in Industrialized Countries (Doc: CFS 87/3)

Author: FAO

7. This document underlines the fundamental importance of more liberal agricultural policies in industrialized countries which have an influence on developments in world agricultural trade for the welfare and food security needs of developing countries. It reviews the rôle of government intervention in the transformation and modernization of the agricultural sector in industrialized countries. In these countries, consumers have been guaranteed regular food supplies and have often been unaffected by price fluctuations in world markets. Farmers have responded to the government support by adopting productivity innovations; their incomes have generally improved, although there have been serious setbacks in some countries in recent years. But, at the same time, agricultural support policies have become very expensive and have created powerful vested interests, making the termination or reform of these policies politically difficult. Producers have been increasingly isolated from the underlying market trends and surpluses have been generated in many agricultural commodities, while final costs of open-ended producer subsidies have escalated far beyond expectations.

8. The adverse effects of industrialized countries' agricultural policies on the agricultural sectors of other agricultural exporting countries have also been numerous. The document lists the following: (i) agricultural imports in those industrialized countries that support domestic production are reduced; (ii) when domestic production exceeds domestic needs and the surplus generated is exported in world markets, the volume of exports of other exporters is constrained; (iii) in a situation of oversupply in the world market, world prices are depressed and thus other exporters' receipts for a given volume of exports are also depressed; (iv) world market prices can also be more unstable than they would have been otherwise and thus adversely affect those exporters which are more open to free market forces.

9. The consequences of industrialized countries' agricultural policies for food-deficit developing countries are also analyzed. In general, on the positive side there are the effects relating to the gain accruing to food importers through having access to food supplies at low prices, as well as through the availability of food aid. However, in the medium - and longer - terms these policies are regarded as having negative effects as low food prices in world markets could make developing countries find it

attractive to capitalize on this situation and choose to pursue a cheap food policy thereby creating a bias against developments in their own agriculture. The profitability of domestic and foreign investment in agriculture decreases, productive resources are diverted to other less competitive sectors, the adoption of new technologies are delayed, and overall economic efficiency decreases. The long-term effect is a perpetuation of food deficit problems and of the dependence on imported food, including food aid. At the same time, the possibilities of developing countries depending on trade-oriented self-reliance are impaired.

10. The document further reviews trade liberalization assessments recently advanced by several empirical studies. Although different models were used, liberalization of industrialized countries' agricultural policies is generally estimated to raise world market prices, to reduce world price variability and to stimulate growth in world trade. This would benefit in particular those developing countries which are substantial exporters of the commodities in which trade would be liberalized. In general, however, it is estimated that the prices of many tropical products would increase more than the prices of those temperate zone products imported by developing countries. Thus, developing countries' overall levels of real income would benefit from multi-commodity trade liberalization in agriculture.

11. Finally, the document concludes that the potential benefits to developing countries from liberalization of industrialized countries' agricultural policies would also depend on their response to a more open world trading environment. To the extent developing countries modify their policies to complement the changes in industrialized countries' agricultural policies, their overall benefits would likely be enhanced further.

Title: Agricultural Policy and Trade
Adjusting Domestic Programmes in an International Framework
(A Task Force Report to the Trilateral Commission)

Author: D. Gale Johnson, Kenzo Hemmi, Pierre Lardinois

12. The report by the Trilateral Commission examines the domestic farm programmes of the United States, Canada, Japan and the European Community and estimates the "excess consumer costs" and "taxpayer" cost of each. They conclude that these programmes involve costs that are very large compared to the net benefits to farm people. With respect to these domestic policies upon international trade, the authors note that in the trilateral countries, domestic price support for virtually all major commodities is set at a level that is above the international market price and thus necessitates some sort of barrier to low-priced imports - be it an import quota, a levy, or restrictive state trading. Domestic programmes of price and income support also affect the imports and exports of farm products through their influence upon production and consumption. If increased production is encouraged, imports will decline and exports, often subsidized, will increase. If the support measure increases consumer

prices as well as the return to farmers, consumption will decline, leading also to declined imports or increased exports. A number of studies of the effects of farm programmes on the level and variability of world market prices are also cited. Agricultural protection per se does not result in increasing world price instability but it is rather the form of protection that causes increased instability. When domestic prices are stabilized, price instability in international markets is increased, as variations in domestic production due to weather or farmers' decisions are not reflected in national prices but instead influence the amount imported or exported. Studies are also cited that indicate the depressing effects such policies have on the agricultural exports of developing countries.

13. The Trilateral Commission report notes that it is quite clear what is required if domestic farm policy regimes are to contribute to an improved international situation for all producers and consumers. First, domestic programmes must be made more market-oriented. This does not mean zero protection, but that, over time, the levels of protection should be significantly reduced and domestic producers faced with some degree of international competition. Secondly, the report recommends that the trilateral countries should undertake this movement in concert, which would lessen the difficulties for each to make the change, over a transition period of approximately five to seven years. Finally, the authors stress that there should be no introduction of new trade barriers or broadening of the existing ones during the transition period.

14. The report examines the effects of moving to more market-oriented policies in the trilateral countries. In general, it notes three transition costs: short-run declines in farm incomes, the loss in asset values from lower market prices, and the costs of adjusting to other employment. With respect to the longer-term effects of market-oriented policies upon the incomes of farm people, the report notes the difference in the effects of price supports on incomes of farm owners and tenants, the growing importance of off-farm income to farms in all trilateral countries, and the declining absolute level of employment in agriculture that accompanies the process of economic growth. In moving to a more market-oriented approach, the report stresses the need for emphasis upon rural development policies, especially those benefiting disadvantaged farmers and which have almost no effect on agricultural production or trade. Agricultural research and extension, they also note, benefits consumers as improved efficiency results in lower costs of production.

15. The report concludes with recommendations for priority adjustments in the trilateral countries, and a brief caution regarding the problems of food aid.

Title: The Political Economy of International Agricultural Policy Reform

Author: Geoff Miller
Department of Primary Industry, Australia

16. The report highlights some of the key indicators of the world agricultural crisis: depressed farm prices and incomes, rising farm bankruptcies, massive stocks of surplus commodities, losses of national income and high costs for both taxpayers and consumers. On a broader scale, it notes that the economies of some agricultural exporting countries have been adversely affected; that unemployment, particularly in rural areas, has been exacerbated; and that the debt problems of many less developed countries have been accentuated.

17. These problems, it is noted, are attributable not only to agricultural policies but also to their interaction with other economic policies and factors. In the 1970's, in light of the strong import demand for agricultural products from both developing countries and those with centrally planned economies, some major developed countries encouraged a significant build-up of capital in agriculture, while shielding their producers from fluctuations in world prices. Following the global recession of the early 1980's, growth of world trade declined and the demand for agricultural products levelled off. The subsequent drop in oil prices depressed demand from oil producers, at the same time as many developing and centrally planned countries responded to their debt payment problems by reducing imports and expanding their own agricultural production and, in some cases, exports. Expanding domestic production in both China and India led to substantial declines in agricultural imports by these large consumers, whereas restrictive policies blocked the potential growth in import demand for farm products into Japan.

18. The author stresses, however, that farm policies should be resilient enough to cope with unexpected changes in the world economy and in commodity demand. The report concludes that it is price and income support and stabilization measures, and related trade restrictions and subsidies, which lie at the heart of the causes of the current crisis in world agriculture. The inflexibility of domestic agricultural policies in some principal developed countries has continued to encourage high levels of production in spite of stagnant demand on both domestic and world markets. In these countries, agricultural imports are restricted while domestic commodity prices are maintained above world levels, encouraging surpluses which are stockpiled or dumped on world markets with the assistance of export subsidies.

19. It is noted that not only have these price and income support measures, trade restrictions and subsidies caused major problems in world markets, but they have failed to fulfill the domestic agricultural objectives. The principal objectives of virtually all developed countries are the stabilization of producer prices, the support of farm incomes, and food security for consumers at a reasonable price. However, there is no evidence that high levels of protection and price support in the agricultural sector create higher farm incomes over time, as these high levels of support quickly get built into the cost structure. The income disparity between farm and non-farm households has been largely eliminated, not because of support policies but because in most developed countries a large proportion of farm households now gain the majority of their income from non-farm activities. These support and protection policies have also resulted in consumers in many producing countries paying prices much higher than world prices, so the objective of "reasonable" prices is not met. And the high self-sufficiency rates which have been achieved for some commodities are essentially artificial, as they are based on levels of production and land productivity that can be sustained only by domestic prices which are several times higher than international prices, whereas the actual levels of consumption are much lower than would be expected if there were no limits on imports and if prices were allowed to adjust to a lower level.

20. The report concludes that the basic objectives of domestic agricultural policies would be more effectively achieved through farm adjustment policies, without distorting world trade. Such adjustment policies should be aimed at managing the rate of exodus from agriculture and assisting farmers facing severe income and financial difficulties. Other specific programmes could provide development assistance to increase productivity and farm efficiency, assure the conservation of land and water resources, and preserve the aesthetic and lifestyle values of rural areas. Countries with a strong concern for food security should contract for food supplies from other countries, and acquire agricultural production and marketing enterprises in foreign countries. While these changes in policies are being made, supplementary lump-sum income payments could be made to farmers, linked to short-term supply control measures.

Title: Government Intervention in Agriculture - Measurement, Evaluation, and Implications for Trade Negotiations

Author: USDA - Economic Research Service (January 1987)

21. The paper examines changes in the world agricultural trade environment by comparing the situation in the seventies with that prevailing in the early eighties. Although many factors account for the adverse conditions currently characterising agricultural markets, the paper supports the view that the agricultural policies of trading countries contribute significantly to them. These policies, coupling border measures with various forms of assistance to farmers, insulate agricultural producers in many countries from international competition and discourage supply adjustments. In this policy environment, world supply has continued to grow while demand has fallen, leading to unprecedented stock accumulations and putting downward pressure on world prices.

22. While these various forms of government intervention in agriculture do protect farmers, they are extremely costly for both taxpayers and consumers and have also heightened tensions among trading partners. Increasingly, this situation gives rise to a search for international solutions that would limit the adverse effect of government intervention in agriculture. The importance attributed to agriculture in the Uruguay Round reflects this concern. In light of this, the paper further reviews the perspectives that major agricultural trading countries will bring into the Uruguay Round and describes some possible techniques for achieving the negotiating objectives set for agriculture in the Ministerial Declaration of Punta del Este.

23. The paper argues that given the very broad scope of agricultural policy issues likely to be addressed in the Uruguay Round, a quantitative analysis of the effects of government intervention in agriculture would be an important contribution, much more than in previous Rounds, towards developing negotiating techniques which would help countries to arrive at reciprocal concessions involving non-tariff as well as tariff barriers.

24. To that effect, the methodology chosen is that based on the concepts of producer and consumer subsidy equivalents (PSE/CSE) which are defined as the levels of subsidies which would be required to compensate producers and consumers for the removal of existing government programmes. The paper focuses on support provided by six broad policy categories: (i) market price support, involving border measures and price setting for the domestic market or for traded products; ii) direct income support, involving direct payments from government agencies; iii) policies affecting variable costs of production; iv) programmes affecting marketing costs; v) programmes affecting long-term agricultural production; and vi) controlled exchange rates. On this basis, PSE and CSE are measured for major trading countries (five developed countries plus the EC, and ten developing countries). They relate to governmental programmes in force for major commodities during 1982-1984.

25. Estimates of PSE provide evidence of extensive government intervention which is very different by country and by product, ranging from moderate to heavy taxation to much subsidization of domestic producers. Estimates of CSEs suggest that the effect of government intervention in the agricultural sector of developed countries has been to tax consumers through higher-than-world domestic prices. Taxpayers also assumed the costs of government intervention through government expenditures. In many developing countries, estimates of CSEs indicate that government intervention in agriculture resulted in consumer subsidies. Through this methodology, the paper also explores the relative importance of different forms of government assistance in different countries and commodity markets. Findings point to great differences in this respect. The paper thus concludes that these differences among countries and commodity markets underscore the difficulties that countries will face in attempts to arrive at mutually acceptable ways of reducing government intervention in agriculture.