

# GENERAL AGREEMENT ON TARIFFS AND TRADE

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## PROPOSAL BY NEW ZEALAND

### Establishment and Adjustment of Minimum Prices

1. In this paper the New Zealand delegation sets out its views on the criteria for the establishment of the minimum prices which are to be included in the Protocols to an International Dairy Arrangement, and the criteria and procedures to be adopted for the adjustment of such prices.

#### (a) Factors determining the parameters of international market price levels

2. In order to determine the criteria for the establishment of minimum prices, and hence the appropriate level for such prices, it is necessary to identify the factors that determine the general level of commercial prices in international trade. The international dairy market is relatively small, currently absorbing a trade in dairy products representing 20 million tonnes of milk equivalent, or 4½ per cent of total world milk production of about 433 million tonnes.

3. Demand in this market is comparatively stable. Imports into developed countries are tightly controlled, while imports into developing countries cannot be expanded suddenly to absorb increased supplies. In over supply situations there is a widespread increased use of substantial export subsidies by major Northern Hemisphere producers. These factors together become the major determinant of the international price level, and the major cause of market disruption. Non-subsidized exporters are forced to match subsidized price levels in order to maintain their share of the market, with the result that in a serious over supply situation, such exporters are forced to make sales at prices below the level necessary to cover the costs of production and sales.

4. When shortfalls occur in the major dairy producing areas, export subsidies are reduced, or even suspended to maintain domestic supplies. As export subsidies are cut back, international export prices rise to a de facto maximum.

equivalent to the support price levels in the Northern Hemisphere (provided those countries do not impose quantitative or financial impediments on exports - and prices will only rise further if export taxes are introduced). This price rise sequence occurred in 1973-74 on the international market when the price for skimmed milk powder moved up to support levels in the Northern Hemisphere (and beyond when an export tax was applied).

5. Thus, the parameters of international export prices for dairy products are, on the one hand, the support price levels in North America and Western Europe in times of relative shortage, and on the other hand, the price levels determined by the internationally agreed minimum prices. Actual market prices tend to be determined by the level of export subsidy paid on exports from the Northern Hemisphere.

6. It is against this background that the rôle of the minimum price must be assessed. Any serious attempt to establish minimum international floor prices must take into account the rôle of support price levels and export subsidies in determining the maximum and minimum levels of international market prices.

(b) The concept of the minimum price level

7. When the minimum price arrangement for skimmed milk powder was established, New Zealand advanced the concept that the minimum price should be at a level which gave an economic return to the most efficient producer. New Zealand continues to regard this concept as remaining relevant today in broad terms, although it is difficult to define in precise terms particularly in relation to any one product in the dairy field. Related to this is the concept of a floor price which, once fixed, should not be reduced if it is to maintain its function and which should not fluctuate with commercial market prices. The practical effect of this concept, together with the lack, in existing arrangements of mechanisms which would maintain the floor prices at consistent levels is that the minimum prices originally agreed upon have been eroded in real terms and their value, even as a floor price, substantially diminished. This effect was demonstrated during 1976 when the recovery in international prices for skimmed milk powder, triggered by multilaterally agreed action, was achieved at too low a price level - a level that was quite uneconomic for the most efficient producers to continue in production for any extended period of time.

8. For a minimum price to provide effective stabilization at the lower limit of market fluctuation it must be regularly up-dated to reflect movements in the parameters to market prices and to provide for future stabilization requirements. Thus a minimum price should broadly move to reflect the changes in support levels, which in turn tend to reflect general cost increases.

(c) Adjustments of the minimum prices - the need for additional criteria

9. As stated earlier, the parameters within which international prices fluctuate are, in general, the effective limits set by official support prices, and the minimums established by international agreement. Any minimum price in effect sets a limit to the size of export subsidies and also sets a limit to the extent to which subsidized exports disadvantage non-subsidized exporters. If stability is to be achieved the latter must be assured of a reasonable return which will enable continued sales on the international market. The severe divergences in the parameters within which international prices have moved in the past cannot be permitted if the minimum prices are to serve their basic rôle of stabilizing international trade in dairy products.

10. In order to preserve reasonable parameters for the export price, the minimum prices should broadly move to reflect reasonable increases in costs of production. Given from previous experience, that it is difficult to arrive at a measure of cost increases that would be generally acceptable, it is necessary to examine other criteria which produce an equivalent result.

11. New Zealand believes one criterion which would achieve this would be the restoration of the initial relationship that existed between support levels and the minimum prices when the latter were originally established for skimmed milk powder and anhydrous milk fat. These initial minimum prices, determined by negotiation, reflected what were at the time minimum tolerable levels of return to the most efficient producer, and established an appropriate floor to the market. Subsequent adjustments in support levels have reflected cost increases in the major producing countries and thus provide a measure of the extent to which minimum price levels should be adjusted to maintain their relevance.

12. Calculations show that in 1970, when the skimmed milk powder minimum price was established, the relativity with the average of support prices in the United States and the EEC (expressed in US dollars at the ruling UA/US\$ rate) was 43 per cent. Applying this relativity to support levels in 1977 the current minimum would be US\$60 per 100 kgs. Similar calculations for anhydrous milk fat show that the minimum price established in 1973 was 31 per cent of the average of United States and EEC support levels for

butter, converted to anhydrous milk fat equivalent. Restoring this relationship in 1977 would have lifted the minimum to US\$110 per 100 kgs. Using the same relationship for butter, a minimum price established in 1978 would be around US\$93 per 100 kgs. The concept can also be extended to whole milk powder. The OECD minimum price in 1970 was US\$45 per 100 kgs., when the average United States/EEC national support price was an estimated US\$1,000 per tonne. This gave a relationship of 45 per cent which, if restored in 1977, would give a current minimum of US\$90 per 100 kgs.

13. A time series of such adjustments between 1970 and 1977 demonstrates that annual adjustment up to 1976 would have achieved steady, but moderate, increases in the minimum prices, which, while well below international market prices for much of the time, would have prepared the market for enforcement in 1976 of minimum prices at significantly higher, and more realistic levels, than proved to be the case.

(d) Conclusion

14. Having established minimum prices to provide an effective and relevant floor price on the basis of the criteria identified, it is necessary to ensure that the levels of the minimum prices maintain their relevance in the light of these criteria. To achieve this there should be an annual review of all minimum prices, which would aim to maintain a floor price that is effective in stabilizing the range of fluctuations in international price levels. This could be achieved by maintaining a broad relationship with support levels in the United States and the EC by restoring the relationships initially established under the existing arrangements and extending them to new products and by undertaking regular (annual) reviews of the minimum prices on the basis of movements in these support levels, also taking into account, where relevant, increases in costs, currency fluctuations, the minimum economic return required to maintain the production of efficient producers, and the current market situation.

15. In relation to current export levels, the relevant minimum prices for butter and anhydrous milk fat could be implemented quite quickly but a more gradual application of the approach may be necessary for skimmed milk powder and whole milk powder.

16. In seeking to ensure that minimum prices play a relevant and effective rôle in the stabilization of international trade in dairy products, the New Zealand delegation proposes that the following provisions be inserted in the draft Protocols to the Arrangement, covering milk powders and milk fats.

Article III:2(a)

"The minimum prices provided for in paragraph 1 of the present Article shall be established with a view to ensuring a greater degree of stability in trade in the products concerned by narrowing the range of fluctuations in international price levels. Accordingly, the price levels set out in this present Article shall be established at levels which take account of the need to establish and maintain a broad relationship with dairy price support levels in /the EEC and the United States/ recognizing the rôle that these support levels play in limiting the upward movement in market prices. Account should also be taken of the current market situation, the need to ensure an appropriate relationship between the minimum prices established in the Protocols to the present Arrangement; and the need to establish and maintain a minimum return to the most efficient producers in order to ensure stability of supply over the longer term."

(Present Article 2 would become Article 2(b) with the words in square brackets being deleted.)

Article III:3

"The levels of the minimum prices specified in the present Article shall be subject to annual review by the Committee established in terms of Article VIII:2(a) of the Arrangement. The Committee shall meet in / of each year for this purpose. In undertaking this review the Committee shall have regard to the desirability of maintaining and improving the relationship between the levels of the minimum prices set out in paragraph 2(b) of the present Article, and the dairy support levels /in the EEC and the United States/ but shall also take account, to the extent relevant and necessary, of costs faced by producers, currency factors, the need to maintain a long-term minimum return to the most economic producers, the need to maintain stability of supply, and the current market situation."