

MULTILATERAL TRADE
NEGOTIATIONS
THE URUGUAY ROUND

RESTRICTED
MTN.GNG/NG5/W/91
28 November 1988
Special Distribution

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

Original: English

URUGUAY ROUND - NEGOTIATING GROUP ON AGRICULTURE

Discussion Paper on Aggregate Measurement of Support

Submitted by Jamaica

1. A number of different titles have been given to this concept starting with the original, Producer Subsidy Equivalent (PSE). It measures essentially the transfer of income to producers over and above that which would be considered normal given the functioning of market forces. In this respect, the transfers due to governmental action are considered to be the cause of market distortion either by way of subsidies or restrictions at the border.

2. If the intention then is to remove the "rent" or extra income which is "unearned" by the producers, the subsidies and restrictions must be removed. How is this to be done?:

- (i) a calculation of the final or output prices should be determined. This includes input costs and profit. The output may however be defined not only in respect of prices but of quantity. The combination of both gives the income from production;
- (ii) if there is to be a freeze followed by reduction of support and protection by government, the amounts will need to be quantified and deducted from the final output;
- (iii) this derived amount would make it possible to arrive at a unit price, net of government support and protection. This unit price should therefore reflect real costs plus profit.

3. If the above approach is economically sound then input subsidies cannot be left out of the calculations nor in fact by extension should any restriction which increases the prices of inputs in the production process. However, for simplicity's sake, it will be assumed that the domestic support by way of subsidy is the only factor at play on the input side.

4. Any freeze should therefore enable the "market" to determine in a transparent or informed manner what is the cost of production and consequently, the margin of profit for the producer. Equally, no down-payment can be made reasonable until one knows the total amount on

which one is making the down-payment. If not, one could be expected theoretically, to continue amortization over an unknown period. (However, it may be that the down-payment will extend only for 1989 and 1990, and the reform process will be guided by other means.)

5. The approach suggested by the Cairns Group seeks to avoid the issues raised above by adopting what is described as a "pragmatic" approach focusing on "output-based support". What does it mean?

- (i) the starting assumption appears to be that levels of output are over and above those which would result from the operation of "market forces" (i.e. the absence of government support and protection);
- (ii) further, it proposes that these "excess" levels should be reduced through the elimination of government policies and measures, excluding input subsidies, leading to the removal of distorted market signals and by adopting supply control measures;
- (iii) the modalities suggested in the proposal do not provide a balanced and comprehensive approach i.e. reducing support on the input side. "Input subsidies" are expressly excluded. Those countries who provide support on the "input" side inter alia transportation, subsidies for raw material inputs etc. would be exempted.

6. On the assumption that continued use of input subsidies gives those producers a competitive advantage and on the assumption that they are not the price makers in international markets, they would earn extra profits, while the importer/consumer would not derive the benefit of the potentially lower prices.

7. Moreover, those producers who benefited from "output-based support" which would be subject to a freeze and reduction would be able to benefit from a shift of subsidies to the input side. This demonstrates the need for a comprehensive approach to product and policy coverage among the developed countries.