Section Five

THE CHALLENGES TO WORLD AGRICULTURAL TRADE FOR THE NEW MILLENNIUM
The challenges to world agricultural trade for the new millennium

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1. Introduction

The conclusion of the Uruguay Round in 1994 heralded a new beginning for world agricultural trade. This was openly accepted that developing countries with promising agricultural potential would benefit from the relaxation of trade controls worldwide. Six years later the opinion has changed to one of disbelief and sceptics, as developing countries have not reaped the benefits from freer trade. Therefore world free trade stands at a watershed as it has been perfectly demonstrated at the WTO Ministerial Conference in Seattle, USA in December 1999.

What are thus the challenges that face multilateral agricultural policy reform? What or which is the way forward? These questions come to mind when thinking of the upcoming agricultural trade negotiations of the WTO. Proactively we should prepare our position for this unique opportunity to maximise our gains and minimise our risk, by challenging the status quo.

2. Background

World agricultural trade remains substantially distorted. Governments of the more developed nations of the world continue to provide support to their local farmers, which boost their income and insulate them from world markets. The Uruguay Round included agriculture due to this reason, yet it seems that little progress has been made.

The current WTO Agreement on Agriculture made provision for reductions in overall support in both the developed and developing countries in order to level the playing field. In short, developed countries were obliged to reduce:

- Bound tariff rates and the tariff equivalents of other import barriers- and average reduction of 36 percent and a minimum reduction of 15 percent for individual items;
- Domestic support- an overall reduction of 20 percent; and
- Subsidised exports- reductions of 21 percent in volume and 36 percent in value of subsidies for individual items.
In addition to these cuts to support levels, three key elements of the agreement related to reforming the instruments used to provide support to agriculture:

- **Tariffication**
  Tariffication involved the conversion of all non-tariff barriers to tariffs or tariff quotas. As part of this process the impact of different border protection measures was calculated as a tariff equivalent. This became the maximum tariff that could be applied and was the basis for agreed tariff reductions.

- **Tariff quotas**
  Tariff quotas were used to ensure minimum access levels for imports. This was done by setting a quota at least equal to the agreed minimum access level and applying a lower tariff to this amount. Amounts in excess of the quota could be imported but at a higher tariff rate.

- **Decoupled support**
  With the decoupling of support the links between support payments and key market variables including production, prices and input use were broken. In so doing it makes producers and consumers more responsive to world prices and therefore could lower market distortions. Such support was excluded from reduction commitments by being placed in the so-called ‘green box’.

Progress has since been made in the reduction of support, however, a number of factors have weakened their impact substantially, and making the progress achieved a mere facelift to the real problem.

**Factors weakening reforms**

*Unrepresentative starting points:* The base period used for the negotiations of the reductions in tariffs and domestic support was 1986-88 and for export subsidies the reductions were from the 1986-90 base period. However, these periods represented times of unrepresentative high protection. This resulted in countries having to do little, if anything, to meet their commitments to reduce support.

*Averaging of tariff cuts:* Tariffs across a broad range of products could be combined as a simple average to calculate the overall tariff cut achieved by countries. This meant that cuts to tariffs on items traded little were given as much weight as cuts to tariffs on items traded rather more prominently.

Consequently, many of the major sensitive agricultural products in developed countries with high protection have been subject only to the minimum 15 percent tariff cut. At the same time, many relatively obscure, less sensitive items were subject to larger cuts to bring averages up to the required 36 percent.
Dirty tariffication: This method is used by countries to exaggerate their base levels of tariffs. This is done by the selective use of prices for determining tariff equivalents in the base period. Tariff equivalents are defined as the difference between domestic prices and import prices. To elevate its base tariff equivalent, a country could use base period domestic prices for a high quality product at a remote location where prices were well above representative levels.

Above representative levels: Further they could use an import price for a low quality product at a port where prices were lower than in most other parts of the country. The result would be to make the tariff equivalents in the base period well above what were, in most cases, already extreme levels. Cuts to such exaggerated base tariffs would have only limited effects on actual tariff levels, thereby weakening the impact of agreed cuts. A study for the World Bank revealed that the EU, for instance, had set its initial tariff bindings at unweighted average levels 61 percent higher than the actual tariff equivalents, while the USA set its initial binding at 44 percent above actual levels.

Market access: Some gains were made in assuring current access and opening up markets through minimum access arrangements, mainly through the use of tariff quotas. However, those gains were not large, as the tariffs for beyond-quota imports are generally prohibitive, enabling tariff quotas to be used as tools for managing trade within highly distorting support systems.

Inappropriate use of special safeguards: Special safeguards are supposed to provide cushion for producers against import surges and precipitous reductions in world prices. Such changes give countries the option to use import control mechanisms. However, in some instances safeguards are being used as an integral part of the market management systems. In the case of EU sugar, for example, safeguards render the negotiated reduction in tariff effectively irrelevant, as sugar entering the EU at world prices would be sufficient to trigger the special safeguard arrangements in most years.

Green and blue box exemptions: Decoupled support (in the `green box`) and support provided under production limiting arrangements (in the `blue box`) were exempted from cuts. These exemptions did, however, validate two trends. In the USA production subsidies were replaced by way of payments decoupled from production variables; and in the EU direct payments replaced trade barriers and export subsidies to an extent. It was already stated that the idea behind decoupling could be beneficial when the links between market and production variables were broken, in order to make producers and consumers more responsive to world prices and therefore could lower market distortions. In practice the picture looks like this: In the USA, so-called decoupled payments to US farmers have been varied to counteract world price movements. The low world prices in 1998 induced the US Congress to vote an additional US$5.6 billion in farm payments. The additional payments reduced farm risks by acting like a farm income insurance subsidy, with the potential to distort world prices.
The agricultural policy reforms in the EU since 1992 have focused on the gradual replacement of trade barriers and export subsidies with direct payments that are exempt from cuts under the blue box arrangements. These direct payments are not decoupled and continue to lock in most of the previous production distortions. For crops in the EU, individual farmers receive payments on areas actually planted subject to commitments under area reduction programs, although there are (rarely enforced) regional limits to payments. Such arrangements lock in production capacity at the highly distorted base period levels. At the same time advances in productivity, in particular, the responsiveness in cereal production to fertilizers is continuing to increase production. For beef in the EU, headage payments are linked to animal numbers with maximum levels per farm, which again provides incentives to sustain animal numbers and production at around the distorted base period levels.

**Exported subsidies:** The reduction in subsidised exports is perhaps the main gain from the Uruguay Round. Subsidized export in the wheat market that was greatly plagued by competitive export subsidisation have declined greatly. However, that advance is partly illusory, as the EU has replaced much of its export subsidies for cereals with direct compensation payments that cover the quantities exported as well as output from domestic consumption. Those payments retain several production and trade distorting features, but are excluded from reduction commitments. Similarly the US direct payments for farmers producing for export as well as domestic sale have risen when world prices have fallen. These payments have some market distorting characteristics.

Also the agreed upper limit on subsidised export provides ample scope for increasing subsidisation in the future. Under the WTO Agreement on Agriculture unused credits on export from early years in the implementation period, when prices were high, could be used in subsequent years enabling subsidising countries to exceed the annual volume limits. This has been the case in skim milk powder and also beef.

### 3. Challenging the status quo and building a better future

From the above background, it is clear that although the framework of the Uruguay Round was set in place for reducing world market distortions, progress has not been as most countries, especially the developing countries, have hoped for. This was again due to factors mentioned above, especially on the side of the developed countries, which through their sheer capacities have been able to pursue every loophole offered under the current agreement on Agriculture to their advantage of freer trade, also due to the further trade distorting practices in the developed countries, but also due to lack in capacities and maybe even an overoptimistic emotional approach to free trade. Many of the developing countries embraced the idea of a new free world market, without being informed enough over its consequences and the structures that needed to have been in place in order to capture the benefits from freer trade. They have opted to open their economies in rapid acceleration, without
being aware of the impact of such an action. Incapability to use the provided tools in managing the influence of free trade and open border policy has cost some countries dearly.

With the first phase of the Agreement on Agriculture coming to an end in 2000, the next negotiations are a unique chance to learn from the past mistakes and thus provide for a better future. The Battle of Seattle in December 1999 had indicated that the time had come for taking cognisance of the past and its mistakes, so as to ensure a better future for all countries. It is therefore of crucial importance that developing countries such as Namibia take stock and assess their position.

**The way forward**

In the up-coming negotiations to achieve benefits from agricultural policy reform, the balance of production must be reoriented from currently high support countries to low support countries. This would enable more agricultural production to take place in countries where the costs of production are lowest.

The key to success in this instance would be to move to a situation in which producers and consumers in all countries face domestic market prices that approach and vary with world market prices. Therefore certain issues need to be addressed urgently within the next negotiations.

**Targeting the biggest distortions**: Surely the largest benefits from reducing support would be achieved by targeting the largest support reductions towards those items with the largest market distorting policies. Key areas would include rice, wheat, feed grains, sugar and milk in Japan; wheat, feed grains, oilseeds, sugar, milk, beef and sheep meat in the EU; and sugar and milk in the United States.

**Target high levels of support**: In addition, many agricultural products in the OECD countries, such as Republic of Korea, Iceland, Norway, Switzerland and Turkey continue to receive high levels of support. These levels must be reduced to contribute significantly to a reduction in world market distortions.

Certain systematic issues need also to be addressed and include:

- Base periods for support should be representative of ‘normal’ years or cuts must be sufficient to achieve actual reductions in support.
- Methods of measuring support should be agreed upon, so that the scope for exaggerating support levels is minimised.
- Safeguards should provide protection only against large falls in world prices or import surges that would harm domestic markets. They should not be used to exclude imports under normal world market conditions.
- The tariff-quota mechanism should be transitory, with trade eventually flowing past the beyond-quota quantity. Otherwise tariff quotas would be used in much the same way as the import quotas that tariffication was supposed to eliminate.
- A move towards genuinely decoupled support could, in time, achieve many of the economic gains from liberalisation while allowing some level of farm assistance. For support to be effectively decoupled, the price that farmers receive for their output must be the world market price and marginal costs should not be affected by support payments. Even then, it takes time for distortions to be markedly reduced because of capacity overhangs from previous support.
- Production limiting arrangements (blue box) as currently applied lock in distorted production capacity. They are not fully decoupled. Having them fully decoupled would be an advance. If this does not occur, the support payments under such schemes must be subject to the same reductions as other forms of distorting support if distortions are to be reduced.
- The elimination of export subsidies will be an important outcome and feature of a new successful agreement.
- Care must be taken to prevent reductions to support in one area being placed with distorting support in other areas.
- Developing and least developed countries should be handled with greater exemptions, as their adjustment is often more costly and time consuming.
- Special safeguards for developing countries should be negotiated for through which domestic production (often supported) in these countries could protect themselves against products from developed countries, which have enjoyed support for decades. The past indifferences in support will have to be accounted for when reductions of support are negotiated.

4. Conclusion

The path to reform can be eased through cooperative international approaches to reduce agricultural support. If all reduce support, world prices rise and become more stable and adjustment costs are less. As others also reduce support, fears that others' subsidised products will undercut domestic producers are reduced.

The next WTO negotiations represent a moment of truth for multilateral trade reform in agriculture. Much preparatory work has gone into bringing agriculture fully into the multilateral trading system. However, that work will be of limited value, unless market distortions in agriculture could be reduced substantially toward levels for other major traded goods.

In the wake of these developments and the upcoming negotiations, developing countries need to position themselves in their approach, their capabilities and their needs. Proactive anticipation of possible impacts needs to be done so as to try and minimise the potential gains. It is therefore essential that these countries pool their resources, build additional capacities and effectively communicate and coordinate such actions between stakeholders.