The Doha Round of Trade Talks and EU/ US Agricultural Policy

Nicole Pohl & Guenter Heiduk

Paper to be presented at the workshop

"WTO and World Trade, IV: The Doha Round of Trade Talks"

Seattle, USA, September 28, 2002

First preliminary version

FT 07/26/02: US proposal to eliminate $ 100bn in domestic supports by 2010 draws sharp criticism from trading partners

EU farm subsidy plan sows discord among ministers

FT 07/26/02: EU attacks plan to cut farm subsidies

FT 07/26/02: Zoellick says the US is prepared to tackle its own trade-distorting policies on agriculture if others agree to do the same

WSJ 07/11/02: EU seeks to reshape its massive farm subsidies

EU farm policy: Is reform really on the agenda?

Complex, expensive system of payments for output is under fire from within

Introduction

It is well accepted that the agricultural sector is one of the most protected sectors in international trade. Tariffs on agricultural products amount to 62 % on average globally (Wall Street Journal 2002a). Developing countries have long complained about the distortions that result from tariffs, subsidies, and domestic support as well as manifold other measures given in support of farmers by developed countries. The EU is one of the most intensive users of protectionist policies in the agricultural sector. EU expenditures for agriculture amount to more than 40 bn Euro.[1] So-called EAGGF-expenditures (European Agricultural Guidance and Guarantee Fund) came to about 8bn Euro in France, more than 5 bn in Germany and Spain and not much less in Italy in 2000 (Mann 2002a). Large costs as well as notorious surpluses in production (milk lakes, butter mountains etc.) have put pressure on EU decision-makers to reform the system, but there is still a lot of resistance in particular by farmers associations. Another impetus for reform could possibly come through the multilateral framework established by the WTO. How farm support in the EU and the US has evolved, in how far the Doha round of trade talks has led to a stronger impetus for a reduction of trade barriers and what kind of reform proposals are currently on the table is the topic of this report.

Support and protection in the agricultural sector have long been based on arguments that go way beyond pure economic reasons and comprise a wide variety of social/ environmental goals as well as normative aims. Historically, the most popular arguments were

- to guarantee the autarky of countries in agricultural supply,
- to stabilize prices of agricultural goods and income of farmers,
- to maximize support by electoral groups, such as farmers.[2]

[1] Appropriations for commitments in EAGGF are 44,505,100,000 Euro in 2002.
[2] Although the quantitative importance of this group has declined sharply.

1. The agricultural sector: basic tools for protection and support

Support in the agricultural sector usually concerns a combination of domestic and external measures with the domestic tools being dependent on the simultaneous application of measures at the border. Different factors contribute to the complexity of any analysis of agricultural markets:

- Policies across different product categories and within the same country differ significantly. This is why general statements about the agricultural market even within one country are difficult.
- Policies within one product category differ internationally. This is why it is difficult to compare levels of protection between countries.
- Policies within one product category typically comprise a complex set of tools.
- Policies have changed significantly historically.

Relevant measures applied to agricultural markets can be divided into trade protection and domestic support. The former category comprises market access measures, such as tariffs, quotas and on the other NTBs as well as combinations of these and export promotion measures, such as export subsidies. The latter category can be sub-divided into price support measures, output restrictions and income support.

- Price support relies on political negotiations that lead to the fixing of certain targeted prices that are higher than world market prices. Often, high prices are sustainable, if governments are willing to buy excess supply. At the same time, protection against imports has to be implemented.
- Output restrictions have two main reasons: On the one hand, they are used to make high prices sustainable, and on the other hand, they help avoid excessive surpluses and the storage costs that go along with these. To achieve output restrictions governments can either set positive incentives for reductions or penalize excessive production.
- Income support can come in a variety of ways ranging from direct payments (that can be headage payments or related to current or historical input or output levels) to indirect payments (e.g. tax exemptions or deficiency payments that cover the gap between a targeted price and the lower market price).

2. Agricultural policy in the EU and the U.S.

2.1 Historical evolution of agricultural policy in the EU and the U.S.

Since 1933, the U.S. congress has required the U.S. Department of Agriculture's (USDA) Commodity Credit Corporation to administer a variety of programs to provide price support and income protection for farmers. This start for a more active farm policy has to be understood against the decline in farmers' incomes after World War I, when European recovery led to decreased demand for U.S. farm products. The Agricultural Adjustment Act of 1933 was part of President Franklin D. Roosevelt's New Deal.

In the EU, a common agricultural policy (CAP) and a set of aims related to the agricultural sector were already part of the Treaties of Rome that created the European Economic Community. According to the EC Treaty, the Commission had to present proposals for a CAP within two years. It is generally acknowledged that EU agricultural policy before the 60s was hardly coherent. Most EEC member countries had adopted their own policies for agricultural stabilization and protection, and these included a variety of different methods. The Commission's first proposals were submitted to the Council in 1959. This started off the so-called agricultural marathons, negotiating rounds that produced a sequence of common market organizations for various agricultural products. By the end of 1963, almost 85 % of the agricultural output of the six original member states were covered by a common market organization.

Table 1 gives an overview over these historical developments in the EU and the U.S.

Table 1: History of farm policy in the EU and the US, selected events

	US	EU
1933	Agricultural Adjustment Act introduces price support programs; price support loans mandatory for designated basic commodities, such as corn, wheat, cotton.	
1935	Agricultural Adjustment Act Amendment gave President authority to impose quotas when imports interfered with agricultural adjustment programs.	

1938	Agricultural Adjustment Act makes price support mandatory for corn, cotton and wheat to help maintain sufficient supply along with marketing quotas to keep supply in line with market demand.	
1958		Treaty of Rome sets out objectives of increasing agricultural productivity, fair standard of living for farmers and reasonable prices for consumers
1962		First common market organizations through price mechanism
1968		Effort to cut the number of people in agricultural sector and to form more efficient farming units
1973	Agriculture and Consumer Protection Act: omnibus law creating target prices and deficiency payments to replace former price support payments	
1988		Reform measures to deal with growing surpluses and introduce budgetary discipline
1992		McSharry reform leads to reduction of price support and introduction of direct income support
1996	Federal Agriculture Improvement and Reform Act accelerates long-term shift toward a more 'market-oriented' farm policy; replaces grains and cotton target price payments with 7-year contracts providing fixed but declining annual 'market transition payments' no longer tied to market prices. Acreage reduction programs and planting restrictions are ended.	
1998	Emergency farm Financial Relief	
1999	Omnibus Consolidated and Emergency Appropriations Act provides nearly 6 bn $ in one-time emergency spending to compensate for "regional economic dislocation, unilateral trade sanctions and the failure of the government to pursue trade opportunities aggressively"	

2000		Agenda 2000 with following aims: - agricultural policy that establishes a clear connection between public support and the services which society receives from farming - globally competitive agricultural sector - sustainability in environmental terms - vibrant rural communities - safety in production - integration of new members

Source: Becker, G. S. (1999): Farm Commodity Legislation: Chronology, 1933-98

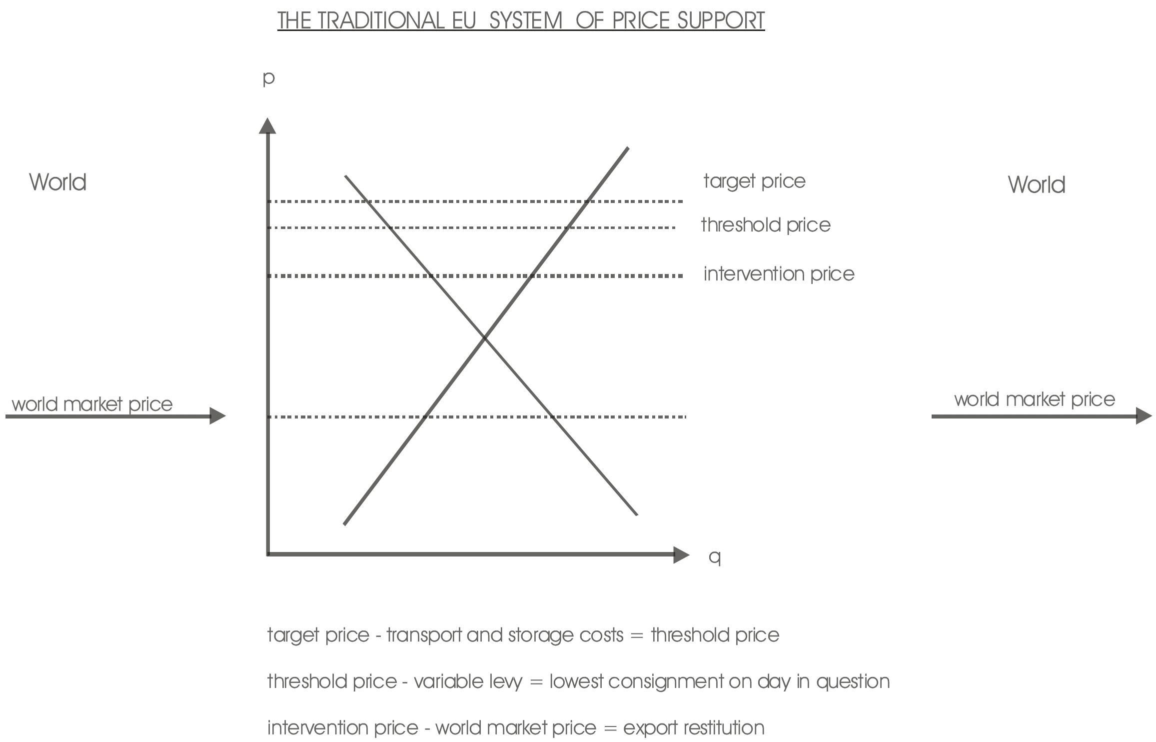
2.2 Basic systems of agricultural support in the EU and the U.S.

2.2.1 European 'Marktordnung'

The European system of price support was based on the fixing of a sequence of different prices (figure 1). Outside protection was integrated into this price system. Firstly, the so-called target price (the preferred price to be received by farmers) was set. The second price was the so-called intervention price. At this price, the EU purchased output from its farmers. Surplus output was stored and periodically resulted in embarrassing phenomena like milk and wine lakes and butter mountains.[3] Both of these prices were fairly higher than world market prices. This is why a third price, the threshold price, was introduced. This price was set between target and intervention price. At the threshold price foreign suppliers were able to import into the EU. To sustain the threshold price variable levies were determined that were charged on imports. To promote exports and reduce output surpluses export subsidies were guaranteed. It is fairly obvious why this system tended to be more than costly (table 2a,b), did not set incentives for productivity improvements and environmentally friendly land use and why it led to massive redistributions of money between net-contributors and net-receivers in the European Union.

[3] The book value of products in public storage with intervention agencies is extremely high (cereals in 12/97 more than 400 mio. ECU, beef nearly as much).

Figure 1: The EU's 'Ordnungssystem' in agricultural markets



Depending on the type of product, support systems in the EU have been modified over time, so that the traditional "Ordnungssystem" can now be found in different facets. Below is a case on EU sugar, a product that has raised a lot of criticism because of the negative effects of the EU's system on the revenues of sugar exporting developing countries.

<u>Case: EU sugar</u>
- quota system brings guaranteed price that is nearly triple the world price - subsidies encourage production even in unfavorable climates - about six mio. tons of surplus production annually - EU dumps surplus on world markets (sells at a fraction of domestic prices) and drives down prices there - EU has evolved from net importer of sugar in the 70s to the world's second biggest importer - Calculations say that production cuts and stop of dumping by EU could improve market price by 20 %. (Wall Street Journal 2002b)

Table 2a: Development of EU community expenditure and EAGGF

	TOTAL community expenditure	EAGGF
1968	higher than 10,000 mio Euro when measured in 2,000 prices	
1978	higher than 10,.000 mio. Euro when measured in current prices	
1979		higher than 10,000 mio Euro
1982	higher than 20,000 mio Euro in current prices	
1986	higher than 30,000 mio. Euro in current prices	higher than 20,000 mio Euro (62.9 % of total)
1988	higher than 40,000 mio. Euro	
1991	higher than 50,000 mio. Euro	higher than 30,000 Euro (56.3 % of total)
1992	Higher than 60,000 mio. Euro	
1996	Higher than 70,000 mio Euro	
1997	Higher than 80,000 mio. Euro	
2000	Higher than 90,000 mio. Euro	
2001		Higher than 40,000 mio. Euro (45.2 % of TOTAL in 2002)

Source: EU

Table 2b shows that – while total agricultural expenditure has been rising, the share of export refunds and storage costs has been declining. This is due to the shift in the EU's agricultural system away from price support towards more direct support to farmers. This change has led to a reduction in the gap between EU and world market prices as well as a reduction of surpluses by increasing domestic consumption and export possibilities.

In 2000, The EU's EAGGF-expenditure amounted to 40.92 bn Euro. Table 2c shows how this money was spent.

Table 2b: Evolution of CAP Expenditures, export refunds and storage costs

	TOTAL in mio ECU	Export refunds as percentage of total	Storage costs as percentage of total
1989	24,084	40.3	11.6
1990	24,936	31.0	16.4 (18.3 in 1991)
1993	33,659	29.7	15.9
1996	39,108	14.6	3.6
1999	39,541	14.1	4.0

Source: Agritrade 2002

Table 2c: EU expenditures by products and economic type (selected) in 2000

	By product (selected)	By economic type (selected)
TOTAL EAGGF 40.92 bn Euro	**25,812 mio Euro on crop products** - 16,663 mio. on arable crops - 1,910 mio on sugar - 2,210 mio on olive oil - 381 mio on dried fodder - 991 mio on fibre plants and silkworms - 1,551 mio on fruit and vegetables - 765 mio Euro on vine-growing sector - 14 mio on tobacco **9,276 mio Euro on livestock products** - 2,544 mio on milk products - 4,540 mio on beef and veal - 1,736 mio on sheepmeat and goatmeat - 435 mio on pigmeat, eggs and poultry - 9.5 mio on fisheries	Refunds: 5,646.2 mio Euro Direct aid: 25,529.2 mio Euro Storage: 951.2 mio Euro (products stored were more than 8 mio tones of cereals, more than 25,000 tonnes of olive oil, more than 1,000 tonnes of skimmed-milk powder, about 800 tonnes of beef and more than 1.5 mio hectolitres alcohol)

2.2.2 The U.S. counter-cyclical flexible system

It seems to be much more difficult to depict a basic support system for the United States. Initially, support in the 30s seemed to rely on price support programs and price support loans combined with protection by import quotas. Historically, measures seemed to react much more flexibly to market changes. U.S. support for grain for instance has tended to increase rapidly in times of drops in world market prices and it has also fallen more rapidly when prices were high. This makes a general evaluation across different periods as well as in an EU-U.S. comparison more difficult. Compared to the U.S. system, the EU's CAP did not allow flexible reactions to market developments.

2.3 The agricultural sector within the GATT/ WTO framework

Trade distortions in the agricultural sector have first been discussed within the multilateral GATT/ WTO framework in 1994. The Uruguay Round was the first time when agricultural policies were brought under multilateral trading rules and disciplines. Already at that time, the agricultural sector was very obviously the biggest hurdle for a new trade agreement. In the final phase, the French government started to require concession from all trading partners because premier minister Balladur feared a revolt of the French farmers association. The Japanese government did not have a much easier time and the South Korean president finally made a public excuse on TV because of opening the rice market and breaking a promise made during his election campaign.

As a result of the Uruguay round, the EU agreed to reduce its support for farmers among other things by

- changing its variable levy system into fixed levies,
- replacing non-tariff barriers by bound tariffs (tariffication) and lowering tariffs,
- gradually reducing the value of subsidized exports of the next six years by 36 %,
- reducing the quantities of subsidized exports by 21 %,
- limiting the import price of cereals to not more than 155 % of the intervention price,
- reducing income payments that are coupled to output,
- agreeing to a differentiated set of measures concerning different forms of domestic support (see table 3).

Table 3: Classification of support policies in the WTO framework

amber box	most trade distorting measures, subject to WTO discipline (market price support, direct payments coupled to output etc.)
blue box	measures that are acknowledged to be trade distorting, but that are related to production limiting programs; exempt from WTO discipline
green box	minimally trade distorting policies; not subject to WTO rules.

The Uruguay round agreement also included a 'de minimis exemption' that states that domestic support for a commodity that is less than 5 % of the value of that commodity's value of production is not included in the Aggregate Measure of Support (AMS).

The Aggregate Measurement of Support (AMS) is an index that measures the monetary value of the extent of government support to a sector. It includes both budgetary outlays as well as revenue transfers from consumers to producers as a result of policies that distort market prices. The AMS includes direct payments to producers (deficiency payments for instance), input subsidies, the estimated value of revenue transferred from consumers to producers as a result of policies that distort market prices and interest subsidies on commodity loan programs.

A different measurement is the Producer Subsidy Equivalent, (PSE) which also measures estimated benefits of non-commodity specific policies (such as research and environmental programs). The PSE is a broadly defined aggregate measure of support to agriculture that combines direct payments to producers financed by budgetary outlays, budgetary outlays for other programs assumed to provide benefits to agriculture and the estimated value of revenue transfers from consumers to producers as a result of policies that distort market prices.

The OECD states that many countries had fewer difficulties in complying with their AMS commitments because policies were reformulated to fit into the blue box or green box. But despite reductions in AMS, the level of agricultural support as measured by PSE is high and has not shown such a discernible downward trend. OECD points out that support has shifted from measures that support higher farm prices financed by consumers to payments financed by taxpayers.

Source: U.S. Department of Agriculture, Economic Research Service

As mentioned above, one of the results of the Uruguay round was tariffication. This aim has however not been achieved completely, as tariff-rate quotas are characteristic for many sectors.[4] They allow fixed quantities (quotas) of imports to be charged a lower tariff rate (in-quota imports), while any imports beyond this are charged higher or even prohibitive rates (out-of quota imports). Both the EU and the U.S. have tariff-rate quotas and many of them have high fill-rates (in the EU above all on cereals, meat and fruit and vegetables; in the US mostly on dairy; average fill rate in both 66 %). Tariff-rate quotas

[4] See Abbott (2001) for an analysis of tariff rate quotas as market access instruments.

are often used for preferential treatment of trading partners. While the fill rates for US quota lines have been increasing during the second half of the nineties, those of the EU have been decreasing.

Table 4 also gives an overview of bound tariff levels in the EU and the U.S. for selected products.

Tariff quotas:

- if domestic price is lower than world market price plus in-quota tariff, no trade
- if domestic price is higher than world market price plus in-quota tariff but lower than world price plus out-of-quota tariff, tariff quota is binding, quota fills, no imports at out-of-quota rates; imports restricted to size of tariff quota
- domestic price higher than world price plus out-of-quota tariff, tariff quota no longer binding, quota fills and some importers pay in-quota tariff, some pay out-quota tariff; rationing problem for volume within quota.

Table 4: Bound tariffs on agricultural products

	U.S.	EU
Cereals (unprocessed)	2	4
Coffee, tea, mate, cocoa	0	3
Dairy	1	0
Oilseeds, fats, oil	16	0
Sugar	4	10
Meat	6	6

Source: WTO (2001); Note: Some WTO members have bound their agricultural tariffs in ad valorem terms, but others have bound many tariffs in specific, mixed, compound or other rates. This is why tariff lines affected by non-ad valorem tariffs were excluded from this table. This is particularly relevant for dairy and sugar in the U.S. and cereals, dairy, sugar and meat in the EU.

In 2001, the Doha round of trade negotiations called for substantial improvements in market access, further reductions of export subsidies (with a view to phasing out), reductions of trade distorting domestic support and an incorporation of agricultural negotiations into a new comprehensive trade round. First proposals in this regard have been put on the table by the U.S. and the EU this year.

2.4 The current situation in the EU's and U.S.'s agricultural market

The current situation in agricultural markets of the EU and the U.S. is a result of both, GATT/ WTO commitments and – in particular for the EU – internal pressure to reduce costs of agricultural support in enlarging union. With an average tariff of 31 %, the EU has higher tariffs than the US (12 %) (Wall Street Journal 2002a). Tariffs in the EU and the U.S. vary strongly across products. There are some tariff peaks that can be as high as 300-500 % (on grains, sugar and dairy in the EU and sugar, peanuts and dairy in the U.S.) Moreover, tariff escalation that penalizes processed foods over raw food is common. Both the U.S. and the EU also have the Special Agricultural Safeguard that allows them to protect designated products from floods of imported goods by raising tariff levels.

It is also the largest user of export subsidies (2bn $ compared to 20 mio. by the U.S.). EU farmers get 35 % of their income from support (21 % in the U.S. and much more in Japan) (Wall Street Journal 2002a). OECD data point out that the Producer Support Estimate for the U.S. is lower than the one for the EU (22 % compared to 36 % in terms of total farm income).

The sectors on which protection and support focus in the EU and the U.S. differ to some extent. Above all, beef, sheep meat and poultry enjoy higher protection levels in the EU than in the U.S. Other differences concern sectors such as rice and oilseeds (see table 5). The largest part of the EU's EAGGF guarantee section is spent on arable crops followed by beef and veal and milk products.

Table 5: EU and US percentage PSE, products 2000

Product	% PSE EU	% PSE US
Wheat	46	48
Maize	41	33
Other grains	50	45
Rice	11	40
Oilseeds	42	27
Sugar	50	50
Milk	43	45
Beef	78	4
Sheepmeat	53	16
Poultry	53	4

Source: OECD (2002)

As regards the methods applied, OECD data show that the EU relies stronger on market price support and less on output payments (as a form of income support) than the U.S. Both countries use payments based on area planted and animal numbers as well as input use, but to different degrees. Many of the U.S.'s support measures are also based on historical entitlements. OECD data also show that the reliance on market price support and output payments – despite their continuing importance – has declined strongly in the EU, while particular payments on area planted/ animal numbers have increased. Tables 6 and 7 illustrate OECD measures of the producer support estimate in the EU and the U.S. as well as measures for the U.S. Aggregate Measure of Support. Abare (2001) also finds that U.S. support for rice, sugar and milk (in terms of % PSE) is higher than in the EU, while the EU has a higher support for wheat and coarse grains as well as oilseeds and beef. In particular for wheat there was however a tendency of convergence of the U.S. level of support toward the EU level in the second half of the 90s.

Table 6: Composition of % PSE in EU and US

	1986-1988		2000	
	EU	US	EU	US
Market price support	86	47	58	30
Payments based on output	5	7	4	22
Payments based on area planted/ animal numbers	3	27	27	7
Payments based on input use	5	16	7	13
Payments based on historical entitlements	0	0	1	21

Source: OECD (2002)

Table 7: Aggregate Measure of Support (AMS), U.S. Amber Box for 1999 and 2000 (estimates) in bn. Dollars

	1999	2000
Price support For dairy For sugar For Peanuts	 4.5 1.4 0.3	 4.5 0.3 0.3
Loan deficiency payments	6.9	6.2
Marketing loan gains	1.5	1.9
Crop loss assistance	1.2	1.2
Other payments	1.0	2.0
TOTAL	16.8	18.6
WTO CEILING	19.9	19.1

Source: Korves/ Skorburg (2000)

The PSE is made up of two types of support. The first of these is indirect or 'invisible' support, which is referred to as Market Price Support (MPS). MPS arises as a result of those policies that affect consumer and producer prices. It is thus support in the form of higher prices paid by consumers, and is calculated by the difference between domestic and world price levels. The second type of support is direct payments to agriculture, or

Budgetary Payments. This refers to direct aid to producers, such as payments based on output, area of crop planted and input use.

Subsequent reforms of the EU's system have focused on possibilities to reduce surpluses. In 1992 (Mac Sherry reform), the EU finished a reform that led to cuts in prices and compensated farmers for their losses through direct compensation payments. For cereals, farmers who took land out of cultivation were compensated by set-aside payments. In general, the importance of less trade distorting direct payments has increased and guaranteed prices have gradually been decreased. While direct payments accounted for only 9.3 % of CAP funding in 1998-1991, they increased to 59 % with the MacSharry reform and their share for 2006 is projected as 68.2 %. The EU's 'AGENDA 2000' program introduced a number of measures aimed at improving agri-environmental performance and promoting rural development as well structural adjustment.

Concerning the situation in the U.S. it can be found that a number of measures have been adopted that differ significantly from EU tools, both in terms of terminology as well as strategy.

- Production Flexibility Contract Payments for crops (wheat, corn, barley, grain sorghum, oats, upland cotton, rice in 2002 Farm Bill): Production Flexibility Contract Payments are annual **direct payments** that depend on the payment rate of the base crop, the payment acres and the payment yield for the farm. They are based on the historical enrolled area of contract crops. Producers enrolled in the 7-year Production Flexibility Contracts are eligible to receive payments. All contracts began with the 1996 crop and extend through the 2002 crop. A farm was eligible for enrollment, if it had a wheat, corn, grain, sorghum, barley, oats, upland cotton, or rice crop acreage bases established for 1996. Once the farm is enrolled, the crop acreage base becomes contract acreage. Commodity-specific contract payments are determined annually based on the statutory spending levels and the amount of enrolled contract acreage. (Source: Catalogue of Federal Domestic Assistance)
- (Marketing) loan rates are loans guaranteed for a product by the time of the harvest or planting. The harvest is used as collateral. The farmer can decide whether to buy the product back by paying back the loan or not to buy back when market rates are low. Loans provide producers with the possibility to store production instead of selling it at a time when prices

are lowest. In this sense, loan rates are a type of deficiency payment. They are often called non-recourse loans because there is no recourse against the loan other than the crop itself. In some cases, direct deficiency payments are made, when market prices are low. These payments cover the difference between the loan rate and the market price. Instead of storing the product, it is sold on the market. The target price deficiency payment system was however not introduced in the U.S. before the 70s.

- Export credit programs: Export credit programs guarantee U.S. commercial banks that they will be repaid for credit that they extend to approved foreign banks for the purpose of financing the purchase of qualifying agricultural goods from the U.S.; they facilitate commercial sales of U.S. agricultural products; the program was extended with the 2002 Farm Bill. Export credits have traditionally used much more intensively in the U.S. than in the EU. In 1998, the U.S. spent 3,929 mio. U.S.-$ on export credits, while the relevant figure for the EU was 1,254 mi. U.S.-$.
- Export Enhancement Programmes (basically similar to export subsidies)
- Food aid: The U.S. uses surplus as food aid.

The U.S. support system is also relatively specific depending on which product category is considered. Until 1996, a counter-cyclical price support system based on deficiency payments was the core of support for crops, while domestic price support and supply and control measures characterized four sectors with high tariff protection (dairy, sugar, peanuts and tobacco).

- Peanuts:
    - historically: import tariff quotas with relatively high out-of-quota tariffs, domestic quotas. The peanut program was a two-tier price support program based on non-recoursive loans. The quota kept prices at a certain quota loan rate. Non-quota production was only allowed for export or domestic crush.
    - Under the 2002 Farm Act, the marketing quota system was eliminated and peanuts are treated similar to 'program' crops, such as grains and cotton. There is a compensation for the elimination of the quota system. The Act provides for marketing assistance loans or loan deficiency payments alternatively.

- Dairy:
  - historically: import quotas that were succeeded by high tariffs and tariff-rate quotas as well as export subsidies
  - Under the 2002 Farm Bill the Dairy Support Program was extended. It includes that the USDA buys storable dairy products at a certain price, that dairy exporters receive cash bonuses when international prices are below domestic prices, and that monthly payments are made to dairy farm operators, if prices are low.
- Sugar: tariff-rate quota with price support loan program; loans are made to processors and not directly to producers; flexible marketing allotments for sugar producers.
- Crops: production flexibility payments and marketing loan provisions; until 1996 counter-cyclical price support system based on deficiency payments

In 1996, the U.S. passed the Federal Agriculture Improvement and Reform Act. This seemed to set the stage for a market-oriented agricultural system. However, by 1997 already, U.S. crop prices had declined significantly. There were frequent calls for relief for U.S. farmers. A continuation of the path that had been chosen in 1996 seemed to be impossible. Emergency assistance was given in 1998, 1999 and 2000.

Table 8 gives a comparison between EU and U.S. farm policy for grains and oilseeds and milk and sugar. What becomes obvious is that the U.S. refrains from using export subsidies for grains, which is done by the EU, and that it also does not use area reduction programs, such as land set-aside.

Table 8: Grains and oilseeds and milk and sugar support policies in EU and US in 2001

Policy	GRAINS AND OILSEEDS		MILK AND SUGAR	
	US	EU	US	EU
Restrict import access	No	**Yes**	Yes	Yes
Domestic support subsidies	Yes	Yes	=	=
Floor price support	Yes	Yes	Yes	No
Export subsidies	No	**Yes**	Yes	Yes
Area reduction programs	No	**Yes**		
Production quota restrictions	No	No	No	**Yes**
Expand market access abroad	**Yes**	=	=	Yes

Source: ABARE (2001)

Table 9 summarizes some of the main negotiating positions of the U.S. and the EU.

Table 9: U.S. and EU negotiating position for next trade round

	Market access	export subsidies	domestic support	special and differential treatment
United States	○ reduce applied rather than bound tariffs ○ eliminate special agricultural safeguard ○ TRQ reform	○ reduce and eventually phase out export subsidies ○ no new WTO disciplines on export credits and food aid	○ reduce amber box support in fixed percentage of total agricultural output ○ reduce and eliminate blue box support ○ retain green box	○ different targets, timetables and exemptions consistently applied to developing countries
EU	○ percent reductions in unweighted average, bound tariffs from specified baseline ○ retain special agricultural safeguard ○ tariff rate quota reform	○ reduce export subsidies if other forms of export support are disciplined	○ reduce amber box payments as percentage of baseline ○ support for amber box reductions conditioned on continuation of blue box ○ retain green box	○ different targets, timetables and exemptions consistently applied to developing countries

Source: Beierle (2002)

3. Current proposals for reform in the agricultural sector

The WTO Agricultural Committee agreed on a work program in spring this year that could help set out the key negotiating principles for a final comprehensive farm deal by March 2003, which is the deadline set in the Doha Conference. In Doha, ministers also agreed on a January 2005 deadline for reaching a final agreement on agriculture. Both the EU and the U.S. have recently made proposals for internal reform of their system (EU proposal) or a wider approach for global liberalization (U.S. proposal).

In May 2002, President Bush signed a farm bill that grants 190 bn U.S.-$ of subsidies to U.S. farmers. Only shortly afterwards, he proposed huge reductions of tariffs and subsidies worldwide. His proposal has been characterized as unbalanced by the EU because it would force European countries to reduce their domestic support much more than the U.S. The U.S. position is that its level of support is already lower than the EU's, and that a level playing field should be created. As part of the U.S. proposal, EU tariffs would drop from an average level of 31 % to 9 %, while U.S. tariffs would fall from 12% to 5 % (Alden et al 2002). The U.S. proposal includes tariff cuts from an average of 62% worldwide to 15 % and a cap on trade-distorting domestic support at 5 % of a country's production. Altogether the proposal would lead to an elimination of about 100 bn $ of trade-distorting domestic support. The EU argues that the behavior of the U.S. government is inconsistent and not credible because the liberalization proposal is counter-intuitive to the recent farm bill. EU commissioner Franz Fischler also argues that it will only reduce subsidies, if other forms of support like export credit programs, state trading enterprises and food aid also become subject to strengthened WTO rules.

Details of the U.S. proposal include:

- elimination of export subsidies with reductions phased in over a five-year period in equal annual increments,
- elimination of export monopolies,
- prohibition of export taxes on agricultural products,
- establishment of specific rules to govern export credit activity by identifying permissible practices,
- expansion of reporting requirements in the WTO to increase the transparency of food aid activities,
- reduction of agricultural tariffs (out-of quota and tariff-only items) from 62 to 15 %,

- expansion of tariff-rate quotas,
- elimination of the Special Agricultural Safeguard,
- limitations on trade-distorting domestic support to 5 % of total value of agricultural production,
- maintenance of basic criteria for non-trade distorting support.

The EU is under strong pressure to make its agricultural policy more acceptable to taxpayers anyway. It is also strongly concerned about growing worries about food safety. As part of the EU's midterm review, Commissioner Fischler has recently unveiled a plan to decouple direct payments to farmers from production in order to reduce the need to buy up surpluses and to subsidize exports. (Mann 2002). He aims at creating a stronger relationship between agricultural policy and environmental, animal welfare and food quality and to promote broader rural development. The proposal also involves a cap on subsidies to individual farms (300,000 Euro per year), but the overall budget for the agricultural sector is to remain at around 40 bn Euro. It includes a 50 % cut in price support for soybeans, wheat corn and rice as well as a replacement of the milk quota system with quotas that are based on market prices.

Those EU members that are the main net-contributers to the budget (such as Germany) would like to see proposals that go even beyond these limitations on support. Other countries, in particular France and the southern European countries state that the EU's budget has been fixed until 2006.[5] Before the U.S. put its proposal on the table, European farmers accused the Commission that it made unilateral concessions, while the U.S. is in the course of even raising the level of subsidies that are paid.

4. Expectations for the next trade round

Traditionally, the EU system had been created as a relatively fixed framework that would allow the integration of a number of different national policies pursued by EU member states. The main idea was to create a long-term 'Ordnungssystem' that was from its very beginnings on built on compromise. Successive annual negotiation rounds in the Council have confirmed and extended the system and created an increasing lock-in effect. This

[5] French right wing leader Le Pen has spoken of peasant genocide (New York Times 2002).

fits nicely into the general observation that centralization in the EU tends to create more centralization or that it is easier to create new systems and institutions than to abolish existing settings.

Compared to this, the U.S. system has never had similar long-term aspiration. It consists of a set of Farm Acts that were reactions to changing world market and U.S. conditions and that seem to be lobbyism-oriented.

Changes in the EU system were mainly due to pressure that came from increasing and nearly uncontrollable costs of the system, the evolution of the union towards an ever more heterogeneous group of countries as well as outside (GATT/ WTO pressure). This has weakened the all-encompassing systemic character of the EU CAP towards a jigsaw puzzle like construction or a fuzzy system.

Meanwhile, U.S. farm policy has developed towards a relatively contradictory set of measures. They clearly reflect the cleavage that the U.S. government faces between internal pressure by lobbying groups and the external aim to be a moral leader in liberalization. It is interesting to see today that this pattern is pretty well repeated in other sectors such as the steel sector.

For coming trade rounds, three possible outcomes can be imagined:

- a gradualist approach that leads to a relatively unsatisfactory muddling through development in the agricultural sector,
- a general redirection of farm policies towards a new and shared market-oriented approach based on hard liberalization,
- the inability of the negotiation partners to agree on a substantial shared agenda.

To evaluate the probability of these scenarios, one has to take into account that any agreement between WTO trading partners has to be preceded formally by the establishment of a common position within the EU. By experience, we know that common positions in the EU have usually been based on a minimalistic level of progress as well as agreement. Moreover, the need for a previously negotiated common position has usually significantly reduced the EU's flexibility during WTO negotiations. What is interesting is that some EU member states seem to have relatively strong preferences for an agreement that includes more liberalization and is therefore in line with the EU proposal. Formally, these countries (like Germany) are not allowed to form a coalition with the U.S. because of the need for a common EU position. Experience has also shown that the U.S. has periodically preferred bilateral talks with EU member states to negotiations with EU representatives.

Another argument against radical change of the EU's system is that significant structural problems with the EU can be expected as a consequence of a complete reorientation of EU agricultural policy. This will hardly be feasible in the short- to medium-run.

At least within a time horizon that goes until 2006, the EU's long-term budgetary plan also sets a basis for inflexibility and it provides those countries (for instance France0 that want to prevent change with a very useful argument.

Finally, WTO agreements have usually been package solutions where a favor in one field has been exchanged against support in another. This means that predictions about future agricultural policy can only made on the basis of an understanding of the role of the agricultural sector in the wider negotiation setting.

There is little doubt that the next agricultural negotiations round will be at least as tough as the previous round. Compared to other sectors, this is also due to the fact that a simple model scenario is not available. While it was clear that overall liberalization would be the ultimate aim for the manufacturing sector, ideas of multifunctionality and the special role of the agricultural sector make this much more difficult for the question of farm support. Moreover, increasing technological progress in the agricultural sector has rendered negotiations much more complex because disputes about tariffs and subsidies have been substituted by more and more complex trade disputes about regulations, standards and norms (such as the trade war about hormone treated meat coming from the U.S.). The current high complexity of support systems that vary across different products are likely to render negotiations a very laborious process. It seems to be very difficult to achieve significant progress, if the major users of agricultural policies do not make progress to come to an agreement on certain binding criteria of how agricultural support systems can and should be designed. Finally, we know that multilateral negotiations with many heterogeneous partners at one table are likely to result in piecemeal reforms and compromise-based solutions. Instead, intensive and constructive dialogue between the major players about more general lines along which progress could be made is urgently needed already before the next negotiating round can start.

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