

International Economics Policy Briefs

This Far and No Farther? Nudging Agricultural Reform Forward

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As countries attempt to restart the stalled Doha Round and continue the negotiations on further agricultural trade reform

and liberalization, it is useful to take stock of the progress made so far in the light of both the objectives of countries and the needs of the trading system. This policy brief reviews the main objectives of the agricultural talks in the World Trade Organization (WTO), examines the major proposals that emerged in the run-up to Cancún and at the ministerial itself, describes the emerging framework for further reform, and suggests ways in which the negotiations can build on this progress to achieve a worthwhile outcome.

The purpose of the current agricultural trade negotiations is to decide whether to continue the process of incorporating agriculture into the mainstream of trade, thus further restricting the agricultural policy space, or whether to abandon the attempt and allow countries more flexibility to pursue domestic objectives.

Assessing the Uruguay Round Agreement on Agriculture

The Uruguay Round marked the first step toward the full incorporation of agriculture into the rule structure of the GATT/WTO multilateral trading system (Tangermann 2000). The Uruguay Round Agreement on Agriculture (URAA) provided a negotiated framework into which both trade policies for agricultural products and domestic farm policies could fit so that conflicts could be avoided and distortions to world markets minimized. Rules and quantitative limits on both trade and domestic policy instruments were imposed: Bound tariffs replaced nontariff barriers, and countries agreed to minimum market access commitments. Export subsidies were limited both in the expenditure and

the volume of exports that could benefit from subsidies. Domestic support was categorized into three groups: minimally distorting (green box), linked to production controls (blue box), or output-increasing (amber box); the last category was subject to agreed limits, which have been reduced over time.

At first, the URAA framework appeared rather permissive, requiring major developed countries to make only a few changes in farm policy. Tariffs were bound at a relatively high level, and export subsidies declined as world market prices firmed in the mid-1990s. Domestic policies seemed relatively unconstrained by the URAA, though over time the noose has tightened somewhat.

The rule-making achievements of the URAA came at the expense of any significant liberalization. Moreover, a number of aberrations and temporary derogations to the rules were introduced, which were apparently necessary for countries to agree to a transition to a new regime. The high level of bound tariffs that replaced nontariff import barriers made liberalization by conventional tariff negotiations difficult. The tariff rate quotas (TRQs) that attempted to induce some market opening have in many cases become locked into preferential agreements, and in others they have gone unfilled. The special agricultural safeguard has protected developed-country farmers from import surges but has not been widely available to developing countries. Export subsidies and equivalent measures continue to distort several important markets and are increasingly seen as injurious to developing-country farmers. There is widespread skepticism of the effectiveness of developed-country farm policy reform, even though it has been along the lines of URAA's domestic-support rules.

The task of liberalizing agricultural trade can be summarized under the three headings of market access, export competition, and domestic support, which were first developed in the Uruguay Round and are still used as the basic framework for the negotiations.¹

Market Access

In accordance with the Uruguay Round rules in market access, WTO members have imposed bound tariffs on their agricultural products and reduced them according to the agreed schedules.² But,

¹ The material describing current levels of protection and subsidies is drawn from Josling (2004), which in turn updates material in IATRC (2001).

² The major exception to tariffication was removed when Japan replaced its quantitative import restriction on rice with a tariff in 1999, and Korea is expected to follow suit in due course.

despite the countries' adherence to the Uruguay Round commitments to reduce agricultural tariffs, their duties on farm products remain very high. Gibson et al. (2001) provide a comprehensive comparative analysis of post-Uruguay Round tariff rates by country and commodity.³ They estimate the global average of post-Uruguay Round agricultural tariffs at 62 percent.⁴ With the exception of the high-tariff region of non-EU Western Europe (104 percent), developing-country regions have the highest tariffs: Africa, the Caribbean, and South Asia have average tariffs ranging from 71 to 113 percent. Among the major OECD countries, average agricultural tariffs in Canada (24 percent), the European Union (30 percent), Japan (33 percent), and the United States

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(12 percent) are lower than the global average.

Masked by these averages is the fact that OECD tariff protection is very high in several important sectors, including dairy (116 percent), grains (78 percent), livestock (82 percent), and sugar and sweeteners (64 percent). These are the sectors in which some OECD countries use megatariffs (defined as tariffs over 100 percent) and in which the number of notified TRQs is concentrated. Non-OECD countries tend to have higher average tariffs than OECD countries but with less variation across commodity groups. Non-OECD countries also have megatariffs, usually established as ceiling bindings in the Uruguay Round. However, in many developing countries, the tariffs actually applied can be

³ Their analysis is based on tariff data from several sources, in particular the Agricultural Market Access Database (AMAD) of post-Uruguay Round bound tariffs, tariff rate quotas, and some applied tariffs for about 40 WTO members (available at www.amad.org). Other tariff data are from the WTO Secretariat and UNCTAD.

⁴ This simple (unweighted) average of post-Uruguay Round bound agricultural tariffs includes the *ad valorem* equivalents of specific tariffs, which are in some cases very high and whose values depend on prices. It also includes the over-quota tariff in TRQ regimes.

considerably lower than the bound rates in the WTO schedules.⁵

The lack of any significant liberalization continues to be the major cause of distortion in world agricultural markets. Developing countries have particularly felt the effect, though their own high protection levels contribute to the problem. Market access has not improved significantly since the Uruguay Round for many of the commodities of interest to developing countries.

Export Subsidies

The URAA has had considerable impact on export subsidies. It prohibited any new export subsidies and blocked increases in existing export assistance programs. The number of countries that can grant export subsidies, and the products that they can subsidize, is now limited. Countries have generally observed these limits. With the exception of Canadian dairy policy, the operation of export competition rules has been without major controversy.⁶

Though the URAA effectively introduced curbs on export subsidies, they are still a major distorting factor in certain world commodity markets. Between 1995 and 2000, WTO members spent over \$36 billion subsidizing exports. The European Union accounted for nearly 90 percent of the expenditures and the United States for about 2 percent. The European Union is the largest user of export subsidies in both value and volume. According to WTO notifications, the European Union spent an average of \$6 billion annually from 1995 to 1998 on export subsidies, though this expenditure fell in 2000 with firmer prices. The United States is the major user of export credit programs and a major provider of food aid, and the European Union has insisted that these programs be included fully in disciplines on export subsidies.

Export subsidies are focused on relatively fewer commodities. From 1995 to 1998, the European Union subsidized nearly all of its exports of butter and butter oil, beef, and skimmed milk powder. Wheat and coarse grain exports were also subsidized over that period. Nearly 98 percent of US export subsidy expenditures have been for dairy products under the Dairy Export Incentive Pro-

gram. Global expenditures of WTO members on export subsidies reflect this commodity composition: Dairy products accounted for 34 percent of all export subsidy expenditures from 1995 to 1998, and beef accounted for 21 percent. Grains, sugar, and processed products together accounted for 35 percent of expenditures over that period. So major improvements in the world markets for dairy and beef products, as well as for cereals and sugar, require the elimination, or at least drastic reduction, of export subsidies.

Domestic Support

The progress in domestic support is more difficult to summarize. The URAA was most innovative in the domestic agricultural support area in terms of establishing new rules that significantly distinguish agriculture from industry. But it is also the area where country commitments were the weakest and where the effectiveness and workability of the URAA have been least tested. The URAA established bindings in domestic agricultural support mainly through limits on the total Aggregate Measurement of Support (AMS). Reduction commitments were intended to constrain domestic support measures that encourage agricultural production or raise consumer prices and are therefore considered to distort trade (amber box policies). Countries are not required to include direct payments under certain production-limiting programs (blue box policies) in their total AMS. More widely applicable are the exemptions for green box policies, which are considered to have no (or at most minimal) trade-distorting effects. In addition, *de minimis* provisions allow countries to omit from their reduction commitments a fraction of specific and nonspecific support payments.⁷ As a result, a large part of the expenditure on domestic programs has in effect been excluded from effective constraints.

Since 1995, levels of domestic support, as measured by the current total AMS, have in many countries remained considerably below their allowed levels. In the years since 1995 for which notifications are available (for most countries up to 1999 or 2000), around one half of all WTO members with domestic support notifications used less than

⁵ For example, the 1998 average applied rate for agricultural tariffs for Latin American countries, at 13 percent, is less than one-third of the average bound rate of 45 percent.

⁶ There was a debate in the Committee on Agriculture on whether the "credit" provisions in Article 9.2(b) should allow countries to exceed their annual commitments on export subsidies if they had "underutilized" them in previous years. This practice was finally accepted, and used in a number of cases (particularly by the European Union).

⁷ Developing countries can exempt a somewhat larger set of policy instruments from reduction commitment. For such countries, investment subsidies for agriculture and input subsidies for low-income or resource-poor producers are exempt from reductions. In addition, support to encourage diversification away from illicit narcotic crops is exempt. These provisions are known collectively as Article 6.2 exemptions.

60 percent of their domestic support commitments. To some extent, the significant slack that exists in many countries' domestic support commitments is due to the use of a base period when support was unusually high. In the European Union, and in the past for the United States, the slack also reflects the use of the blue box to shelter a large part of actual support to farmers in the form of direct payments. The *de minimis* allowances also have provided a significant "loophole" for domestic support payments. In other cases, though, the low "utilization" of domestic support commitments reflects policy changes, when support has been decoupled from

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production and hence moved from the amber box into the green box. The US Federal Agricultural Improvement and Reform (FAIR) Act of 1996 is the most prominent example of a shift to the green box, though the subsequent "emergency" legislation introduced in 1998 and enshrined in the 2002 farm bill (the Farm Security and Rural Investment Act) reversed that trend and increased the payments under the amber box.

The fact that domestic support commitments have not (yet) proved restrictive may explain why there have only been two formal WTO complaints specifically challenging domestic farm policies, those brought by the United States and Argentina against Korean beef programs. The eligibility of policies for inclusion in the green box has yet to be challenged.⁸ Either the system is working rather well or the rules are deemed to have inadequate teeth to make a challenge worthwhile.⁹

⁸ The Brazilian challenge to the US cotton policy is in part a test of the domestic support provisions of the URAA, but it also involves the issue of whether the cotton subsidies rose to such an extent that they were no longer sheltered by the peace clause.

⁹ If a country is well within its allowable total AMS levels, it makes little sense to challenge green box policies to have them declared "amber."

Building on the URAA

The next stage of reform should build on the foundation of the URAA and continue the liberalization of markets and the reform of trade and domestic policies.

The Doha Round was intended as a further step in the incorporation of agriculture into the mainstream of trade policy. It was intended as an opportunity both to contribute significantly to the opening up of trade and to tidy up some of the loose ends from the URAA. Article 20 mandated such continued negotiations regardless of whether they were incorporated in a full round. However, in reality, any substantial reform needs to be anchored in a broader set of negotiations to allow for offsetting benefits for those who would have the most political problems with agricultural reform.

Two innovations in the URAA were intended to stimulate continued reform: the establishment of a WTO Committee on Agriculture and the inclusion of the peace clause to limit the applicability of the Agreement on Subsidies and Countervailing Measures (SCM) to agricultural policies.

The Committee on Agriculture has offered the possibility to WTO members of challenging the policy notifications of other members, but such challenges have rarely led to any changes. The committee has been more successful as a sounding board for ideas about further reform of the rules and has enabled early preparation for the current negotiations in a relatively informal setting. At its special session meetings, the committee has acted as the main negotiating body for the agricultural component of the Doha Development Round, though it failed to meet the deadlines agreed at Doha for the talks.

The peace clause has provided legal cover for the reform of domestic farm policy and has limited disputes over subsidy levels (Steinberg and Josling 2003). But the peace clause expired at the end of 2003, and its renewal would only have been possible if there had been substantial progress in the current negotiations. So it remains to be seen whether the possibility of litigation of domestic (and export) subsidies acts as a stimulus to further reform.

A New Framework

Countries have been searching for a framework for the next stage of agricultural reform to advance the process started in the Uruguay Round. To evaluate that framework, it is useful to specify the requirements for a constructive "phase two" of the incorporation of agriculture into the rules and practices of the trading system and the reduction of the

imbalance arising from the higher levels of protection in this sector.

A constructive framework for the talks should encourage substantial further reform of the trade rules to the extent that the necessary political will is present. At a minimum, such a framework should

- cap tariffs at a reasonable level and reduce the highest tariffs the most;
- enlarge TRQs and reform TRQ administration to encourage the filling of quotas;
- allow tariff- and quota-free access to developed-country markets for products of least developed countries;
- provide for a rapid phase-out of export subsidies and subsidized export credits on products of interest to developing countries;
- mandate a phase-out of all such subsidies to exports within a reasonable period;
- provide for significant reductions in trade-distorting domestic subsidies beyond the levels achieved in the URAA;
- prevent the circumvention of domestic subsidy limits via the redefinition of the blue box;
- ensure that only minimally trade-distorting subsidies qualify for the green box;
- provide for the full participation of developing countries, with due regard to their capacity to undertake reforms and to their particular needs; and
- avoid special rules for developing countries that allow them to opt out of the trade liberalization process and perpetuate a two-tier trading system for agricultural and food products.

Recent Framework Proposals

Many proposals have been made for the continuation of reform and further liberalization of agricultural trade, though they have varied widely in their degree of ambition. In the lead-up to the Cancún Ministerial, considerable progress was in fact made in clarifying the range of options. The chairman of the Committee on Agriculture, Stuart Harbinson, after a discussion with the delegates in January

2003, prepared a draft of the “modalities” that could be used to form the basis for an agreement. The Harbinson draft was presented for discussion at the February meeting of the committee and revised for the March meeting (WTO 2003a). The draft was not universally accepted as a basis for negotiations, and countries failed to meet the March 31 deadline for an agreement on the modalities. The Harbinson draft may in fact have been too detailed, even including possible quantitative targets. Countries expressed the desire for agreement on a framework before the precision of draft articles and numerical commitments. Subsequently, the chairman reported to the WTO Trade Negotiating Committee (TNC) in July, giving his own interpretation of the issues to be decided and the options available.

A flurry of activity in the month leading up to Cancún gave some hope that a framework agreement would emerge from the ministerial. On August 13, 2003, the European Union and the United

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States jointly proposed focusing on a feasible modalities framework before Cancún (WTO 2003b). One week later, Brazil, India, South Africa, China, and 16 other developing countries presented their own version of the “framework” for the agricultural modalities (WTO 2003c), in response to that of the European Union and the United States.¹⁰ Taking into account these new proposals, the TNC included in the draft document for Cancún that it presented to the General Council in late August an outline of a framework that could be agreed at the ministerial. The chairman of the General Council, Carlos Pérez del Castillo, in turn presented these suggestions to the ministers at Cancún as an annex to the Draft Ministerial Declaration (WTO 2003d).

¹⁰ Many of the Cairns Group countries associated themselves with the proposal, as did several non-Cairns Group WTO members. The group originally numbered 20 countries, but three others associated themselves with it (and one left), giving rise to the name of G-22. Since Cancún, at least three countries have distanced themselves from the group.

At Cancún, the discussion of the agricultural issues took up much of the time.¹¹ The G-22 still insisted that their draft be discussed along with the Castillo draft that they felt mirrored too closely the EU-US joint proposal. As with the other contentious areas of the talks, a facilitator was appointed to forge a compromise. Eventually, the facilitator for the agricultural discussions at Cancún, George Yeo, produced a draft modalities framework that was incorporated into another version of the Draft Ministerial Declaration, presented by the chairman of the General Council at the ministerial level, Luis Ernesto Derbez Bautista. The Derbez draft was widely criticized, contributing to the impression that countries were still far apart. The G-22 presented amendments to the Derbez draft, which would have met some of their concerns. Both the Derbez text and the G-22 amendments remained on the table when the ministerial was closed and provide a possible starting point for an agreement. Discussions since the Cancún Ministerial have not made noticeable progress, though Castillo incorporated some new ideas into a document presented to the TNC on December 15, 2003, and expressed the hope that negotiations could begin on bridging the remaining gaps and agreeing on a framework.¹²

Evaluating the Proposals

Are we reaching a convergence of ideas in the three areas of negotiations: market access, export competition, and domestic support?¹³ How do the recent proposals stack up against the minimum requirements suggested earlier? The four proposals discussed under the three areas (summarized in the appendix table) can provide a constructive framework for the talks. However, agreeing on a framework is only the first step, as countries must eventually commit to significant trade liberalization.

¹¹ One agricultural issue that engaged the attention of negotiators and commentators was that of cotton subsidies and their impact on farmers in developing countries. Four African cotton producers had launched a Cotton Initiative in the weeks before Cancún that called on the developed countries (the United States and the European Union in particular) to reduce cotton subsidies or to pay compensation. This issue is still under discussion, and it is likely that a specific arrangement on cotton subsidies may be necessary as part of the final agricultural package.

¹² At the time of writing (February 2004), the negotiations are about to restart under the new chairpersons that have been appointed for the various committees.

¹³ A recent paper that suggests several specific ways in which the Derbez text could be improved is available from the International Food & Agricultural Trade Policy Council, with which both authors are associated (IPC 2004).

Market Access

There is some convergence of ideas on the method of reducing tariffs. This is apparent from the Harbinson draft modalities document, which suggested a graduated formula for tariff cuts. However, the Harbinson suggestions for tariff-cutting had left both the United States and the European Union unsatisfied, with one arguing that the suggestions were not ambitious enough and the other indicating that they penalized countries that started with higher tariffs. The US-EU proposal of August 13 approaches the issue in a different way, by dividing agricultural commodities (tariff lines) into three groups: Tariffs in one group would be reduced on a Swiss Formula

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basis and those in the other on the basis of the Uruguay Round cuts. The third group would be granted duty-free entry. This categorization would allow all countries to shelter some sensitive products from sharp cuts in tariffs.¹⁴ In addition, the US-EU paper proposes a tariff cap, with the option of increasing TRQs to have an equivalent effect.

The G-22 broadly supports this three-tranche “cafeteria” approach for developed countries but adds the requirement of a steady increase in TRQs and the reduction of within-quota tariffs to zero. The G-22 formulation also allows the developing countries to choose among a Uruguay Round cut, a formula reduction, or tariff elimination for a certain percentage of their tariff lines, but they would not be subject to a tariff cap. In addition, the G-22 insists on the creation of a category of “special products” as had been introduced in the Harbinson draft.

The General Council chairman’s draft follows the EU-US paper quite closely with respect to the developed-country obligations but is significantly more lenient on developing countries. The “special product” category is retained from the Harbinson text, and developing countries are allowed to keep tariffs above the cap. The Derbez draft of September 13 adopts the EU-US formula for employing three

¹⁴ The US-EU proposal also includes a greater reduction in tariffs on goods of interest to developing countries.

reduction methods, suggests a target for the average tariff cut, retains the notion of a tariff cap with a TRQ option, and agrees with the Harbinson proposal to reduce tariff escalation. But within this proposal, a new element is introduced (in brackets, denoting further discussions) of a “very limited” number of products to be designated on the basis of nontrade concerns, which would not be subject to the tariff cap. The G-22 amendment to the Derbez text removes this bracketed provision, as well as dropping the provision for an average and a minimum cut for the Uruguay Round tranche (for developed countries) and omitting the tariffs that are eliminated from the calculation of the average overall reduction. It adds a provision that the reduction in developing-country tariffs be in three tranches each of the Uruguay Round type (i.e., no Swiss Formula and no zero tariff tranche) and inserts a condition that these reductions be tied to a particular percentage of the developed-country tariff cut.

As these recent proposals do not indicate the depth of cuts that could be negotiated, it is not clear whether they would constitute a significant reduction in barriers to trade. The key issues outstanding are therefore to do with the overall depth of cuts, including those in developing-country tariffs, the ability of countries to avoid opening markets by the allocation of products among the tranches, and the desirability of a “special product” category for reduced tariff cuts. The ability of developed countries to dilute the effect of tariff reductions by placing high tariffs in the Uruguay Round tranche should be resisted. Some agreed reduction in the average tariff (as opposed to the average tariff cut) would ensure real market opening even for sensitive commodities. Developing countries should be encouraged to significantly cut tariff levels in their own interest as well as to stimulate agricultural trade.¹⁵ But some degree of flexibility is probably necessary to reach agreement. The designation of a “special product” category, however, is a retrograde step that should be avoided if at all possible.

On TRQs, there is somewhat less convergence. The Harbinson proposal calls for a doubling of the TRQs, from 5 to 10 percent of consumption. The

more recent proposals have been less specific on TRQ expansion. The US-EU draft revives an idea from earlier in the negotiations (put forward by Canada) that countries could choose expansion of TRQs as an alternative to some part of their tariff reductions. The G-22 paper calls for an expansion of TRQs and an improvement in their administration but does not deal with issues such as within-quota tariffs or quota fill. The General Council chairman’s pre-Cancún draft picks up the idea of offering countries a choice between tariff reductions and greater market opening through TRQs. The Derbez draft, however, reverts to earlier formulations, including the reduction of in-quota tariffs and the negotiation of an expansion of TRQs. The G-22 amendment to the Derbez text strengthens the obligation to expand TRQs. The post-Cancún Castillo paper does not mention TRQs.

There seems to be general agreement that the expansion of TRQs provides an alternative way to open up markets protected by high tariffs that are unlikely to be reduced enough by any feasible tariff-cutting formula. This alternative use of the TRQs may reflect the reality of trade negotiations but can

The Derbez draft may need to be less permissive in granting exceptions from trade liberalization. With respect to export competition, it is in line with the views of most countries. But the most controversy exists in domestic support.

also detract from the main aim of increasing the TRQs and improving their administration. The system of TRQs was introduced to ensure that the high tariffs that replaced the quantitative trade barriers under the URAA did not reduce market access. They have been transformed from a device exporters support to ensure minimum access to an instrument importers favor to limit access to some maximum level. If importers make above-quota tariff reductions but keep quota volumes low, then market access will not have been improved. The objective should be to increase TRQs enough that the above-quota tariff is less relevant. Countries also need to agree on a way of ensuring quota fill through reductions in in-quota tariffs and improvements in the administration of the TRQs.

¹⁵ As there is often a significant difference between applied and bound tariff levels for developing countries, and as high tariffs often have considerable “water,” even the same percentage cuts for developing countries may have a smaller impact on trade. Special and differential treatment can be more effective if expressed in terms of tariff reductions in products of export interest to developing countries rather than allowing developing-country importers to maintain “unused” protection.

The proposals on Special Safeguards (SSG) laid out in the Harbinson draft and taken up in the Castillo and Derbez texts envisage that they be phased out for developed countries. The G-22 amendment to the Derbez text goes one step further and calls for a timetable to be established for the elimination of the SSG. The notion of introducing a developing-country safeguard “to enable developing countries to effectively take account of their development needs” has been a feature of the more recent proposals. The EU-US draft argues for the creation of such a safeguard for some products, and the G-22 and Castillo and Derbez drafts all call for the negotiation of such a safeguard. As currently being discussed, the modified safeguard, known as a special safeguard mechanism (or SSM), would apply to a defined range of products (perhaps designated at the 8-digit level) and would involve both price and quantity triggers.¹⁶

The concept of a special safeguard has political saliency as it is a way of reassuring domestic producers that they will have temporary protection against import surges and world price movements. The issues are whether to make such safeguards specific to developing countries and whether to limit them to particular commodities. The SSG was introduced primarily to complement the conversion of tariffs to nontariff barriers. It was the counterpart of the TRQs: one assuring some minimum access and the other some limited ability to raise tariffs. But if the concept of a safeguard is accepted, and the existing general safeguards and other trade remedies are deemed inadequate for agricultural markets, then a broad safeguard may be better. It is difficult to justify a system that favors trade remedies on some commodities and some countries.

Export Competition

The question as to whether export subsidies could finally be eliminated has dominated the negotiations on export competition. In search of a compromise, the Harbinson draft suggests further sharp reductions in export subsidies and their elimination within a few years, albeit with some flexibility. One-half of the export subsidies could be reduced at a slower rate. The US-EU proposal elaborates

on the Harbinson notion of flexibility by suggesting elimination of export subsidies on “products of interest to developing countries” and reductions in subsidies on other products using both quantity and expenditure limits, as in the URAA.¹⁷ The G-22’s suggestion is more explicit: All export subsidies should be eliminated even if those on products of interest to developing countries should go first. The Castillo and Derbez texts agree with the EU-US formulation, though they include the provision that the date for the eventual elimination of all subsidies can be discussed. The G-22 amendment to the Derbez text firms up that intention by calling for a date

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to be negotiated for the phasing out of export subsidies. Thus the long-term future of export subsidies is still a point of contention. Setting a date for the elimination of all export subsidies would be a major step in the direction of improving the trade rules for agriculture.

The Harbinson draft modalities paper supports the EU proposal for disciplining export credits (no hidden support) and food aid (where there should be no commercial advantage). In addition, it picks up on the notion of requiring private-sector exporters to compete with current “single-desk sellers” such as the Canadian Wheat Board, as well as on other disciplines on state trading exporters (no exports at less than the purchase price and no special financing). The US-EU proposal also addresses the export competition issues as a package, in accordance with the European Union’s suggestion: Disciplines on export credits would be introduced in parallel, also avoiding export credits on products that developing countries export. Disciplines would also be applied to food aid, and state-trading exporters would have to relinquish their monopoly positions. The G-22 draft calls for rules to discipline export credits and

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¹⁷ If the phrase “of interest to” were to be interpreted as all products that developing countries export, then it would cover grains and oilseeds as well as sugar but possibly not dairy products (that are exported primarily by other developed countries). But one could argue that export subsidies disrupt domestic markets in importing developing countries. In this case, the list would be longer, and the effect would be *de facto* elimination.

for the elimination of the subsidy element of such credits. State trading enterprises would similarly be disciplined. The Castillo draft suggests simultaneous elimination of the trade-distorting element of export credits and the export subsidies on those products agreed to be of interest to developing countries and suggests phasing out over time the subsidy provided by state trading enterprises. The Derbez text picks up on each of these issues, indicating the possibility of agreement once the more divisive question of the date for the elimination of export subsidies is settled.

Domestic Support

The issue of domestic support is becoming more divisive than those of market access and export competition. The United States and the European Union, in their earlier proposals, were far apart in their suggestions as to how to negotiate further reductions in trade-distorting domestic support. The United States proposed bringing down such support to a particular percentage of agricultural revenue; the European Union suggested cutting

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support across the board as in the Uruguay Round but by a higher percentage. The Harbinson draft's suggestions for domestic support reduction were somewhat more ambitious than the European Union's but followed a similar formula. Though still aggregated across commodities, the AMS would be cut by 60 percent from the 1999–2000 average over five years (but only 40 percent in 10 years for developing countries), and amber box payments by commodity would not be allowed to rise relative to the 1999–2000 base.

The US-EU proposal introduces a new idea, that of using “bands” analogous to the Harbinson market access formulation to limit domestic support. Those with high levels of support would reduce those levels by a higher proportion. This, together with the proposed reduction in the *de minimis* exemptions, would require significant reductions in domestic support. The G-22 agrees with the banding proposal but stipulates that reductions in the AMS be on a product-specific basis and in addition puts a limit on domestic support on export crops. The

Castillo draft does not include these refinements and follows the formulation of the EU-US draft, but the Derbez draft reinstates the notion of a cap on product-specific AMS levels. The G-22 amendment to the Derbez text adds the provision for negotiating down product-specific AMS levels and reinstates the earlier idea of a special discipline on subsidies for products that are a significant share of exports on the world market. The post-Cancún Castillo paper extends the discussion somewhat by raising the issue of whether countries might contemplate phasing out amber box subsidies altogether.

The need for reduction in the level of trade-distorting domestic support at a much more significant rate than in the Uruguay Round is generally agreed. Introducing some product-specific caps and reducing the *de minimis* exceptions are widely thought to be desirable. A further cut in amber box payments is therefore one area where there is apparent convergence, though the link with export shares may be a sticking point.

The same convergence is not yet evident in the treatment of the blue and green boxes. Under the Harbinson plan, the blue box would either be capped and reduced by 50 percent in five years (33 percent in 10 years for developing countries) or included in the AMS (i.e., the amber box) immediately for developed countries and after five years for developing countries. The US-EU proposal of August 13, 2003, argues for a redefinition of the blue box and for a limit of 5 percent of agricultural GDP to be imposed on spending. Recent changes in the European Union's Common Agricultural Policy have made it more possible for the blue box to be limited this way without necessitating major changes in domestic policy. The G-22 paper proposes the elimination of the blue box, but the Castillo draft adopts the US-EU approach, including a 5 percent cap and a declining budget ceiling for the newly defined blue box. The Derbez draft also incorporates these provisions, but the G-22 amendment argues for a cap of 2.5 percent and substantial linear cuts “with a view to phasing out” the blue box.

Disagreement over the fate of the blue box was one of the points of contention when the Cancún Ministerial ended. The attempt to redefine it to accommodate recent policy changes alerted developing countries to the significance of the boxes in domestic policy decisions. Rather than a simple mechanism for dealing with payments that were linked to price but tied to production constraints, the blue box would become a haven for payments linked to past acreage and yields and production levels. But such payments could still stimulate output and keep land under particular crops. It is important that the blue box not be transformed into

an easy way to shelter formerly amber box policies. The compromise could come in the form of significant and continued reductions in the blue box payments so that output-enhancing impacts could be minimized.

The discussion of the green box, until the run-up to Cancún, had been centered on the issue of expanding the criteria to include policies that responded to domestic demands to support “multifunctional” agriculture. The Harbinson draft modalities paper suggests no change in the green box criteria, except that the compensation payments for animal welfare regulations be added to those currently allowed in the green box for environmental payments and that the rules applying to developing

Perhaps the most difficult stage of the negotiations will be to put numbers in place of the Xs in the Derbez text. Thirty-one such numerical targets are missing.

countries be eased somewhat. The US-EU draft of August does not suggest major changes to the green box either. It was left to the G-22 to suggest a cap on certain green box expenditures (including direct payments, crop insurance, and disaster relief), but the Castillo draft makes no mention of these restraints. Instead, the issue of the green box criteria is left “open for discussion.” The Derbez draft also follows this path, leaving open the possibility of further restricting the green box policies by tightening the rules rather than by reducing the level of payments.

There has been no convergence of opinion between the developing and the industrial countries on green box support restrictions. Developing countries consider that the developed countries have been “box switching” to shelter domestic programs and avoid reductions. Though the URAA’s intention was to encourage the use of less trade-distorting instruments, it has instead engaged developing countries in the issue of total spending on agricultural policy in developed countries rather than in policy reform. Clearly, some forms of expenditure on rural public goods, such as research and infrastructure, are likely to continue. Other green box

payments are tied to compensation for price cuts or other forms of income support at least in principle for a transitional period. How to bring pressure to bear on countries to limit these latter payments is problematic: It would be counterproductive if trade rules were to make it less easy for these payments to be introduced as part of a shift from even more trade-distorting subsidies.

The resolution of the conflict over further constraints on all forms of domestic support, including any restrictions on green box spending, can only be found in a package of measures that satisfy the “bottom line” requirements of the major participants. All the current proposals envisage restraints on total trade-distorting support, defined as AMS plus blue box plus *de minimis* payments. Such a solution would keep the pressure on developed countries to further reform their farm policies so as to avoid passing the costs on to other countries. But in turn the developing countries have to accept that green box policies, if carefully monitored, are not necessarily incompatible with open markets and may be the only way to prevent more serious disruptions to trade.

What Is Needed Now?

The combination of the original proposals—the Harbinson draft, the Harbinson report to the TNC, the US-EU agreement, the subsequent set of G-22 suggestions, and the Castillo text—offered a reasonable range of options from which an eventual settlement could have emerged at Cancún. The Derbez draft includes elements of most of the earlier proposals, and the G-22 amendment revives others. But there were still enough points of disagreement that the framework could not be finalized. In the absence of any new and more radical suggestions, a final agreement will likely reflect some combination of these elements. The task for negotiators is to come up with a balanced package that at the same time is a major step toward a more open agricultural trade system.

Could the Derbez text (and the G-22 amendment) be used as a starting point for such a package? On tariff cuts, the three-tranche approach has widespread support, and if the depth of the cuts is significant enough (at the least it should be greater than agreed in the Uruguay Round), and if the tariff ceiling is set low enough, then this part of the package would be constructive. However, the Derbez draft may need to be less permissive in granting ex-

ceptions from trade liberalization: The introduction of special products, whether for developing countries or any country claiming “nontrade concerns,” would be a step backward.

The call for special and differential treatment should be met by positive efforts to bring more developing countries into the trading system and to ease the burden on their administrative capacity.¹⁸ This is better accomplished by offering improved market access and ensuring that liberalization is not retarded in products of export interest to developing countries. Tariff- and quota-free market access for exports from least developed countries should be added to the package, and middle-income developing countries should be encouraged to open their markets to such exports.

Other aspects of the market access proposals could be improved. Expansion of TRQs should remain a major goal and not just be treated as an option for importers wishing to avoid tariff cuts. The special agricultural safeguard should be made generally available, including to developing countries, and extended to all products. But it should be more rigorously monitored. In particular, price triggers need to be set at realistic levels to avoid increasing protection.

With respect to export competition, the Derbez text is in line with the views of most countries. If an expiry date can be agreed for export subsidies, and for the subsidy inherent in export credit and state trading policies, then this aspect of the agreement would give a major boost to the possibility of getting support for the package as a whole. Stronger disciplines on export restraints would assist in allowing developing countries to open markets.

The most controversy exists in domestic support. The problem arises with respect to programs that rely on direct payments and are geared to such ends as income stability. There is no agreement on how far the WTO rules should curb such policies. The Derbez text leans toward the EU-US formulation, which shelters many of these programs from cuts. The developing countries consider this approach to be at the heart of the problems they face in trade. In this case, economic logic and political perception diverge. Shifting to more decoupled payments has been constructive for the trading system, even though it has allowed developed countries to maintain generous farm programs. Though some

constraints may be necessary on many types of programs, significant restrictions on decoupled, well-targeted direct payments could set back rather than enhance the cause of trade liberalization by taking away the “exit strategy” for countries seeking to reform outdated price supports.

Perhaps the most difficult stage of the negotiations will be to put numbers in place of the Xs in the Derbez text. (Thirty-one such numerical targets are missing.) The country proposals and the Harbinson draft modalities paper did contain some numerical

Countries must balance the costs of adjustment implied by reducing import barriers with the benefits that they reap as exporters.

suggestions, which should form the basis of further discussions. If the three tranches of the Derbez draft tariffs were to be cut by 36 percent, brought down to 25 percent, and eliminated, respectively, the reductions would be at least as effective as the EU proposal and probably more ambitious than the Harbinson plan. Only if the Uruguay Round tranche were set too high (say, above 50 percent of tariff lines) would the Derbez formula be more modest, and in that case a low tariff cap would be needed to compensate.

With respect to export subsidies, the key questions raised by the Derbez draft are when to require their elimination and how to define which products are “of interest to” developing countries. The end date for all such subsidies would still have a symbolic meaning but be less significant to world trade.

For domestic support, the picture is somewhat cloudier. It is difficult to see an AMS reduction of less than 60 percent being either acceptable to non-subsidizing countries or helpful to world trade. But a cut of this magnitude would put additional pressure for maintaining the blue box and keeping the green box uncapped. So the Derbez draft’s modest target for AMS reduction may reflect the need to see the boxes as a whole and to choose between overall spending caps and instrument-switching as a way to stimulate trade and avoid distortions.

Can an agreement be reached along these lines? And would it be worthwhile if it could be reached? There seems little doubt that an agreement on a framework is within the grasp of negotiators if they got the signal from politicians that such an agree-

¹⁸ One particular issue in the context of special and differential treatment is whether all developing countries should be treated alike. As the category is self-defined (as opposed to the category of least developed countries), there is concern that some developing-country exporters may be relieved of obligations in sectors in which they are fully competitive.

ment would be valuable and if the necessary degree of mutual trust could be established among trade partners. Generating the political will needed for essential compromises will not be easy and may yet prove the downfall of the Doha Round. Elections in major countries in the next year make concessions more costly at home. But countries must balance the costs of adjustment implied by reducing import barriers with the benefits that they reap as exporters.

As they contemplate their longer-term economic development, most countries will conclude that the expansion of international markets provides a firm foundation for domestic policy, in agriculture and food as well as in manufacturing and services. In that regard, a continuation of the progress made in the Uruguay Round toward the extension of a rule-based trading system for agriculture and a significant reduction in trade barriers and trade-distorting domestic support would be a worthwhile contribution to economic growth and development.

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Appendix: Comparison of Market Access, Export Competition Support, and Domestic Support Proposals Discussed at Cancún

Area of discussion	EU-US joint proposal	G-22 proposal	General Council chairman's draft	Revised Cancún draft
Market access				
Tariff cuts	Three options for cuts: Uruguay Round reductions, Swiss Formula, and elimination; introduce a tariff cap or equivalent access via TRQs	Three options for cuts: Uruguay Round reductions, Swiss Formula, and elimination; introduce a tariff cap or equivalent access via TRQs	Three options for cuts: Uruguay Round reductions, Swiss Formula, and elimination; introduce a tariff cap or equivalent access via TRQs	Three options for cuts: Uruguay Round reductions, Swiss Formula, and elimination; introduce a tariff cap or equivalent access via TRQs; possible exemption from tariff cap for some products for nontrade concerns
Special and differential treatment	Seek duty-free access for x percent of imports from developing countries	Duty-free access for all tropical products and x percent of developing countries; reduce tariffs by Uruguay Round formula; designation of special products; no TRQ expansion for developing countries	Reduce tariffs by Uruguay Round formula, using three bands or mix of Uruguay Round and Swiss formulae; TRQs may be used in combination with tariff cuts for sensitive products; special products subject only to minimum linear cut and no TRQ; seek duty-free access for x percent of imports from developing countries	Reduce tariffs by Uruguay Round formula, using three bands; TRQs may be used in combination with tariff cuts for sensitive products; special products subject only to minimum linear cut and no TRQ; discuss tariff cap for developing countries
TRQs	Use in combination with tariff cuts to improve access	Expand TRQs; eliminate in-quota tariffs; strict rules for administration	Use in combination with tariff cuts to improve access	Reduce in-quota tariffs; negotiate TRQ expansion
Safeguards	Discuss SSG for developed countries; create SSG for some products for developing countries	Discontinue SSG for developed countries; negotiate SSM for developing countries	Discuss SSG for developed countries; establish SSM for developing countries	Discuss SSG for developed countries; establish SSM for developing countries
Other		Reduce processed tariffs proportionately	Address tariff escalation; take into account importance of preferences	Tariff escalation reduced through Harbinson plan
Export competition support				
Export subsidies	Eliminate export subsidies on products of interest to developing countries; reduce other export subsidies by Uruguay Round formula	Eliminate export subsidies on products of interest to developing countries; eliminate export subsidies on other products over x years	Eliminate export subsidies on products of interest to developing countries; reduce other export subsidies by Uruguay Round formula; discuss date for elimination of export subsidies	Eliminate export subsidies on products of interest to developing countries; reduce other export subsidies by Uruguay Round formula; discuss date for elimination of export subsidies

Export credits	Eliminate subsidized export credit on products of interest to developing countries; reduce subsidies in export credit in parallel with export subsidies	Discipline by rules; reduce and eliminate subsidy component	Eliminate subsidized element of export credit	Eliminate subsidized export credit on products of interest to developing countries; phase out export credits on other products
Food aid	Prevent commercial displacement by food aid	Prevent commercial displacement by food aid	Prevent commercial displacement by food aid	Prevent commercial displacement by food aid
State trading enterprises (STEs)	Discipline STEs	Discipline by rules; reduce and eliminate subsidy component	Eliminate subsidized element of activities of STEs	Eliminate subsidized element of activities of STEs
Export restrictions				Strengthen disciplines on export restrictions
Domestic support				
Amber box	Reduce AMS by significantly more than Uruguay Round reductions; greater efforts by countries with higher amber box payments; reduce amber box plus blue box and de minimis payments below 2000 AMS levels	Reduce AMS on a product-specific basis; greater efforts by countries with higher amber box payments; down-payment in first year; higher reductions for commodities important in export markets; reduce sum of AMS and de minimis	Reduce AMS by significantly more than Uruguay Round reductions; greater efforts by countries with higher amber box payments; reduce amber box plus blue box and de minimis payments below 2000 AMS, blue box, and de minimis levels	Reduce AMS by significantly more than Uruguay Round reductions; greater efforts by countries with higher amber box payments; cap product-specific AMS levels; down-payment in first year; reduce sum of AMS and de minimis
Blue box	Redefine to remove production-limiting requirements based on fixed areas and yields and on limited quantities; cap payments to 5 percent of value of agricultural production	Eliminate blue box	Redefine to remove production-limiting requirement, include only payments based on fixed areas and yields and on limited quantities; cap payments to 5 percent of value of agricultural production and reduce	Redefine to remove production-limiting requirement, include only payments based on fixed areas and yields and on limited quantities; cap payments to 5 percent of value of agricultural production and reduce
Green box	No changes mentioned	Cap and/or reduce payments in developed countries	Discuss green box criteria	Review green box criteria
<i>De minimis</i> provisions	Reduce the level of <i>de minimis</i> payments	Reduce the level of <i>de minimis</i> payments for developed countries	Reduce the level of <i>de minimis</i> payments	Reduce the level of <i>de minimis</i> payments

Source: Authors' compilation based on proposals and drafts cited in text, and analysis by the International Food & Agricultural Trade Policy Council.