Domestic Support and WTO Negotiations from Developing Countries’ Perspectives

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I. Introduction

In anticipation of the completion of the Uruguay Round (UR), the WTO began the initiations for the new round of negotiations. After a long three years of arduous negotiations, the fourth WTO Ministerial meetings in Doha, Qatar in November 2001 finalized the agenda to launch the new multilateral trade round. During the tenuous negotiation period, agriculture was at the forefront because of developing countries’ disenchantment with the raw deal they got from the Uruguay Round Agreement on Agriculture (URAA), in particular with the rich countries’ massive domestic subsidies (Coleman and Meilke; The Economist 1999a). The three pillars of the URAA aimed at liberalizing agricultural trade barriers are market access, export subsidies, and domestic supports. Though limited progress have been made in all three fronts, agricultural subsidies seem to escalate through various means. As a result developing countries are concerned with domestic support measures because developed countries’ high domestic subsidies and the resulting over production and exports unfairly affect the developing countries’ agriculture (Taulananda; The Economic Times 2001a and 2001b).

The purpose of this paper is to review the recent developments by focusing on the trade distorting effects of developed countries farm policies and the progress made in the current negotiations. The rest of the paper is organized as follows: Section II identifies the factors behind the setback of the negotiations in the Seattle meeting. Section III presents the URAA commitments for domestic support policies. Section IV explains how developed countries circumvented the URAA reduction requirements. Section V identifies the adverse impacts of developed countries massive subsidies on poor countries. Section VI briefly points out why the developing countries were averse to trade reforms. Section VII observes the obligations of developed countries to support their agricultural industry. Section VIII
presents developments in the WTO agricultural negotiations in 2000 and 2001. Section IX covers some of the agricultural proposals put forth by the WTO member countries. Section X focuses on the agricultural agenda formulated in the Ministerial Declaration at the Doha meetings. Section XI discusses the tasks ahead for successfully completing the negotiation of the new round. Section XII examines the U.S. farm bill provisions and implications for the WTO negotiations. Section XIII provides concluding remarks.

II. Setback in Seattle

The debacle to launch a new round of trade liberalizations in Seattle in 1999 was not caused by the overwhelming agitations by the mass protestors as perceived by the public but by the uncompromising stance of the member countries over their competing priorities. In particular lack of consensus between developed and developing countries over several divisive agenda attributed to the collapse (The Economist, 1999a, 1999c, and 2001c; Huff; Coleman and Meilke; Dunphy). These thorny agendas include: environmental regulations, labor standard, restrictions on textiles imports, implementation issues over the URAA, food security, lack of openness in the WTO negotiating process, etc. However, one of the most bitter disputes was over the developed countries’ domestic farm supports, with the developing countries insisting on dismantling these subsidies and the developed countries’ intransigence in relinquishing these supports (See Coleman and Meilke; Dunphy; Huff; Kleckner; Taulananda; The Economic Times 2001a and 2001b; The Economist 1999a, 1999b).

III. URAA Disciplines on Domestic Supports

To understand the anguish of the poor countries over rich countries’ domestic supports, it is important to comprehend the domestic policy disciplines of URAA and how rich countries circumvented
URAA provisions of domestic supports are based on the traffic light analogy of red, amber, and green boxes. The **Red Box** no longer exists since the prohibited level of farm subsidies in this box are not allowed under WTO rules. The **Amber Box** contains policies that are most trade distorting and measured by the Aggregate Measurement of Support (AMS). The AMS is computed as the difference between the government administered price and a fixed external reference price times the quantity of production. The fixed external price is the average f.o.b price in years 1986-1988. Then total AMS is computed as the sum of AMS of all agricultural products. Developed countries are required to reduce the total AMS by 20% over 6 years (1995-2000) and developing countries are obligated to cut the total AMS by 13% over 10 years (1995-2004). The reduction is not required on a commodity-by-commodity basis. In particular, a commodity can be excluded from this reduction if the domestic support it receives is less than 5 percent of the total value of production. Also, domestic policy that is non-trade distorting need not be reduced.

Two sub-categories under the Amber Box are the Blue Box and *de minimis* policies. The **Blue Box** covers support payments exempt from URAA reduction commitments but limit production. Example of these policies are direct payments for set aside and quotas, which impact production and thus trade, yet they are spared from reduction commitments. The *de minimis* rules specify the levels of support that can escape commitment (10% of developing countries’ and 5% of developed countries’ value of production).

The **Green Box** includes support payments that are supposed to have no or very minimal effects on trade. These subsidies are to be paid by government and should not result in higher consumer prices.
Also, these subsidies are primarily direct income supports and are not intended to cover a particular product and augment production and prices. Examples include expenditures on disaster relief, research, food security, stocks, conservation programs, etc. Finally, “The Due Restraint Peace Clause” (Article 13) restricts the use of countervailing duties by poor countries to counteract Green Box supports. Thus, the Peace Clause safeguards the interests of the rich countries by preventing the poor countries from retaliating during the implementation period. (See Kennedy, Brink, Dyck, and MacLaren; Blanford; and Hobbs and Kerr for more details of the URAA provisions.)

IV. How Developed Countries Circumvented the Disciplines

Under the URAA, AMS was to be reduced by 20% from the 1986-88 base level. But the base level of support was so high that the reduction commitments are largely meaningless, (Rude and Meilke). Since AMS did not identify sector specific reductions, it allowed countries to reallocate supports among commodities and permit an increase in trade-distorting policies for a particular product at politically opportune times (Blanford; Kennedy, Brink, Dyck, and MacLaren; Burfisher et al.). The poor countries’ wrangling over the price supports also arose from the range of instruments that rich countries use under the Blue and Green Boxes to circumvent the reduction commitments. The U.S. 1996 Farm Bill and the EU’s “Agenda 2000” have shifted support payments from Amber to Blue and Green Boxes. Also, the \textit{de minimis} provisions provide opportunity for the high level of domestic supports (Kennedy, Brink, Dyck, and MacLaren).

Poor countries also took note of rich countries’ ever escalating (instead of declining as required by the URAA) domestic supports and the resulting endemic distortions in the world market. The domestic supports measured using producer subsidy equivalents (PSE) went up by 29% in EU and an
 alarming 260% in the United States from 1995 to 1999 (Blanford). In 2000, OECD countries spent $327 billion on agricultural supports (The Economist 2001b). Over 48% of the EU’s budget is spent on common agricultural policies’ farm subsidies, and EU’s market-distorting price supports account for 65% of subsidies (The Economist 2001a). The U.S. “Freedom to Farm” bill of 1996 to wean farmers from government dependency has failed to work; instead, government’s role in subsidizing agriculture has exploded and direct payments to farmers have tripled since 1996. The U.S. government has given more money to wheat, corn, soybean, rice, cotton, and oat producers than ever before (Spokesman Review 2001a). In the fiscal year 2000, the U.S. government spent about $27 billion in farm subsidies, and federal payments totaled about half of the farm income in the United States. The U.S. emergency assistance payments rose from $1.86 in 1998 to $7.66 in 2000 (Spokesman Review 2001b). In 1999, every full time farmer in Norway received about $33,000, Switzerland $32,000, Japan $26,000, the United States $21,000, and the EU $17,000 in subsidies (The Economist 2001a).

Green Box subsidies enlarge the domestic supports through direct payments, which have the potential to expand output (Blanford). Whereas price-related subsidies directly impact market prices, direct payments indirectly distort market through capital investment, enhanced production, and lower prices in the following years (The Economist 2001b). Of the $59 billion in domestic supports by the United States in 1996, 88 percent come under Green Box and thus are exempt from reductions (Rude and Meilke; Blanford). Of the $95 billion ECUs of domestic supports by the EU in 1996, 46 percent come under Blue and Green Boxes and thus are exempt from reductions (Blanford).

**V. Adverse Impacts of Rich Countries’ Farm Subsidies on Poor Countries**

Developing countries are predominantly agricultural, with 40% or more of their GDP generated
from agriculture (McCalla). About 70% of the world’s poor depend on the agricultural economy for employment (McCalla, The Economic Times, 2001a). In addition, poor countries experience chronic unemployment problems. The human aspects of structural adjustments which result from the flood of imports from rich countries are so significant for poor countries to ignore since agriculture is a way of life for the majority of the population (The Economic Times 2001a and 2001b). Unlike rich countries, poor countries cannot afford to provide trade adjustment assistance to 70% of their population. The massive economic dependence on agriculture, livelihood of a vast farm population, and persistent unemployment problems force poor countries to resist rich countries’ domestic supports.

Developed countries are the ones mostly use domestic support policies, which cause low prices, and implicitly, tax on poor countries’ agriculture (Diao, Somwaru, and Roe). All OECD countries subsidize their domestic agriculture in varying degrees (Meijl and Tongeren). Though some poor countries subsidize agriculture, the magnitude of the subsidies does not come even remotely close to the rich countries’ farm outlays. The OECD countries spend $1 billion a day on domestic agricultural subsidies (Moore), and the total payments exceed the entire Africa’s GDP (The Economist 2001b). People in sub-Sahara Africa live on less than $2 a day but EU provides subsidy of $2 for every cow (FitzGerald). Domestic supports in the United States, Canada, Europe, and Japan account for about 80% of the world’s total (The Economist 2001b).

In 1997, more than half of EU’s, Japan’s, and U.S. domestic supports are trade distorting (The Economist 2001b). Developed countries’ farm program keeps the domestic price artificially at high level. For example, EU prices of lamb, butter, and sugar are all more than twice the world market price (the Economist 2001b). Such artificial high domestic price can turn the EU from importer to exporter, as
shown by the trade reversal in the figure below.

If the free trade price were to prevail in the EU, the EU might be importing at $P_w$. Instead, the domestic price support at $P^*$ could cause the EU to produce more and dispose the surplus of $cd$ amount in the world market using export subsidies. Poor countries felt that rich countries want to have it both ways, i.e., provide high domestic support and dump the excess supply in the developing countries (Burfisher et al.). The developed countries’ policies, as expounded by Coleman and Meilke and the Economist (2001b), gradually eroded poor countries’ trust in the global trading system and was partly responsible for the well publicized collapse of the negotiations in Seattle.
Elimination of agricultural distortions in the long run will increase the world welfare by $56 billion annually (Burfisher, et al.). The benefits of agricultural trade liberalizations not only accrues to poor countries but also to rich countries because of reduction in food prices. Reduction of either global farm policies or manufacturing tariffs by 40% augments the world welfare by same amount, even though manufacturing value added is two-and-a-half times larger than that of agriculture (The Economist 2001d). This highlights not only the importance of agriculture but also the degree of massive distortions in this sector. If rich countries were to remove the farm subsidies, poor countries would benefit by more than three times the amount of all the foreign aid they receive (The Economist 2001b).

VI. Developing Countries’ Aversion to Trade Reforms

The unanimous economic thinking is that the developing countries will gain more from a comprehensive freer trade polices than the developed countries (Stiglitz). Most developing countries are aware of this potential gains; yet, they are averse to trade reforms because, as elucidated by McCalla, of the predatory practices of the large rich countries. Stated differently, poor countries want a free trade that eliminates rich countries’ distorted policies and questionable bail outs but not an uneven playing field that will allow rich countries to subsidize their agriculture and dump the excess production in the poor countries. Poor countries realize that the UR did not deliver anticipated gains as rich countries continue to protect their domestic agriculture (Huff; The Economist, 2001c).

VII. Developed Countries Obligations to Their Producers

The legislators in the developed countries are under intense pressure to support the farmers in their countries. In wake of depressed farm prices in the last few years, farmers in the developed countries are under severe financial stress. Cuts in farm productions and financial losses also affect other
markets in the rural economy such as from input markets, lending institutions, and output sales markets. Consequently, lawmakers are increasingly concerned about the welfare of their farming constituencies and the rural economy and justify the need for domestic farm programs. Thus, lawmakers in the developed countries are obligated to meeting the important societal goals to save the farming communities, rural employments, and businesses and improve the environmental standard. For example, in 2000, the United States spent $7.66 billion in emergency assistance payments to farmers (Spokesman Review 2001b).

VIII. Progress in 2000 and 2001

The derailment of the Seattle meetings led the WTO to establish a Special Committee on Agriculture, court the developing countries back to the negotiating table, and attempt to regain the poor countries’ trust in the global trading system. Agricultural negotiations were held over two phases. The first phase was carried out under the guidance of the Agricultural Committee over six Special sessions in 2000 (March, June, September, and November) and 2001 (February and March). During the first phase, members submitted proposals detailing their starting positions, reviewed, discussed, and provided rebuttals on each of the proposals. In the second phase, six more meetings (from March 2001 to February 2002) were held to negotiate specific topics and technical details. The purpose of these meetings were to develop specific proposals and reach a consensus on agricultural agreements.

IX. Interim Agricultural Proposals

Many countries, including the United States, EU, Cairns group, India, and other developing countries, submitted interim proposals in the first phase of the negotiations. The U.S. proposal divides the domestic supports into exempt and non-exempt measures. The exempt measures are continuation of
programs in the Green Box and also maintaining the *de minimis* provisions, which will have minimal trade distortions. The exempt measures allow programs deemed essential to the rural development and food security goals of developing countries, and also to environmental protection, farm income safety, technology adoption, investment, and infrastructure improvement. India and Hungary positively viewed the part of the U.S. proposal pertinent to developing and transition countries. The non-exempt measures will reduce AMS to a fixed percentage of the member’s value of total agricultural production (WTO 2000a, 2000b). The URAA required a AMS reduction of 20% by the developed country and 13% for developing country. The U.S. proposal for non-exempt supports calls for deeper cuts by the countries with large domestic subsidies. Japan and Norway, given their rich tradition of supporting their farmers, are critical of U.S. proposals and do not want a major overhaul of the URAA.

The EU’s proposal calls for maintaining the Green and Blue Box policies, which EU claims are transparent and market oriented (WTO 2000c). In this regard, the EU proposal vastly differs from the U.S. proposal, and it is not surprising given the EU’s large domestic subsidies using Green and Blue Box policies. The EU recommends lowering AMS and *de minimis* supports. The EU wants to apply specific discipline to Amber Box subsidies aimed at expanding exports to compensate for market price gyrations. The EU, in appeasing the developing countries, promotes rural development, food security, and poverty alleviation. The EU’s goal of supporting agriculture to preserve the non-trade concerns and multifunctionality role contrasts its call for reducing AMS measures.

India’s proposal called for rich countries to reduce all of their domestic supports by 50 percent by the end of 2001 from their 2000 level and eliminate within a maximum period of 3 years (The Economic Times 2001a). India also proposes that direct, decoupled, insurance, income safety payments
should be included in the non-product-specific AMS and should be reduced to the URAA *de minimis* level.

Developing-11 (Cuba, Dominican Republic, Honduras, Pakistan, Haiti, Nicaragua, Kenya, Uganda, Zimbabwe, Sir Lanka, and El Salvador) countries totally overwhelmed by the URAA, particularly with the Green Box subsidies that expand the rich countries’ domestic supports through direct payments (Blanford), want a complete overhaul of domestic support measures. Their proposal, which significantly differs from the U.S. proposal, combines the traffic light analogy of Boxes into just one general Subsidy Box that will allow a common level of support. Their proposal will also have an additional Development Box which contains import controls, tariff barriers and *de minimis* level of domestic support to protect the interest of the poor countries. See Kennedy, Brink, Dyck, and MacLaren; Hobbs and Kerr; and Miner for a summary of the various proposals and rebuttals by other countries.

X. New Round

The past two years of grueling negotiations culminated with the fourth Ministerial meetings (in Doha, Qatar in November 9-14, 2001) finalizing the agenda to launch the new round of global trade agreements after tortuous wrangling over a host of uncompromising issues. Since majority of the WTO members are developing countries, the Ministers, unlike in the previous rounds, placed the developing countries’ interests at the forefront. The ministerial declaration specifically takes into account of the special needs of the developing countries by noting that

*We recognize the particular vulnerability of the least-developed countries and the special structural difficulties they face in the global economy. We are committed to addressing the*
marginalization of least-developed countries in international trade and to improving their effective participation in the multilateral trading system.

The work program for agriculture commits to establish a fair and market-oriented trading system through a program of fundamental reform encompassing strengthened rules and specific commitments on support and protection in order to correct and prevent restrictions and distortions in world agricultural markets;

to comprehensive negotiations aimed at: substantial improvements in market access; reductions of, with a view to phasing out, all forms of export subsidies; and substantial reductions in trade-distorting domestic support;

that special and differential treatment for developing countries shall be an integral part of all elements of the negotiations.

The work program sets the following time schedule for negotiation: March 31, 2003 for establishing the modalities for the further commitments; mid 2003 (date is not fixed yet) fifth Ministerial Conference in Mexico for submitting the comprehensive draft schedules; and January 1, 2005 for concluding the negotiations.

XI. Tasks Ahead in the Negotiations

Review of the interim proposals suggest that developing countries and Cairns group want a reduction in domestic supports, but developed countries (the United States, EU, Japan, Norway and Switzerland) oppose cuts in one or more of these policies (Hooke). These disagreements clearly indicate that the controversy surrounding the agricultural trade liberalization will continue to swirl (Hobbs and
Agricultural trade’s most fundamental problem lies at the domestic level because the most egregious trade distortion is domestic support, which most developed countries refuse to cut, let alone, to eliminate. Thus, the agreement on agricultural trade negotiations will be one of the most contentious issues. The negotiations over domestic support is not only challenging but will overshadow the other agendas and become increasingly important issues for the WTO negotiations (Rude and Meilke; Blanford). If the developed countries’ resist to reduce domestic farm subsidies, the agreement could be elusive since there exists irreconcilable difference between developing and developed countries over the provisions of domestic supports (Moehler). The developing countries are better organized and informed than they were in the previous rounds, and will not accept an agreement sown up between the United States and EU (The Economist, 1999a). But, the rich countries do not seem to heed the poor countries’ pleas to phase out the domestic farm supports. For examples, the United States plan to spend about $74 billion in the new farm bill. The U.S. law makers often state that they will not allow the U.S. farm policy to be written in Geneva by the WTO. Complexity of issues surrounding domestic farm policies in the United States, EU, Japan, and Korea can scuttle the negotiations. Free trade aims to bring down the subsidies, whereas lawmakers in these countries try to augment the subsidies to satisfy the needs of their producers.

As laborious and treacherous as it was to successfully launch the new round, the Ministers had agreed only on the agenda. Also these agendas establishes only the premises and rules of the game for
negotiating commitments to liberalize trade and much needs to be accomplished to complete the agreement. Between the beginning of the negotiations, that is now, and the end of negotiations, January 1, 2005, a myriad of snags and obstacles will arise, which could effectively scuttle the whole process. Though WTO’s goal is to complete the negotiations within three years, if the UR (which took eight years) experience is any indication, the negotiations process could drag for a longer period. In the worst case, the whole negotiations could crumble under the weight of too many contentious issues (The Economist, 2001d).

One possible approach toward successful negotiations in agriculture is to target the problem areas in the URAA (Kennedy, Brink, Dyck, MacLaren). Five important categories for negotiation are 1) domestic support, 2) export competition, 3) market access, 4) non-trade and multifunctionality concerns, and 5) special and differential treatments for developing countries. In the domestic support category, issues include AMS versus commodity specific commitments and reducing trade-distorting Amber Box domestic supports; deciding on policies and supports to come under the Blue and Green Boxes; retaining the existing provisions and/or reducing them in the de minimis categories; addressing the Due Restraint Peace Clause, non-trade environmental concerns; ways to financially help the depressed farm economy; and abolishing the “Due Restraint Peace Clause,” which may eliminate much of the incentive to shift policies from Amber to Green Boxes. In summary, for negotiations to succeed, Europe, Japan, and America need to reduce their agricultural subsidies and open up their markets for poor countries’ farm exports, and rich countries have to earn the trust of poor countries who remember bitterly the UR’s benefits were mostly reaped by the rich countries.

XII. The U.S. Farm Bill
The U.S. farm bill passed in May 2002 budgets $180 billion over a ten-year period. This farm bill will increase the subsidies by more than 80 percent and spend $83 billion more than the current programs. The provisions of this bill center around production flexibility contracts, marketing loan programs, loan deficiency payments, decoupled transition payments, and countercyclical payments. Loan rates for corn, wheat, oats, barley, and sorghum are increased. The farm bill brings back the target price program existed before 1996, which provides income support if prices fall below a specified level. The biggest beneficiaries are producers of traditional crops (corn, cotton, rice, wheat, and soybeans) and large agribusiness firms. This bill also introduces new subsidies for crops such as lentils, chickpeas, and peanuts. New subsidy programs also cover dairy, honey, wool, and mohair. This farm bill extends sugar price support programs by limiting imports.

The huge subsidy provided by the farm bill lead Rep. Pat Tooney, R-Pa., to criticize the bill as “a step toward Soviet-style agriculture. We’re in danger of turning farmers in to dependant serfs of the federal government.” Senator Charles Grassely, R-Ia., observed that the farm bill might break the WTO obligations. The provisions of the farm bill are not consistent with the WTO agenda established at the Doha meetings because the current WTO negotiations call for deeper cuts in all form of domestic supports (not just the amber box programs) including direct payments. The U.S. trading partners around the globe including, the European Union, Cairns group, Mercosur members, and several developing countries strongly denounced the U.S. farm bills because of the enlargement of the domestic supports. These countries accuse the United States for not holding up to the U.S. negotiators’ commitments to the current WTO negotiations. It is widely viewed that the U.S. farm bill will hurt developing countries agriculture. Consequently, the U.S. negotiators have difficult task of defending the domestic farm
policies and at the same time convince the WTO members to move toward non-distorting policies. Since the proposed farm bill expenditures will not meet substantial reduction requirements, it remains to be seen whether United States (and other developed countries) will scale back their farm program expenditures or WTO will relax its agenda of deeper cuts.

**XIII. Conclusions**

Because of the unsatisfactory outcomes of the Uruguay Round, the developing countries have heightened their concerns over agricultural negotiations in the current round of negotiations. This paper summaries the developments since the Seattle meetings by detailing the developing countries’ views, developed countries’ farm subsidies, current status of the negotiations, the agenda for the new round, tasks ahead in completing the negotiations, and the new U.S. farm policies.
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