3

The Current Status of Agricultural Trade Reform

Progress in agricultural trade reform can be judged by contrasting the current situation with that prevailing prior to the start of the Uruguay Round. World markets for the major temperate-zone agricultural products had been in disarray for the previous two decades, as the surpluses of the 1960s gave way to shortages in the 1970s, with the vagaries of weather exacerbated by destabilizing trade policies.[1] The 1980s began with a brief grain shortage caused largely by a surge in demand but made worse by the reaction of the major countries. A long slump in the prices for the main traded commodities followed.[2] By the mid-1980s, soaring budget costs from farm programs were conflicting with pressures for fiscal restraint. It became widely recognized in the United States and Europe that the situation was rapidly becoming untenable.

This crisis had already been studied, and remedies had been discussed in international organizations. The two most significant preparatory exercises were the mandate to the OECD to investigate the link between domestic policies and agricultural trade (the 1982 Trade Mandate) and a decision in the same year to establish a Committee on Trade in Agriculture (CTA) within the GATT. These actions led to the incorporation of agricultural trade in the stated goals for the new Uruguay Round of trade

1. D. Gale Johnson (1975) offers the classic analysis of the problems of agricultural trade over this period.

2. The behavior of commodity markets over this period is discussed fully in Hathaway (1987). See also Josling, Tangermann, and Warley (1996, chapter 6).

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negotiations, an OECD ministerial declaration in May 1987 supporting the development of more market-oriented agricultural policies, and the July 1987 agreement at the Tokyo Summit to give the issue high priority.

This chapter discusses the outcome of this flurry of activity. The first part deals with the Uruguay Round as the major new multilateral development. A discussion of domestic policy reform in some of the major countries follows. A new element, which would not have been considered significant in the mid-1980s, is the growth in size and scope of regional trade agreements. These agreements have begun to play a more substantial role in the reform of agricultural trade policy as they incorporate agricultural trade. Whether this role supports or conflicts with the multinational reform process is discussed later.

The Uruguay Round as a New Point of Departure

From the start, agriculture played a central role in the Uruguay Round trade negotiations.[3] The emphasis on agriculture came in part from the countries who saw closed markets and restricted trade opportunities as anomalous with the more liberal trade regime in manufactured goods. It also stemmed in part from the frustration caused by rules for agricultural trade that were not precise enough to be useful either in preventing disputes or in resolving disputes that had arisen. But the main emphasis came from a widespread sense that the systems of domestic farm support had become too costly and troublesome, that these programs were largely responsible for the chaos in world agricultural trade, and that an international solution to these domestic problems was necessary to provide the basis for modified trade rules and an agreement to lower external protection.[4] This link with domestic policies set apart the Uruguay Round talks on agriculture from previous negotiations. However, the link also prolonged negotiations and made the final agreement so difficult to reach.

The focus on domestic agricultural policies was necessary to resolve the fundamental problems that had beset the GATT's treatment of agricultural trade from the start. Unlike many areas of trade policy, it has never been easy to separate agricultural trade rules from the conduct of domestic farm policy. Given the political strength of groups that had a stake in these domestic policies, trade policy tended to take a back seat. Had the domestic farm policy not been tackled in the Uruguay Round, any result-

3. This discussion of the URAA is based in part on IATRC (1994).

4. The role of domestic policies and the anomalies in the GATT's treatment of agriculture are documented in Hathaway (1987).

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ing trade agreement would have been of doubtful value to world agricultural markets. Accordingly, two main criteria in evaluating the round are the extent to which domestic agricultural policy reforms were encouraged by the negotiations and the extent to which these policies are now effectively constrained by the terms of the agreement.

The Uruguay Round goes back to 1982, when protectionist sentiments were rising, particularly in the United States, where Japanese competition was fierce.[5] The Tokyo Round concluded in 1979 with a somewhat weak agreement on curbing nontariff import barriers and the negotiation of a number of codes to tackle issues such as antidumping measures, the use of export subsidies, and the existence of heterogeneous standards. However, the codes had not proved a great success, and nontariff barriers proliferated. Agricultural trade had benefited a little from the reduction of some quantitative trade restrictions, notably by Japan, but no substantive degree of liberalization had been possible. The two commodity agreements concluded in the Tokyo Round, for dairy products and for beef, were not designed to liberalize trade. And an agreement on the international management of grain stocks had proved elusive. With high world agricultural prices at the start of the Tokyo Round in 1974, market liberalization appeared less pressing than stabilization.

Agricultural markets were again firm in the period after the conclusion of the Tokyo Round; major countries experienced record agricultural export earnings in 1981. This contributed to renewed concerns about food shortages in world markets. Against this backdrop, the early plans for agriculture in the upcoming round were focused on rule changes that would assist the settlement of disputes. A GATT Committee on Agriculture was appointed in 1982 to study such rule changes.

By 1986, the situation had changed dramatically. World prices, on a downward slide, reached their lowest point in many years. US agricultural exports fell precipitately, and support costs escalated. Export subsidy programs were reintroduced, and trade disputes became more common and more bitter. In the European Community, subsidized exports became the main outlet for surplus production, at an increasingly high cost to the budget of the European Community. Small and medium-sized exporters of agricultural goods increasingly began to suffer under the burden of the export market competition of the two agricultural "superpowers." In this situation, the prospect of the Uruguay Round as a solution to the disarray in world markets began to look more attractive. By the time that governments met in Punta del Este to launch the Uruguay Round in September 1986, a consensus had been reached to reform agricultural policies in order to liberalize agricultural trade.

5. Schott (1994) discusses the achievements of the Uruguay Round as a whole. The story of the treatment of agriculture in the GATT, from its early days through the Uruguay Round, is found in Josling, Tangermann, and Warley (1996).

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The negotiations fall conveniently into three phases. In the first phase, which began in 1986, countries exchanged ideas on how to improve agricultural trade and how negotiations should proceed. In July 1987, the United States unveiled a proposal for the improvement of the trade system that would eliminate all trade-distorting farm programs over a 10-year period. Only what became known later as "decoupled" payments (those not tied to output), together with genuine food aid and domestic nutrition and poverty programs, would remain. The OECD PSE measure, which aggregates the effects of diverse policy instruments into a subsidy-equivalent, was suggested as a possible mechanism to embody these commitments. The newly formed Cairns Group of 14 small and medium-sized exporters followed with a proposal that would have immediately froze price supports and then gradually reduced them until a new set of rules could be introduced to regulate agricultural trade. The European Community countered with a two-part proposal to negotiate reductions in support levels, but only after action in the short run to shore up world prices.

This phase produced more heat than light and culminated in a stalemate at the ministerial meeting in Montreal in December 1988. The talks were rescued in April 1989, when countries finally agreed to a "midterm" package that froze support prices (the first time such an agreement had been possible) and outlined the timetable for the rest of the negotiations. More significantly, it included a political commitment to a progressive reduction in trade-distorting subsidies, to the improvement of import access, and to the curbing of export subsidies.

In the second phase, each (major) participant refined its negotiating points, with the intention of combining it into a document that all parties could focus on. It was at this stage that the final agreement began to take shape. The United States proposed a strategy, in contrast to its 1987 proposal, that would focus on rules to guide both domestic policies and agricultural trade. Nontariff import barriers were to be converted to tariffs. Export subsidies were to be banned. Domestic policies were to be categorized into those that were acceptable (minimally trade-distorting) and those that were objectionable and therefore had to be reduced. The Cairns Group broadly supported this approach. The European Union, however, argued against the rules on individual policy instruments. Though the European Union reluctantly agreed to a form of tariffication, it strongly resisted export subsidy controls. In place of the "rules" approach, the European Union argued for an across-the-board cut in support levels by means of an instrument similar to that proposed by the United States in 1987.

The first document that attempted to pull these ideas together was prepared in June 1990 by the chairman of the Negotiating Group on Agriculture, Aart de Zeeuw. This paper was a substantial and comprehensive draft agreement, but it still did not command full support as "a basis for negotiations." The European Union felt that it followed too closely the US/Cairns Group line and rejected it. Despite further attempts to reach

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consensus in December 1990, the "final" negotiations of the Uruguay Round (including all sectors under consideration) in Brussels in collapsed, largely as a result of the impasse on agriculture. There was no agreement on the structure of an agricultural package until February 1991, after the European Union had proposed substantial modifications to its internal agricultural policy so that it could live with the changes implied by a GATT agreement. In this third and final phase of the negotiations, the details of such an agreement were incorporated into the "Draft Final Act" of December 1991, usually called the Dunkel Draft because Director General of the GATT Arthur Dunkel submitted it. The Dunkel Draft kept the tripartite structure of "market access," "export competition," and "domestic support" and introduced a timetable for liberalization of support and protection. The Dunkel Draft was not, however, immediately acceptable to the European Union, which still considered it too restrictive on the CAP.

The package of reforms for the CAP proposed by Agriculture Commissioner Ray MacSharry, which called for a significant cut in cereal prices and the introduction of compensation payments, finally offered the way to an agreement in Geneva. The European Commission saw that this reform package would allow them to react to the intensifying pressure to accept the Dunkel Draft as a basis for negotiations while modernizing the CAP and checking the upward drift of budget cost. In particular, the lower cereal prices would allow the European Union to agree to subsidy limits so long as the compensation payments were excluded. Technical discussions started up again in Geneva, and the EU Council of (Agricultural) Ministers passed the MacSharry reforms in June 1992. Tense negotiations followed, culminating in the November 1992 Blair House Accord between the United States and the European Union. This deal finally allowed the European Union to accept the disciplines on export subsidies, though the cutback was less than what the Dunkel Draft proposed. The accord also gave assurance that the MacSharry compensations, along with the US deficiency payments, were protected from challenge in the "blue box" and would not have to be cut back.[6] In addition, it weakened the discipline of the Aggregate Measure of Support (AMS) constraint by aggregating over all commodities and introduced a "peace clause" that sheltered the fundamentals of the CAP from further challenge if the policy did not deviate too much from the present situation. A compromise settling the long-running oilseed subsidies conflict was rolled into the package and agreed on, though the accord itself had to be refined by last-minute negotiations (known as Blair House II) in December 1993. The Uruguay Round came to a close, and the URAA went into effect in 1995.

6. The term "blue box" was introduced as a convenient label for those payments that were tied to acreage control but not fully eligible for the "green box" of minimally trade distorting subsidies.

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The Uruguay Round Agreement on Agriculture

The agreement established a set of completely new and more operational rules for agriculture. In particular, it legally bound tariff rates for agricultural goods and imposed constraints on the most trade-distorting agricultural policies used throughout the world. In the past, governments had considerable scope to design and pursue their agricultural policies as they saw fit for domestic interests and to treat agriculture as a special case under trade rules. The GATT did not effectively constrain most government agricultural policies that affected trade. The Uruguay Round imposed binding international commitments that cover nearly all import and export border measures and also apply to domestic support—to the extent that this support has a noticeable effect on international trade. It is hard to overestimate the significance of this fundamental change in the scope of the trade rules. An important sector in world trade, which previously had escaped most GATT disciplines, was now effectively brought under control. However, the level of protection was not significantly reduced by the agreement.

The Final Act, the text of an Agreement Establishing the World Trade Organization, and various Ministerial Decisions and Declarations embody the eventual outcome of the Uruguay Round. The WTO agreement has a number of annexes, which contain the new rules for international trade. The URAA, along with the Agreement on Trade in Goods,[7] is spelled out in the first of these annexes

The three major areas on which negotiations focused—market access, export competition, and domestic support—provide a convenient framework for understanding the URAA. In each of these areas, two approaches were applied: the definition of new rules and the reduction in levels of support and protection. The reduction schedules contain the specific "concessions" on market access and commitments on export and domestic subsidies. Each substantive area also includes a set of safeguards, guarantees, and accommodations that were necessary to reach agreement. In addition, a Peace Clause was negotiated to gave countries certain assurances against challenges under GATT rules. Under the principle of "Special and Differential Treatment," the provisions of the agreement apply less stringently to developing countries. A separate agreement on Sanitary and Phytosanitary Standards (the SPS Agreement) was concluded, which will be discussed after the URAA.

7. The important details covering implementation of the URAA are contained in the commitments entered into by each country in the schedules that form part of the overall agreement. The discussion of the implementation of the agreement by individual countries is deferred to a later section (section 11, 39).

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Market Access

Perhaps the most far-reaching element of the URAA is a change in the rules regarding market access. With a few temporary derogations, participating countries have agreed to convert all existing nontariff barriers (along with unbound tariffs) into bound duties and refrain from introducing new nontariff measures (Article 4). The new bound tariffs and those tariffs already bound have to be reduced by 36 percent over the six-year implementation period (1995 to 2000), on a simple (unweighted) average basis, with a minimum rate of reduction of 15 percent for each tariff line.[8] The agreement to convert all nontariff import barriers to bound tariffs takes agricultural trade a big step toward the treatment of manufactures within the GATT. Tariffication, as this process is known, has a number of desirable features:

- It improves transparency of trade measures for traders and the domestic interests influenced by tariffs.
- It removes many "gray area" techniques employed by countries to control imports, such as variable levies, which had effectively escaped GATT disciplines.
- It makes it easier to negotiate subsequent reductions in tariffs.
- It improves the distribution among countries of the burden of adjustment to world market shocks.
- It increases the influence of market signals in shaping production and consumption decisions.
- The indirect control of the level of export subsidies is implied by the absence of nontariff barriers to prevent reimportation.

However, the tariff levels chosen in the schedules were high, as mentioned above, both relative to manufactured trade and in relation to the level needed to reproduce previous market conditions (i.e., the tariff equivalent). Nonetheless, tariffication could change the nature of world trade in agricultural goods, leading to more liberal, more predictable, and more stable world markets.[9]

To secure minimum trade gains when tariffs were bound at prohibitively high levels, and to counter the ability of state trading import agencies to restrict trade, in cases of tariffication the agreement provided for

8. These percentages and provisions regarding the establishment of base-period tariff equivalents and initial tariffs are not contained in the text of the agreement but in a paper (known as the modalities paper) that was on the table during negotiations. The legally binding commitments for each country are in its schedule.

9. For a discussion of the merits of tariffication, see IATRC (1989).

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"minimum access opportunities." Imports had to be granted a share of the domestic market rising from 3 percent to 5 percent of consumption (see modalities, paragraph 5 and Annex 3) to apply in cases where nontariff barriers had been tariffied. Thus, a quantity-oriented element was added to the provisions regarding market access.

The introduction of Tariff Rate Quotas (TRQs) was devised to provide for this minimum access. Moreover, where exporters enjoyed preferential market access in the past, as through bilaterals, their access opportunities remained protected under a "current access" provision (modalities, paragraph 6 and Annex 3) implemented through TRQs. However, imports of these minimum access quantities were not guaranteed, but to ensure an incentive to fill these quotas, "low or minimal duties" were to be charged. However, market access conditions were not completely and unconditionally improved through tariffication. Because of domestic difficulties in Japan and South Korea with the prospect of opening up their rice markets, a special treatment clause was included in the agreement (Annex 5). The clause, which was tailored to the two cases concerned, allowed Japan and South Korea a several-year delay of tariffication. Moreover, special safeguards for imports of products subject to tariffication were included for all importers, in the event of import surges and low world prices (Article 5). If imports of products that have been tariffied exceed a certain percentage of the preceding three-year average, called the "trigger level," additional duties (of up to a third of the level of normal applicable duty) can be imposed.[10] Alternatively, the importer can apply additional duties, on the basis of a schedule relating such duties to the difference between the import price and a trigger price, when import prices for these products drop below this trigger price.

Export Competition

One of the main issues under discussion in the negotiation was the ability of countries to define and control export subsidies in agriculture. The agreement attempts for the first time to ban new export subsidies. Existing subsidies are, however, allowed to continue subject to agreed on reductions. The schedules establish the level of such subsidies deemed to exist in the base period. These base levels replace the "equitable shares" defined under GATT Article 15:3 and the Subsidies Code (though few would argue that these existing market shares are indeed equitable). By entering base levels of subsidized exports and outlays on export subsidies

10. The trigger level is set at 105 percent of base period imports for products where imports make up more than 30 percent of the domestic market; at 110 percent of base imports where they make up between 10 and 30 percent of consumption; and at 125 percent where imports account for less than 10 percent of domestic sales. The trigger level is adjusted by the change in domestic consumption between the two most recent years, but it cannot drop below 105 percent of the preceding three-year average.

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into their schedules, members have agreed that the figures contained in the schedules are an adequate representation of their export subsidization in the past. More important, based on these past levels of export subsidization, countries have accepted legally binding commitments regarding maximum export subsidization in the future (Article 3). Hence, there is no longer any doubt as to what (maximum) level of export subsidies a country can grant in agricultural trade.

The agreement lists the export subsidies that fall under schedule commitments (Article 9). Moreover, it includes provisions that guard against circumvention of commitments, including rules on food aid (Article 10). The burden of proof for not subsidizing exports is on the exporting country (Article 10:3). In addition, export subsidies cannot be extended to commodities not subsidized in the base period (Article 3:3 and modalities, paragraph 12).[11]

Under the agreement, countries accepted commitments leading to a reduction in expenditure on export subsidies of 36 percent and a reduction in the quantity of subsidized exports by 21 percent during the six-year implementation period (modalities, paragraph 11). To provide some flexibility, countries can shift their export subsidy commitments between individual years of the implementation period, though only within narrowly defined limits. However, the commitments did not include export credit schemes, and countries have not yet been able to agree on their limitation. Moreover, certain privately financed export aids appear to have escaped the net of the export subsidy definition.

Domestic Support

Another innovative feature of the agreement is the set of rules and commitments it establishes for domestic support policies, though in practice the short-term influence of this innovation is likely to be modest. Given the link between domestic agricultural policies and international trade, it is significant that GATT commitments now impose quantitative constraints on certain types of domestic support.

The nature of the constraint on domestic support warrants some explanation. The variable constrained under the domestic support commitments is not just expenditure on domestic subsidies but the level of total support (including market price support through administered prices) provided by other policies covered under the agreement. This support includes the value of administered market price maintenance, measured against the fixed external reference prices of the base period. This, together with the expenditure on domestic programs deemed to be trade-distorting, makes up the AMS. The AMS is then aggregated over both pol-

11. Paragraph 12 of the modalities paper also provides for the possibility of negotiating commitments regarding exports to individual or regional markets.

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icy instruments and commodities to be matched against the agreed level. The agreement specifies the method of calculation of the AMS (Annex 3), requires countries to enter their base period (1986–88) AMS in their schedules and sets a 20 percent rate of reduction in total over the six-year implementation period. The result is an annual AMS commitment specified in the schedules.

However, rather than binding all policies, measures with no, or at most minimal, trade distortion effects or effects on production have been exempted from reduction commitments under the AMS approach, and these measures are therefore not included in the AMS calculation. A "green box" is defined both by general criteria and in terms of a list of eligible policies that include advisory services, domestic food aid, decoupled income support, income insurance and safety-net programs, set-aside payments (if land is retired for a minimum of three years), regional and environmental aids, and those policies that encourage early retirement (Annex 2). In addition to the green box policies, a *de minimus* provision exempts support below 5 percent of the value of production of any given commodity (Article 6:4). GATT challenges can not be made to green-box policies (see the discussion of the Peace Clause, below). Policies that are not accepted as "green" are called "amber" policies and automatically become subject to reduction commitments as a part of the AMS.

As a result of the Blair House Accord between the United States and the European Union another exemption was agreed upon. Neither the US deficiency payments (as authorized under the 1990 Farm Bill) nor the new compensation payments under the reformed European Union's CAP need to be included in the AMS calculation. In this way, both the United States and the European Union escape the reduction commitment on major aspects of their domestic policy. The wording chosen for this exclusion (called the "blue box") exempts "direct payments under production-limiting programs" provided that they are made on the basis of fixed area and yield (number of head for livestock) or on a maximum of 85 percent of base level of production (Article 6:5).

The Peace Clause

As an incentive for countries to accept the new disciplines and commitments on domestic support and export subsidies, it was agreed that policies that conform to the new rules are sheltered from international challenge under the GATT. The Due Restraint provisions (Article 13), known as the Peace Clause and valid during the implementation period, state that green box policies (in accordance with Annex 2 of the agreement) are nonactionable for purposes of countervailing duties and other GATT challenges. Domestic support that conforms with commitments, including blue box payments under production-limiting programs (i.e., US deficiency payments and EU compensation payments), is subject to counter-

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vailing duties only if it can be shown to have caused injury. It is exempt from other GATT challenges as long as support does not exceed the level operative in 1992. Finally, export subsidies within the constraints of the agreement are exempt from most GATT challenges and subject to countervailing duties only if they cause injury.[12]

The Uruguay Round could substantially improve trade relations in agriculture by improving bilateral relations between countries, notably the United States and the European Union. Agricultural trade conflicts will not disappear overnight, but they will take place within a clearer framework of rules and obligations. This clarification could change national policy behavior by constraining agricultural policies within effective GATT rules, and countries would face greater risks when administering policies that offer excessive protection to agriculture. National policies will run up against these constraints and adapt more quickly.

An important factor determining the effectiveness of the agreement is that it not only establishes general rules to be observed in agricultural trade but also requires that all participating countries undertake specific commitments, which are expressed in their schedules. The real power of the agreement lies in the binding nature of these country-specific commitments, because they relieve the process of implementing the agreement from the need to find appropriate interpretations of general rules for each country's policies. Indeed, all waivers and special exemptions for agriculture in the trade rules are to be removed. New types of commitments have been made in the GATT, in agriculture or in other sectors. Whereas GATT schedules in the past contained only tariff bindings, their agricultural components now also contain bindings regarding export subsidies and total support. This legal innovation is an important aspect of the agricultural negotiations, made necessary by the complexity of dealing with domestic farm policies at the international level.

The Sanitary and Phytosanitary Agreement

Participants concluded an Agreement on Sanitary and Phytosanitary Standards (the SPS Agreement) in addition to the provisions on domestic and trade policies.[13] The goal was to improve the operation of Article XX of the GATT by making it easier to distinguish between disguised protection and genuine health and safety issues. The right of countries to set

12. The injury provision existed in the GATT rules on countervailing duties and is not a new feature of the Uruguay Round. The other GATT challenges include "nullification and impairment" of a country's GATT obligations and "serious prejudice" to another country's interests, usually in third markets.

13. Sanitary and phytosanitary measures relate to animal and plant health regulations as they relate to trade.

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their own safety and health standards is reaffirmed, but with the proviso that such standards be based on "sound scientific evidence" and that international standards be used when possible.

Although the SPS Agreement is separate from the URAA, it has close substantive links with it. In particular, commitments to reduce economic barriers to trade may intensify the use of technical standards to protect domestic farmers. The SPS Agreement guards against such inappropriate use of sanitary and phytosanitary standards, while also dealing with "technical" issues relating to standards that can be better agreed on at the international level. In particular, the SPS Agreement made progress in ensuring that these standards achieve their objectives in the protection of human, animal, and plant life and health, while not causing economic waste by unduly restricting international trade. The SPS Agreement could prove as important for these issues as the URAA will be in the realm of economic measures. The SPS Agreement is the fourth pillar of the Uruguay Round achievements in the area of agriculture, complementing the new rules and commitments in market access, export competition, and domestic support.

The SPS Agreement differs in many regards from the URAA. In particular, the SPS Agreement does not regulate any specific policies. Hence, the agreement does not commit any country to adjust its policies. Instead, it establishes general guidelines for government behavior in the areas concerned. Some of these guidelines are open to interpretation, and the WTO dispute settlement process is beginning to adjudicate between alternative interpretations of the SPS Agreement.

Implementation will rely heavily on the principles of harmonization and equivalence laid down in the SPS Agreement. Where harmonization is achieved—that is, where national sanitary and phytosanitary standards are based on the standards agreed on in the relevant international institutions—such standards are presumed to be consistent with the SPS Agreement and disputes should not arise. However, harmonization at the international level may not always be appropriate, as technical conditions may differ. The SPS Agreement therefore allows the option of equivalence, whereby the importing country accepts that the sanitary and phytosanitary standards in the exporting country can achieve an appropriate level of protection, even though they differ from the measures used in the importing country. In the long run, widespread application of the equivalence principle may result in harmonization as trading partners learn more about each other's measures and find out which measures are most appropriate in certain situations.

If a country chooses not to rely on harmonization or equivalence but rather insists on its domestic standards, it must comply with several requirements. For example, it must not discriminate among exporting countries that have identical or similar conditions of production, and it must not apply its standards as a disguised restriction on international

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trade. These requirements fundamentally existed under GATT Article XX, but the SPS Agreement is somewhat more demanding. However, the SPS Agreement requires that the measures concerned are consistent with scientific evidence and that they are based on an appropriate risk assessment. These additional requirements are completely new, and governments must develop procedures for fulfilling them.

The criterion of scientific justification for a particular measure is a general rule that is likely to be crucial to the implementation of the SPS Agreement. It is not without ambiguity, however. Scientists sometimes disagree on the implications of particular practices (e.g., can a hormone fed to an animal affect the health of those that consume the animal?). Countries can disagree on how much risk the consumer should be protected from. The SPS Agreement allows countries to define their own level of acceptable risk, so long as it is internally consistent. However, there will still be scope for interpretation in each case. Therefore, much will depend on how quickly, vigorously, and effectively disputes arising from different interpretations of the SPS Agreement are settled.[14] Although the new SPS Agreement is a significant advance in rule making, its effectiveness in curbing trade disputes arising from health and safety standards is not certain. Many environmental and consumer groups fear that standards will be lowered in the name of freer trade. The significance of these trade rules should soon be apparent. The first test has come with the WTO panel report that ruled against the European Union's ban on hormone-treated beef. The European Union must decide how to modify its practices to be consistent with WTO rules. There are many other important issues that threaten to test these new SPS procedures, such as inconsistent regulations on the use of bovine somatotropin (BST) in dairy production, different approaches to food irradiation, and disparate requirements for food labeling. In addition, the question of GMOs poses a particularly emotionally charged challenge to the system.

The Implementation of the Agreement

It is one thing to negotiate a complex set of rules for the agricultural sector. It is quite another to see them in operation. The credibility of the world trading system would be compromised if countries chose to interpret the URAA as they wished or decided to ignore it if it were politically unpopular at home. So far, most countries seem to have implemented the URAA with reasonable diligence as they assimilate its provisions into legislation and practice. Some countries have even devised new policy

14. A new WTO Committee on Sanitary and Phytosanitary Measures was established under the SPS Agreement to help clarify some of these issues.

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instruments to take advantage of ambiguous wording in the agreement. Canada has defined an export category of milk that can be sold at a lower price than domestic milk. As the producer usually gets a "pooled" price over both uses, this could be seen as avoiding the export subsidy regulations. The European Union reconstitutes cheese from butter and milk powder to avoid the constraints on export subsidies on dairy products. Some of the side deals, such as the "maximum levy-paid import price" for cereals in the European Union that was agreed to at Blair House, have proved difficult to interpret and have led to conflicts. Hungary has claimed that there were computational errors in its schedules on export subsidies, and it has renegotiated an increase in the allowable subsidies with the major exporters in the transition period. Countries have gone their own way in allocating TRQs, and this has led to considerable debate about making the process more uniform.[15] But too much should not be made of these exceptions. Overall, the main thrusts of the URAA—the move to tariffs as the only import barrier, the binding of existing export subsidies, and the categorization of domestic support measures—have proceeded smoothly. Proposed revisions to the agreement, discussed below, are more in the nature of completing and tidying up rather than correcting significant mistakes. A look at how some of the major regions have implemented the agreement indicates substantial compliance.

Implementation in North America

The United States has implemented the provisions of the URAA with relatively little change in domestic policies. In this regard, the US experience differs from that of the European Union, Canada, Japan, and many importing countries, where impacts are more immediate.[16] Indeed, to secure US domestic support for the round, it was useful that the United States gained access to other markets for agricultural products while not relinquishing policymaking to international negotiations. Nevertheless, the agreement does have some impact on future policy developments and has already encouraged changes that have been implemented for largely domestic reasons. And these domestic policy changes may increase the significance of international trade negotiations on domestic policy.

Market access provisions in the Uruguay Round did not dramatically open up the US market for agricultural goods. For many products, trade barriers were low before the round, while for the few sensitive items such as dairy products and sugar, liberalization was modest. Tariffication took

15. For a critical look at the allocation of TRQs and other aspects of the implementation, see Ingco and Hathaway (1996).

16. More detail of the implementation of the agreement in the United States is given in the chapter by Sumner in IATRC (1997).

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Table 6 US implementation of market access provisions, FY 1995 (thousands of tons)

	TRQ	In-quota imports
Beef	676.60	462.10
Cream (thousands of liters)	5,921.30	4,362.50
Evaporated and condensed milk	3.65	1.31
NFDM	2.06	1.94
DWM	0.96	0.73
Dried cream	0.10	0.00
Dried whey	0.23	0.22
Butter	4.58	4.04
Butter oil	4.00	3.62
Dairy mixtures	2.35	1.24
Blue cheese	2.66	2.47
Cheddar cheese	7.38	7.08
American cheese	3.46	3.25
Edam, Gouda	6.15	5.39
Italian type	13.08	11.09
Swiss/Emmental	33.33	28.46
Other NSPF	45.46	42.54
Low-fat cheese	5.47	4.08
Peanut butter and paste	19.15	18.25
Chocolate crumb	17.61	4.54
Low-fat chocolate crumb	2.12	0.00
Ice cream (thousands of liters)	3,760.60	37.60
Infant formula	0.10	0.01
Animal feed containing milk	7.40	1.30
Raw cane sugar	1,117.20	2,015.80
Other sugars	22.00	20.50
Mixes and dough	5.40	3.90
Mixed condiments	0.70	0.30
Short staple cotton	8.50	0.20
	765.40[a]	40.40[a]
Rough staple cotton	0.90	0.00
Long staple cotton	5.20	0.00
Long staple cotton	25.50	0.00
Cotton waste	1,835.40	0.00
Cotton processed	1.00	0.80

a. Additional global quota.

Source: US notification to WTO (11 March 1997).

place in several sectors, notably in beef, where voluntary export restraints (to avoid the imposition of quantitative restrictions) had been used to bolster the domestic market over parts of the cattle cycle, and in dairy, where nontariff import barriers had been widely used to control milk-product markets. In these cases, TRQs were established to maintain access (beef) and provide for minimum access (dairy) along the lines of the agreement. The TRQs for beef and dairy appear not to have been filled in the first year of operation, 1995, as shown by the gap between the quota and the recorded level of imports in table 6, though sugar imports have exceeded the quotas. Although tariff levels for all agricultural goods were cut on

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Table 7 US export subsidy commitments and actual outcomes, FY 1995

	Outlays (millions of dollars)		Quantity (thousands of tons)	
	WTO limit	FY 1995	WTO limit	FY 1995
Wheat	765.5	0	20,238.3	559.8
Coarse grains	67.7	0	1,906.3	0.3
Rice	15.7	0	271.7	9.9
Vegetable oils	53.0	0	587.5	0
Butter and butter oil	44.8	0	43.0	0
Skim milk powder	121.1	16.8	108.2	63.7
Cheese	5.3	2.1	3.8	3.3
Other milk products	14.4	1.6	12.5	4.5
Beef	33.5	0	21.5	0
Pigmeat	0.7	0	0.5	0
Poultry	21.4	5.2	34.2	22.3
Live cattle	17.5	0	13.5	0
Eggs (dozen)	7,587.9	0	30,261.8	7,565.5

Source: US notification to WTO (11 March 1997).

average by 36 percent over the period up to 2000, the United States took advantage of the minimum allowable cut of 15 percent for dairy and sugar products. Thus, action on these commodities is a natural focus for the next round of negotiations. Implementation of the agreement had one significant impact in terms of import access to the United States. The notorious Section 22 of the Agricultural Adjustment Act, which gave the president the mandate to use quantitative controls whenever imports threatened domestic support programs, was removed. This in turn removed the need for the waiver from GATT rules, which had been in effect since 1956. The removal had symbolic importance: it indicated that even the United States will allow agreed on international trade rules to impinge upon domestic programs.

Export subsidy programs in the United States were subject to cuts agreed on in the round. However, the rise in world prices since the base period of the agreement, and more particularly the high prices in 1995 and 1996, meant that export subsidies for cereals naturally declined. In fact, the congressional appropriation for subsidies has actually decreased substantially in recent years, and there is evidence that the Export Enhancement Program (EEP) is unlikely to be used to its fully authorized level in the near future. This is despite the rhetoric, which regards export subsidies as necessary aspects of commercial policy that maintain market shares and prevent the European Union and other exporters from undercutting US sales abroad. The combination of high prices and buoyant export markets has reduced the need for such subsidies (see table 7).

As expected, the URAA has had little impact on US domestic support programs such as the deficiency payments scheme for cereals. The Blair House deal ensured that result by allowing both the United States and the

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European Union to shelter their direct payments in the blue box reserved for payments linked to supply control programs. Even without this, it is unlikely that the payments would have violated the AMS limits, which were based on a period of higher subsidies.

However, even the indirect restraints of the blue box are likely to have been made redundant for the United States by the substantial changes in domestic policy embodied in the Farm Bill of 1996. This bill, the FAIR Act, removed the acreage-set-aside conditions for receiving direct payments for cereals. Though there is still some incentive to remain in agriculture, this change essentially decouples payments from output levels. Therefore, it can be assumed a priori to be a green box policy, leaving the European Union alone in sheltering its direct payments from challenge under the GATT by means of the blue box.

The rest of the world does not see US agricultural trade policy as the model free trade regime expounded by US politicians and negotiators. Significant tariff and other restrictions on imports of sugar, peanuts, and dairy products tend to exclude even efficient foreign suppliers from these markets. The big question is, will the United States be willing to back up its leadership in pushing for free trade in areas such as cereals and oilseeds by offering significant concessions on sensitive products? Dairy products and sugar are likely to be at the heart of the next round. Though some progress was made in the FAIR Act toward further reducing price supports for dairy products, and the sugar program just survived a congressional attempt at radical surgery, the willingness of the United States to put these sectors on the international bargaining table has yet to be tested.[17] Canada has had a somewhat different experience in implementing the results of the Uruguay Round.[18] Two changes in domestic policy in particular were made in direct response to the round. First, the long-running transportation subsidies, which gave Canadian grain an advantage on world markets, was finally terminated. This change has long been debated domestically, but pressure from the Uruguay Round limits on export subsidies was effective in finally forcing the issue. Second, the nontariff import barriers that have bolstered the domestic market in the supply-managed commodities (poultry, eggs, and milk) were converted into bound tariffs as a direct result of the URAA. This would probably not have been possible for years without the pressure from the round. The new tariffs are, however, very high (in some cases over 300 percent), and access depends on the TRQs, which carry a much lower rate of duty. Thus, the extent to which the TRQs will be expanded in further negotiations is one key issue for

17. The sugar program may disappear for purely internal reasons. Another bill introduced recently in Congress aims to abolish the system of quotas and support prices in favor of direct payments, as a way of reducing consumer costs.

18. For a more complete discussion of the implementation in Canada, see the chapter by Miner and McClatchy in IATRC (1997).

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Canada. There will likely be strong resistance from the provincial marketing boards, which run the supply management programs.

Mexico demonstrated a remarkable capacity to change domestic agricultural policies as it reduced protection and reformed its economy. Not much of this change was due to the Uruguay Round. The conversion of nontariff barriers to tariffs had taken place as a part of domestic economic reform. Export subsidies were already minimal, and domestic support was cut drastically from the base period as a result of domestic policy changes. The main impact of the WTO on Mexican agricultural policy is through the TRQs, though NAFTA's schedule of tariff reductions for Mexico is a stronger force for opening up the Mexican market.[19] In addition, the policy reforms are to a large extent locked in by the schedules and bindings, and a future Mexican administration would have difficulty returning to the costly and distorted programs of the past. In this respect, Mexico is typical of several countries in Latin America that underwent structural reforms in the last decade.

Implementation in South America

Without exception, the South American countries had embarked on drastic reform of agricultural trade policies in advance of the outcome of the Uruguay Round. This made implementation of the URAA relatively easy for these countries. Quantitative restrictions to trade had been removed in almost all countries in the region as part of economic reforms. Price support policies had been abandoned in many countries and reduced in others. Export subsidies were rare in the region. This relatively liberal stance enabled these countries to take an active role in the talks. Five of the countries had participated in the Cairns Group of agricultural exporters, which was instrumental in ensuring that the issues of agriculture were not once again swept under the rug in the Uruguay Round.[20]

The tariff schedules submitted to the WTO by the South American countries for agricultural products reflect this open position. Virtually all tariffs are now bound, and the bound rates are often less than in other regions. Argentina, Brazil, Bolivia, Chile, Peru, and Venezuela have declared agricultural tariffs ranging from 25 to 68 percent, and Colombia proposed a tariff schedule for agriculture starting at 100 percent and declining to 70 percent (90 percent for a few commodities) over the 10-year period (see table 8). Because the "ceiling binding" option was widely

19. Above-quota tariff bindings for Mexico are still substantial in sensitive commodities such as corn, poultry, and dried milk. Actual tariffs are somewhat lower than these bindings.

20. The Cairns Group members from the region include Argentina, Brazil, Chile, Colombia, and Uruguay. Both at the Montreal midterm review meeting and again at the Brussels meeting in 1990 that was meant to end the Round, the Cairns Group had been the one to prevent any agreement that did not include agriculture.

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Table 8 Tariff bindings for selected Latin American countries

Country	Tariff binding (percentages)	Number of product groups excepted	Range of tariffs for excepted products
Argentina	35	2	3.8
Brazil	35	9	18–55
Chile	25	4	31.5
Colombia	90	14	70–194
Dominican Republic	40	—	—
Paraguay	35	—	—
Peru	30	6	68
Uruguay	35	4	20–55
Venezuela	40	—	—

Source: IATRC (1994; 1997).

used, only a small number of countries and commodities underwent tariffication. Thus, there are few TRQs and the possibility of use of the special safeguard is small. Similarly, not many countries declared that they had export subsidy programs. Therefore, they are highly restricted in what they can do in this area in the future. The same restraint applies in principle to transfers that are made through instruments in the green box. By failing to declare such transfers, countries will find it more difficult to implement such policies in the future.

Implementation in New Zealand and Australia

Exporters of temperate zone commodities that felt negatively impacted by the subsidies of the European Union and the United States also had an interest in the outcome of the round. During the negotiations, these countries, as the Cairns Group, played a major role in keeping the issue of agriculture to the fore. Leadership of this group, which included a number of developing countries, rested with New Zealand and Australia.[21]

Implementation of the URAA posed few difficulties for New Zealand. The domestic policy reforms of the mid-1980s had removed many trade-distorting domestic subsidies, in particular for the livestock sector. Import restrictions had been largely converted to tariffs, and the rates tended to be below those required by the agreement. Export subsidies were rarely used, and import controls for sanitary and phytosanitary purposes seemed to be noncontroversial.

Australia has had to make a few more changes to implement the agreement. Nontariff barriers on sugar imports were converted to tariffs, as were those for some dairy products. Cheese was assigned a TRQ to ensure minimum access. The export subsidy on dairy products was modified to be more consistent with WTO rules, though the new export rebate scheme

21. For more discussion of the implementation in Australia and New Zealand, see the chapter by MacLaren in IATRC (1997).

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may come under scrutiny at some stage. The operation of the Australian Wheat Board has also been modified to give private traders more scope in the internal market, though Australian grain exports are still handled through the board.

New Zealand and Australia undoubtedly will try to keep the issue of further trade liberalization in agricultural goods high on the agenda of future multilateral trade talks. Their targets are likely to be export subsidies and the high levels of import protection. They will, however, be under pressure to further modify their export marketing boards so that other exporters can be assured that they are not exploiting a loophole in the restraint of export subsidies.

Implementation in the European Union

The European Union reformed the CAP in 1992 to be able to agree to the Uruguay Round outcome. Unlike in the United States, where the Uruguay Round had relatively little impact on domestic policy, the European Union has made still more changes since 1992 to implement the agreement. Nevertheless, the policy changes were minimized by various devices, which have preserved many of the policy instruments of the CAP. The cereals market, for example, is still protected by a variant of the variable levy, because of the deal made at Blair House that the duty-paid price of imports should not exceed 155 percent of the intervention price (the prevailing threshold price). The maximum duty-paid price is not exactly the same as the threshold price: if world prices drop, the duty-paid price could be below the former threshold level. But when prices are firm the effect on the market is similar. The duty actually paid is the difference between the world price and the agreed-on maximum duty-paid price, just as it would have been under the former variable levy system.[22] Similarly, with the import duties for fruits and vegetables, the use of tariffs conditional upon the relationship of import prices to predetermined entry prices acts much as the previous policy of supplementary duties triggered by reference prices.[23]

Not only have the mechanisms determining market access changed little, but the ease of access has improved only marginally. There are TRQs for many products, as shown in table 9, but for the most part these reflect current access (i.e., the bilateral agreements that the European Union has

22. There was a long dispute, now settled, between the United States, Canada, and the European Union on whether the maximum duty-paid price should apply to each transaction (as the agreement appeared to say) or to all transactions at a particular time. Clearly, this dispute had major implications for the incentive to ship different qualities of grain.

23. If the import price is less than 92 percent of the entry price, then a high (often prohibitive) tariff applies (see the chapter by Tangermann in IATRC 1997).

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Table 9 Implementation of the market access provisions in the European Union, 1995–96 (thousands of tons)

Commodity	TRQ 1995	In-quota imports 1995–96
Beef, cuts	50.000	33.000
Pork, cuts	7.000	2.620
Pork, loins, and hams	5.670	2.340
Sheep meat	298.740	255.450
Cheese for processing	3.500	3.110
Manioc	6,852.590	3,280.800
Sweet potatoes	605.000	35.550
Citrus	35.000	21.120
Maize	2,000.000	1,551.820
Sorghum	300.000	214.300
Cereal residues	475.000	83.690
Orange juice	1.500	0.520
Eggs (in shell)	82.650	.008

Source: Tangermann in IATRC (1997).

had with other countries). When new "minimum access" quotas have been opened up, they have not always been filled. The above-quota tariffs are often prohibitive, as were the threshold prices that they replaced, and true market access awaits the next round of trade negotiations. In some cases, market access actually declined as a result of tariffication, as it did for pig meat and other products that had levies previously tied to domestic cereal prices. CAP reform had already reduced import levies on pig meat, but they increased again when based on the tariff equivalent in the WTO base period.

The export side is more encouraging. The constraints on export subsidies negotiated in the round are the most binding: that is why it was so difficult to achieve agreement on them. For many products—wheat, sugar, beef, and cheese in particular—the export subsidy constraints have already dictated domestic policy decisions. However, in the case of wheat, high world prices rescued the policy from the constraints of the WTO schedule, because the need for export subsidies temporarily waned. And in the case of cheese, the export restriction has been circumvented somewhat by the production of processed cheese in bond using already exported butter and skim milk combined with imported cheese.

The deal secured at Blair House to place the MacSharry compensation payments in a blue box, implying that they do not count toward support that needs to be reduced (and are sheltered from most WTO challenges unless they are increased), ensured that the European Union stayed well within the AMS constraint. The issue for the next round will be whether the European Union can change the way it allocates compensation payments so that it does not need the blue box at all.

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Implementation in East Asia

Japan has implemented its scheduled obligations with precision if not enthusiasm; the improvement in market access has been modest. In part, this reflects the problem of the domestic food processing and distribution system, which is still more tightly controlled than in most other OECD countries. The way that the access agreements have been administered demonstrates this problem. Japan converted some 28 commodities from nontariff protection to tariffs under the URAA, including wheat, barley, milk products, starches, legumes, and pork.[24] But the market access differs between those commodities where the private sector is the importer and TRQs were used and those where state trading is still practiced and the tariffs faced by private traders exist alongside markups for the state enterprise. For these commodities, private imports are an alternative, but the markups for cereals have been set to give the state agency an advantage. The incentive, therefore, remains for the private sector to purchase from the state importer, thus maintaining effective control over the market. For milk products, the private trade is allowed to import under a TRQ for particular purposes (see table 10). Import arrangements for pig meat are complicated by a device designed to reproduce some of the stabilization of the previously used differential tariff, which operated like a variable levy. The duty charged is still a function of the world price, and there is no minimum access through a TRQ.

The rice that Japan is obliged to import is purchased by the Food Agency, which adds a fixed markup to the cost of imports.[25] Little reaches the domestic market, and some finds its way into stockpiles or processing uses. (Stocks were reported to have reached 3 million tons by the end of 1996.) Japan also has a food aid program that might eventually benefit from imports. The increased private involvement in the marketing of domestic rice under a 1995 law (designated corporations can now distribute some part of the ordinary rice, and anyone can sell rice outside ordinary marketing) has not yet spread to the sale of imported rice. That change will come when tariffication is fully implemented and the permissible role of state trading entities is clarified.

South Korea has also made efforts to apply the URAA scrupulously. Access has improved for certain products, in line with a gradual liberalizing trend over the past few years. In fact, actual import quotas for some commodities have exceeded the required levels. However, rice has been spared tariffication for a period of 10 years; instead, South Korea has

24. For information on the details of implementation, see the chapter by Honma in IATRC (1997).

25. Small quantities of rice can be imported by the private trade under a scheme known as "simultaneous buy and sell," a method for price discovery in a market that is not accustomed to absorbing foreign rice (Honma in IATRC 1997).

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Table 10 Japanese imports of goods subject to tariff rate quotas (thousands of tons)

Commodity	TRQ 1995	Actual imports 1995	Actual imports 1996
Skim milk (school lunch)	7.3	4.8	4.5
Skim milk (animal feed)	85.9	42.5	35.5
Unsweetened condensed milk	1.6	1.1	0.7
Whey (animal feed)	45.0	22.5	22.4
Whey (for milk powder)	25.0	6.6	5.0
Butter and butter oil	0.6	0.5	0.3
Dried legumes	120.0	110.9	110.1
Groundnuts	75.0	42.1	43.2
Starches	157.0	107.6	120.6

Source: Honma in IATRC (1997).

agreed to import a minimum quantity, which rises to 4 percent of consumption by 2004 (Lee in IATRC 1997). State trading agencies still dominate the import of agricultural products in South Korea, and the TRQs that were agreed on along with tariffication are essentially administered by these agencies. In fact, the agencies benefit financially from the profits (quota rents) from importing and use those funds to finance other rural projects. In other cases, domestic producer associations have been allocated the import TRQs, illustrating again the need to clarify the allocation mechanisms that would be acceptable to all WTO members.

Neither South Korea nor Japan have engaged significantly in export subsidies, and therefore they need not implement new constraints. Both countries have had to comply with AMS constraints on domestic support, through reduced spending on agricultural programs or lower administered prices. For Japan, this has caused no problems, as prices were in any case lower than in the base period. South Korea, however, has found it more difficult to live with the constraint on domestic support. Both countries are reorienting their spending toward productivity enhancements, through land consolidation, market development, and research activities that reduce the need for price support and border protection.

Implementation in South Asia

The implementation of the agreement by the countries of South Asia reflects their tendency to rely on broad developing-country exemptions to avoid forcing domestic policies to adjust to external agreements. As Pursell notes, "Before the [r]ound, India, Pakistan[,] Bangladesh[,] and Sri Lanka had routinely used the balance of payments exemption [from the restriction on quantitative import controls] to justify the general use of import licensing of agricultural products" (Pursell in IATRC 1997). Pakistan, Bangladesh, and Sri Lanka abandoned nearly all import licensing in recent economic reforms, but India kept extensive import restrictions in

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place. Thus, some of the most important import policies in the region, such as India's quantitative restrictions on imports of consumer goods, including foodstuffs, survived the round intact as a balance of payments safeguard measure under Article XVIII:B of the GATT.[26]

The countries of the region chose ceiling bindings rather than tariffication of existing nontariff import barriers. The ceiling bindings chosen were generally high relative to those in Latin America, but not out of line with those chosen by African developing countries. Most bindings in India are set at 100 or 150 percent. In Pakistan the ceiling is 100 percent, and in Bangladesh it is 200 percent. Sri Lanka chose a more modest ceiling of 50 percent. Most of these bindings operate over the entire 10-year implementation period, while one-third of those of India represent the final levels in the year 2004 (Pursell in IATRC 1997).

Imports into the region are unlikely to surge because of the round. Imports and domestic markets are still controlled by state trading enterprises, in particular in India. This implies that improved access may have to wait until the WTO has firmed up the regulation of such institutions. It is also possible that there is little repressed trade in agricultural goods in the region and that an open trade system would have a relatively small effect. But experience from both Europe and Latin America suggests that agricultural trade can blossom if entrepreneurs can take advantage of market opportunities and consumers can choose between different suppliers.

Improvements Needed to the Agreement

The WTO Committee on Agriculture was entrusted with monitoring the URAA. This committee has met several times each year since the agreement went into force, and it made its first report to the Singapore Ministerial in December 1996. The committee's experience forms the backdrop for the consideration of changes in the agreement that, in addition to the items discussed below, might be suggested for the next round of negotiations.[27]

Perhaps the part of the agreement in need of the most urgent revision is the administration of the TRQs, which were intended to open up previously closed markets. The TRQs for agricultural trade are hardly the jewel in the crown of the URAA. Their negotiation created a slew of bilaterals that promise to keep agricultural trade an intergovernmental affair for years to come. Moreover, they have created a new wave of govern-

26. Intensive bilateral discussions have been going on between the United States and India and between the European Union and India on the quantitative restrictions. The dispute may have to be resolved in a WTO panel.

27. The committee has also been involved in the discussion of the agenda for the next round, through a device called "Analysis and Information Exchange." A subgroup of the committee discusses "nonpapers" on particular topics.

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mental interference with agricultural trade through licensing procedures, and they provide a playground for rent-seeking traders who will, in turn, have an incentive to lobby for the continuation of the high above-quota tariffs. The question is, how can the TRQs be prevented from interfering any more than necessary with the competitive development of trade?

The negotiations will probably focus on developing a more uniform system for the administration of the TRQs. One issue is whether to allow them to be auctioned, as has been suggested in some academic circles.[28] This would seem an economically sensible solution to the problem of the capture of rents, and it would counteract the incentives to keep the system in place. But that is also a reason why exporters are likely to resist such a move. If the TRQs were auctioned to the exporter, the impact would be much like a tariff. The exporter would bid up to the height of the tariff concession for the right to sell in the import market. The government rent capture through the auction process in effect turns the TRQ into a quasi-tariff, with the height determined through the auction process. Where the TRQs replace previous access agreements that allocated the quota to the exporter, the auction would reduce the return from selling in this market. Thus, there could be considerable resistance to the auctioning of TRQs. The best solution may in the end be to steadily increase the TRQs, as suggested below, until the issue of how to allocate them is rendered moot.

The Special Safeguard Provisions also need some patching and more uniformity. Though subject to abuse, trade safeguards are generally considered by governments a necessary concomitant to trade liberalization and market access. However, the use of the Special Safeguard Provisions by developed countries to maintain protection against imports is likely to be an issue for the next round of trade negotiations. One way to avoid the misuse of the provisions is to seek agreement on trigger prices. Wherever technically possible, trigger prices should be identical (or equivalent) to the external prices that governments used to calculate initial tariff equivalents in the Uruguay Round. Governments tended to use the lowest feasible external prices for calculating tariff equivalents in their Uruguay Round schedules. Hence, using the same prices as trigger prices for the safeguards would ensure that additional duties are not used too often and not set too high. The Special Safeguard Provisions should be phased out after the second period of transition. This could be done by adjusting the percentages in the quantity and price trigger provisions every year so that the safeguards are less and less likely to cut in.

28. Tangermann (1997) explores the arguments in favor of auctioning the TRQs. The issue of auctioning quotas was addressed some years ago by Bergsten et al. (1987) in the context of US import policy. It is an interesting comment on the lack of economic rationality in trade policy and the attraction of rents to trading interests that such a simple device as auctioning quotas has not so far caught on with politicians and policymakers.

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In addition to the overt export subsidies identified in the Uruguay Round, agricultural exports are often assisted by export credits and credit guarantees. These are clearly forms of export subsidy, given to export firms by governments trying to expand trade. The practice was criticized in the Uruguay Round, and at the round governments agreed to "work towards the development of internationally agreed disciplines." Discussions on the subject of export credits in general have continued in the OECD, and it is possible that agricultural export credits will eventually be brought into conformity with those in other areas of trade.[29] The question of export credits is still thorny for several smaller exporting countries that are not represented in the OECD. It should be possible to take the terms of an OECD pact and incorporate them into the WTO structure.

The Uruguay Round allowed both Japan and South Korea to delay tariffication for an initial period, though they had to give access for somewhat more imports than they would have done under tariffication. Though this political deal was necessary in order to get an agreement, the pressure will be on these countries to step into line and remove the anomaly. Japan is preparing for eventual liberalization of rice imports. The Food Control Law, which since 1942 has mandated state purchase and sale of rice, has recently been changed, and the amount of rice privately traded is increasing. Imported rice is finding its way into the Japanese food system despite predictions that consumers would reject it.[30] South Korea, partly because it joined the OECD, has been more willing to modify its domestic practices in light of outside pressure.

But the question is, when will the major policy decision to adopt tariffication be taken?[31] Japan must decide by the end of 1999 whether to seek an extension of the delay. The specially negotiated additional access (4 percent rising to 8 percent, as opposed to 3 percent rising to 5 percent for goods newly tariffied) is seen in Japan to have increased domestic pressures more than tariffication would have. This is true in particular if the initial tariff had been set at a high level by the use of a low world price. For Japan, to get an additional extension would require not only negotiating capital but also a more generous access agreement that would cause even more price competition on the domestic market. In all likelihood, the Japanese government will agree to tariffication rather than seek a further temporary derogation. South Korea will probably make a similar decision but has a little more time to consider its options. The other countries that maintained

29. Current issues involve the allowable interest rates and the length of credit terms that will be acceptable for the sale of agricultural goods.

30. It has been estimated that the minimum quantities agreed on in place of tariffication were greater than the small volume of rice imports that would have entered Japan under the very high tariffs that would have been agreed on. This reinforces the likelihood that tariffication will be agreed on for Japanese rice in the next few years.

31. Under the agreement, Japan has until 1999 and South Korea has until 2003.

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nontariff measures on the coattails of Japan and South Korea, namely the Philippines and Israel, will not be in a strong position to resist tariffication once Japan and South Korea have decided to go forward with it.

Developments in Domestic Agricultural Policy

The main constraints on international trade policy reform have been the domestic farm support policies of the industrial countries. In fact, trade policies and rules were often developed to validate those policies. Some domestic policies, such as the CAP in the European Union, depended on trade instruments such as variable levies and export subsidies. Others, such as the cereal programs of the United States, relied on trade measures such as the EEP to keep domestic markets in balance and to control domestic spending. Section 22 of the US Agricultural Adjustment Act mandated import controls to support domestic prices and necessitated a waiver from GATT rules. With these domestic policies in place, there was little hope for major reform of the trade system.

However, domestic policies in the developed countries were changing—if from domestic more than external pressures. Country after country faced the same issues: Advances in technology and structural change in agriculture increased yields, but domestic market growth was slow. The choices were (1) control supply (an unpopular solution with farmers), (2) store the surpluses against the next period of shortage, (3) export with generous subsidies (thus distorting other countries markets), or (4) lower farm support prices. Paying compensation to the disadvantaged would make this last option more palatable. Until the mid-1980s, most countries combined supply control and surplus disposal, with some attempts to constrain price increases. After 1985, countries modified their domestic policies and then incorporated new trade rules from the URAA that reinforced the domestic policy changes. The European Union resisted until 1992, when the MacSharry reform allowed the CAP to survive the new trade regime. The United States followed up with the FAIR Act in 1996, which effectively decoupled payments to grain and oilseed farmers and removed the main requirements for supply control.

The aggregate statistics that monitor the development of farm policies are beginning to reflect these policy changes. The OECD split its PSE calculation between market price support (MPS) and direct payments and other (noncommodity) support. In 1986–88, MPS made up 79 percent of the total subsidy equivalent for all OECD countries. By 1996, the MPS had dropped to 60 percent of the PSE. The change is primarily due to the MacSharry reforms in the European Union, where the share of MPS in PSE dropped from 98 to 51 percent. By contrast, Japan still relies predominantly on MPS: the ratio of MPS to PSE is still at 85 percent, the same value as in 1986–88. For the next round, the start of serious domestic reform of

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trade-distorting policies in industrial countries (with the partial exception of Japan) is a given. Thus, negotiators will be able to focus on further necessary changes in the trade rules and on reducing levels of protection.

The New Paradigm in Domestic Policy

Reform in the developed and middle-income countries has ushered in a domestic policy for the agricultural sector that is more trade friendly and more efficient. Policy has shifted away from the manipulation of the commodity price level to assist the agricultural sector and toward direct payments to farm families on the basis of present or past activities. Early signs of this shift in developed countries were the adoption of commodity-based deficiency payments in place of price supports, which allowed consumer demand to respond to market prices. These deficiency payments have become decoupled from present production to reduce the incentive to overproduce. The decoupled payments have, in some cases, been targeted to environmentally friendly farming practices. Income and crop insurance schemes have also been introduced to stabilize rural areas. Developing countries have avoided the budget cost of such programs and generally moved to remove impediments that hindered agricultural production.

The shift occurred because the old paradigm was clearly inappropriate in an open world economy and a less-regulated domestic market. Commodity price intervention rewarded farmers according to their output, regardless of the state of the market. Farm output and structures responded to policy signals rather than consumer demand, and agriculture became dependent on government assistance to dispose of surpluses. Moreover, environmental groups noticed that farming systems geared to high-price policies were creating problems for the water supply, worker safety, public health, and the preservation of plant and animal species. Targeting payments to the farmer is more direct, involves less distortion in production incentives, can be tied to environmental standards, and allows the consumer to chose more freely among competing products (OECD 1994).

Farmers who preferred to be paid through the market, however much that market was distorted by border protection and export subsidies, resisted the policy shift at first. Moreover, the world market was often deemed, with good reason, to be unreliable and unstable. In part, a growing awareness that policies were not achieving their objectives convinced governments to change: The farmers who needed the most help were not the ones who sold the most. Governments also recognized that because so many different countries had these policies, they effectively offset each other, so that a coordinated removal of the policies would have less impact on farmers than a unilateral change by one country. Furthermore, governments reacted to the growing political visibility of environmental

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groups in many countries and to the need for farmers to be more responsive to green concerns. Coupled with these specific reasons was a more general change in government's role in the marketplace. As the notion that governments could, or should, control prices was replaced by the idea that market forces should be the main determinant, the end of commodity price support was in sight.

There has also been a shift in the political influence of agriculture, due in part to the general unpopularity of programs that support particular groups at the expense of the consumer or taxpayer. But in the case of agriculture it may also be connected with the move away from commodity-based support systems. If the government supports the price of a commodity—by restricting imports, subsidizing exports, buying up surpluses, or taxing substitute products—then it usually needs to work through the processing sector or the wholesaler to implement the policy. Sugar policies are operated largely through sugar beet factories and cane refineries. Dairy policy is implemented through the dairies and creameries. Grain policies involve storage and shipping of cereals through merchants and middlemen. Oilseed policies involve oils and meals as well as seeds and beans. When the basis of farm payments is commodity output, there is some coincidence of interests between the processor and the farmer. When the farmer is paid bonuses on the basis of historical hectare and regional yield, the processor has less interest in the profitability of the domestic producer and is more willing to import the raw material and look for the cheapest source of supply.

This decoupling of support from output has had a profound impact on the range of trade policy choices in the sector. Essentially, a country can recast its trade policy for agricultural goods to be consistent with that for nonagricultural goods. Shifting from price supports to income insurance schemes, for instance, makes it possible to relax import regulations: financial instruments can be substituted for physical commodity market intervention, generally at lower cost. Similarly, production constraints that limit government payments on export subsidies are no longer needed if the market price does not influence compensation payments to farmers. The decline of commodity programs liberates trade policy, just as delinking price from income liberates social and environmental policy. These trends in domestic policies have been manifested in different ways in different regions of the world. The next sections review some of these changes as a way of painting the picture of the new environment for agricultural trade policy reform.

Structural Adjustment in Latin America

The Latin American economic reforms that took hold in the mid-1980s were notable (among other things) for their including agriculture. Tariff reform has been extended to agricultural import goods, domestic market-

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ing agencies have lost their exclusive control over supplies, domestic subsidies have been eliminated or sharply cut back, export taxes have been removed, and export agencies have been relieved of their monopoly responsibilities. Agriculture has been made a full partner in the development of a competitive and open economy.

In Chile, reforms were undertaken in two phases, the first from 1973–83 when general macroeconomic adjustments were put into place, and the second from 1984–90 when attention shifted to more sector-specific changes.[32] Trade policies shifted rapidly toward the use of tariffs and the consolidation of most tariff lines at the very modest rate of 10 percent. However, some stabilization measures were reinstated and a "price band" scheme was introduced, which allowed for extra protection for a range of basic foodstuffs (initially wheat, sugar, and oilseeds) if the world price dipped below a five-year moving average. For milk products, a customs valuation scheme was introduced with similar protective effect. But the most remarkable outcome of Chile's economic reform was the rapid development of a sophisticated, quality-based export business that takes full advantage of the country's location in the Southern Hemisphere and overcomes the handicap of distance from markets by investing in infrastructure and negotiating free trade pacts with any willing country.

Changes in domestic policy in Brazil have been particularly important to the liberalization of trade in the region. In 1989, the mass of quantitative restrictions that had hampered agricultural imports was removed, and several state trading agencies, such as those for sugar, wheat, and import licensing, were eliminated. Tariff rates were cut drastically from an average of 62 percent for agricultural and processed goods to 12 percent. At the same time, the government reduced expenditure on agriculture and subsidized credit for rural areas. Emphasis shifted to areas such as rural education and natural resource management. This change coincided with the opening up of the Brazilian market to Mercosur partners and to the adoption of the Mercosur common external tariff, which for agricultural goods ranges from 6 to 20 percent. Argentine pressures for freer trade have since led the Brazilian government to curtail the minimum-price program for farmers and the marketing-loan program, which allowed farmers to sell crops to the government. State involvement in domestic marketing has also been cut back sharply.

Mexican policy toward the agricultural sector has also changed dramatically over the past few years. After the high budget cost of the programs of the 1980s, caused by policies that generally kept prices high for farmers and low for consumers, economic reform was bound to bring some adjustment. However, the speed of adjustment was notable. The

32. The reforms in Chile are discussed in Valdés (1994), Krueger (1992), and Williamson (1994).

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parastatal agency that had regulated the market for basic foodstuffs, CONASUPO, was relieved of most of its powers, and private importation was allowed of all products except for milk powder and the most sensitive commodities, corn and beans. Domestic sectors felt the pressure immediately, with the dairy industry in particular contracting, but the cost of imported feeds declined and the fruit and vegetable sector expanded. A politically bold reform of the land tenure law followed, allowing peasants to buy and sell their shares in communal holdings (*ejidos*) and borrow on the basis of such holdings. Finally, high prices for the major *ejido* products were cut and replaced by payments in the PROCAMPO program that were guaranteed over a period of 15 years. These payments are essentially decoupled from current output and are another example of a policy shift away from commodity price support. The payments have recently been incorporated in a package of policy measures called the Alliance for Agriculture (*Alianza por el campo*), which includes investment incentives and infrastructure improvements. It is too early to say whether these policy reforms will generate a strong competitive agricultural sector, but they are a bold step in that direction.

In Latin America, these domestic policy changes were both necessary to and supportive of the inclusion of agriculture in regional trade agreements. The policy changes make it possible to contemplate opening up agriculture to trade with other countries in the region, and those policies are locked in by the trade agreements. The Mexican case illustrates most clearly the link between domestic policy reform and the negotiation of regional trade agreements. If serious economic policy reform did not extend to the agricultural sector, NAFTA would not have included free trade in agricultural goods. The same story is repeated in many other countries of the region. The Andean Group has established relatively free trade in agricultural products largely by extending the dramatic economic and trade reforms in Bolivia, Colombia, and Peru (and to a lesser extent in Ecuador and Venezuela) to the farm sector and by removing much of the apparatus of state-controlled markets. The major economies of Caricom have also undertaken sweeping reforms of agricultural policy, which have allowed essentially free agricultural trade within the region. Agricultural policy reforms in Argentina and Brazil made it possible to include free agricultural trade within Mercosur.

Policy Reform in New Zealand

In 1984, New Zealand took the lead among the developed countries in the policy reform race. Facing a deepening economic crisis, the new Labor government took a bold approach to economic reform, introducing monetary stringency, economic deregulation, and trade liberalization. The reform also overhauled agricultural programs, which had become

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unwieldy and ineffective.[33] Assistance had increased during the early 1980s, as world prices slumped. The new government judged that the costs were unsustainable, and it terminated output price assistance for agricultural products.

The key to the acceptance of such radical reform was that all sectors of the economy shared in the economic upheaval. The cost of nonfarm protection to the farm sector was already well known. Several of the farm programs had been introduced in part to offset the negative impact that tariffs on manufactured inputs, high interest rates, and uncompetitive exchange rates had on the traditional rural export sectors (e.g., sheep and dairy). Therefore, farmers were assumed to benefit from the reforms in the rest of the economy, which lowered costs through tariff reform and exchange rate adjustment. The programs that were cut included the price-support schemes for livestock, subsidies on capital and inputs, and tax breaks for landowners. In addition, many of the marketing boards, which had been set up as government-sponsored monopolies, lost their market power. The wheat and poultry industries were deregulated, and there was a partial deregulation of the liquid milk sector (Sandrey and Reynolds 1990).

The results were closely watched in case they had some relevance for other reforming countries. Output and land prices fell initially, not least because interest rates were high and the exchange rate was unrealistic.[34] The reforms accelerated changes in the patterns of farm output. But within two years the agricultural economy had rebounded and become profitable again, now in the absence of government support. Reform of the marketing system led to a surge of entrepreneurship in foreign markets and a diversification of the export base, in particular toward Asia. Farmers seem reconciled to life without subsidies, though much of this reflects the generally well-structured farm sector and the absence of uncompetitive sectors in the industry. Moreover, the programs that had been removed were of more recent origin than the farm policies of the United States, Europe, or even Japan. The lessons were perhaps more applicable to a middle-income country that had favorable agricultural prospects but a counterproductive mix of agricultural policies giving inappropriate signals to an otherwise competitive farm sector.[35] However,

33. Assistance to agriculture had grown to about 10 percent of the total public expenditure. For a small economy dependent upon livestock export earnings, these subsidies imposed a heavy burden. The political conditions that allowed these reforms are discussed in Williamson (1994).

34. Total agricultural output fell from $7.6 billion in 1985 to $6.9 billion in 1986. It rebounded to $7.6 billion by 1988 and by 1990 was up to $9.9 billion. Real farmland values declined from 70.2 (1982 = 100) in 1985 to 42.4 in 1988 but started to rise again in 1989. Total assistance to agriculture fell from $1,060 million in 1985 (23 percent of output) to $209 million (3 percent of output) in 1990 (Sandrey and Reynolds 1990).

35. See Valdés (1994) for a discussion of the similarities and differences between the Chile and New Zealand experiences.

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in practical terms it gave New Zealand a new authority in international discussions of farm policies, because it was willing to make dramatic policy changes similar to those suggested to others.

The United States and the FAIR Act

Until recently, the pace of US policy reform made the largest agricultural country seem a laggard by international standards. But as Zulauf (1994) has pointed out, the fundamentals of farm policy had been changing significantly since the early 1980s. Direct income payments had largely replaced commodity price supports to protect farm income, domestic food stamps had replaced public stocks as the main food security instrument, environmental requirements were replacing set-asides as farm program entitlement criteria, and crop insurance was increasingly being used to enhance income stability. These new policy instruments were much more in tune with the needs of a liberal regional trade environment.

US farm policy is by tradition modified by farm bills passed every four or five years. The 1973 Farm Bill contained the first stirrings of reform, with the introduction of target prices and deficiency payments set over rather low loan rates. In 1981, despite efforts by the Reagan administration, there was some backsliding, as price supports were raised for fear of shortage and US agriculture was in a state of shock from rising interest rates. The next significant change in policy came in 1985, when payments were decoupled from yield (i.e., historical yield and acreage were used to calculate the deficiency payments).[36] In 1990, more flexibility was introduced to plant other crops (flex acres), but payments were reduced. The changes in the 1996 Farm Bill, known as the FAIR Act, took a large step in the evolution of agricultural programs.[37]

Traditionally, farm policy debates take place in the Agricultural Committees of both the House and the Senate. Each body debates alternative bills from within the committees and from outside, including the executive branch (the US Department of Agriculture [USDA]). The committees are helped by a range of special interest groups and their lobbyists, each with firm ideas as to the outcome. Although the two political parties usually take diverging views on certain issues, farm policy has been essentially nonpartisan. The situation in the run-up to the 1995 Farm Bill was somewhat different. This time, there was a new actor: the Republican majority

36. A much more sweeping reform from the Reagan administration, to phase out all price supports, was announced dead on arrival at Congress, which was not prepared for such drastic measures. The proposal resurfaced in the early stages of the Uruguay Round, in the context of multilateral removal of trade-distorting policies in the first US position paper of July 1987 (see Moyer and Josling 1990).

37. For an in-depth analysis of the 1996 Farm Bill debate and its significance, see Paarlberg and Orden (1996).

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in Congress, which was elected in 1994 with a tough budget-cutting mission, was wielding a sharp ax to many sacred cows. On the basis of its "Contract with America," the Republican majority began to attack much of the legislative program that the previous 40 years of Democratic control had established. The degree of partisanship increased noticeably, with votes along party lines becoming common, particularly in the House of Representatives. In this climate, farm policy became embroiled in party conflicts.

The push to reduce public spending in all areas and balance the budget dominated much of the political agenda of the new Congress. The big question was, would agricultural programs be subject to their full share of these cuts? Or, would farm programs be spared because of their strong political connections? In the end, the desire for an equitable distribution of the burden outweighed the arguments of the farm interests and their supporters in Congress. In June 1995, Congress adopted its overall budget strategy. Agriculture was to meet a target reduction of $13.4 billion over the seven-year period leading to a balanced budget.[38]

The main congressional actors were the chairmen of the respective Agricultural Committees: Congressman Pat Roberts from Kansas, a strong supporter of traditional farm programs, and Senator Richard Lugar from Indiana, a free trade advocate and critic of conventional farm support programs.[39] Lugar was ready to contemplate a radical reform: he had earlier sent a questionnaire to farm leaders (and academics) that asked fundamental questions about the need for farm supports. Roberts, however, was widely seen as the most powerful voice for the agricultural coalition of commodity groups and farm organizations. The Clinton administration kept a low profile and did not submit a farm bill proposal of its own.

Senator Lugar introduced a bill in August 1995 that was perhaps less radical than might have been expected from a proponent of liberal markets. It was, however, in the tradition of gradual reform started in the 1970s. It would have given farmers greater flexibility to farm set-aside acres but cut price supports and target prices to reduce budget exposure. But in August 1995, Congressman Roberts launched the farm bill debate into high gear with a more radical proposal, dubbed the Freedom to Farm Act (FFA), which would end all constraints on farmers' planting decisions and guarantee continued payments for seven years. Neither bill was voted out of committee. The Lugar bill lost because it failed to garner the support of the Democrats and the more traditional farm-state Republicans. In its place, the Senate committee reported out a bill that essentially preserved

38. The budget cuts are reductions from the Congressional Budget Office baseline estimate of spending under current programs. The relevant baseline calculation was that completed in February 1995.

39. Senator Lugar was at that time a candidate for the Republican Party nomination for president.

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the current programs, subject to sufficient reductions in price to stay roughly within budget targets. The defeat of the House bill was even more surprising and can be attributed in part to the inability of the chairman to convince peanut and sugar interests that the bill would not harm them.

The fact that no farm bill emerged from the House Agriculture Committee was unprecedented. The Agricultural Committees jealously guard their position as initiators of legislation. On this occasion, the momentum of the budget process impelled by the zeal of the Republican freshmen overruled the protection of agricultural turf, and the House leadership chose to put the provisions of the FFA into the budget bill that they sent to the president. However, the budget bill was rejected, causing the government to shut down—on two separate occasions—until the appropriations for the administrative departments had been agreed on. Although the USDA was not among the agencies without a budget, there was some urgency in reaching agreement on agricultural legislation for the upcoming year.

In response to this urgency, a fresh attempt was made to introduce legislation in the House and the Senate, including an Agricultural Market Transition Program (which reproduced the main provisions of the FFA). Finally, in February 1996, the House and Senate each passed a version of the farm bill that included the key elements of the FFA, and a reconciled version of the bill went to the president for signature in April. The secretary of agriculture expressed some lingering doubts on the wisdom of total decoupling, and President Clinton announced that he was dissatisfied with the weakening of the safety net for farmers, but in April the president signed the Federal Agricultural Improvement and Reform Act (FAIR) into law.

The 1996 Farm Bill is novel because it replaces the deficiency payment program with decoupled payments. The payments are specified as a budget subvention of $36 billion spread over seven years. The first-year payment is $5.6 billion. The payment is reduced to $4 billion in the last year of the program, a 28 percent decline.[40] The total is divided by commodity and paid to farmers based on past acreage and yields. Any crop can be grown on the acreage that was previously in the program (and thus can be eligible for the payment), with the exception of fruits and vegetables (unless already double cropped with arable acres). Set-asides are no longer required as a condition of receiving payments.

Not all features of the previous legislation were removed. The system of loan rates is broadly preserved. Farmers can deed their crops to the

40. Based on normal yield, the payments can be expressed (for comparison) as if they were deficiency payments. The USDA calculation of the per-unit benefits for the four major crops in 1996 was $34/ton ($0.92/bu.) for wheat, $0.08/bale cotton (upland), $10/ton ($0.26/bu.) for maize, and $2.78/cwt. for rice. The strong world market caused these decoupled transition payments to exceed the deficiency payments that would have applied under the old legislation. US farmers received a windfall gain from the new farm bill.

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Commodity Credit Corporation (CCC) at the time of harvest and receive a loan. If they wish to sell the crop to a commercial buyer, they repay the loan. If, however, the market price is below the loan rate, the farmer can leave the title with the CCC and keep the loan amount. This nonrecourse loan is a convenient (and popular) way of putting a floor in the market. Marketing loans, which have become common in recent years, also survived. Originally, the notion was to combine an element of export assistance with domestic support. If the price in overseas markets fell below the loan rate, the farmer who sold goods abroad only had to pay back the lower amount. The farmer, in effect, got the loan rate even on foreign sales. The loans for cereals, oilseeds, cotton, and rice under the FAIR Act are all converted to marketing loans. Transforming the deficiency payments into contract or transition payments strengthens the role of the loan rate as a price floor. The loan rates are, however, generally low relative to current market prices and are not expected to be a major factor in the market. Moreover, they can be further reduced if the level of stocks (CCC-held commodities against nonrecourse loans) is high.

The situation for commodities other than cereals and oilseeds changed less. For peanuts, there is a small reduction in price and some increased flexibility in the ability to trade quotas. However, peanuts continue to be a highly protected commodity that generates substantial rents to those who hold the production quotas. Sugar policy was changed slightly: the type of loan is now dependent upon the quantity of imports. When imports are high, the loan becomes nonrecourse, giving producers more price security. Dairy policy is modified somewhat, so that government support is decreased. Support prices will decrease over a period of four years and then be replaced by recourse loans. This gives the CCC the opportunity to eventually withdraw from the purchase and long-term storage of butter, skimmed milk, and cheese. The bill also reduces the number of Milk Marketing Orders, which limit the movement of liquid milk among regions. Finally, the market provisions of the bill place a slightly more restrictive ceiling on the amount one individual may obtain from the program.

The trade provisions of the farm bill contain a few items that are likely to have an impact on other countries and on the trade system. The bill emphasizes export promotion (in part because direct exports subsidies are now restricted by the GATT schedule). Congress trimmed the current program for promoting exports a little (as a contribution to the budget limit), and it tightened eligibility to reflect the criticism that large corporations were gaining most of the benefits. In addition, the government is obliged to help to form an export company (a potential parastatal?) that could market US exports. Congress authorized expenditure on the EEP to increase from the low levels of the past two years to the limit allowed under the GATT schedule. The Dairy Export Incentive Program (DEIP) is also authorized at the maximum GATT-agreed level. High tariffs on

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above-quota imports of dairy products, sugar, and peanuts continue to provide considerable protection for these products.

The conservation provisions of the 1996 Farm Bill are also interesting. Although Congress saves the Conservation Reserve Program (CRP)—up to 36.4 million acres can benefit from payments when placed in the reserve—it will now be easier to bring land into and out of the reserve. Thus, high world prices are likely to stimulate production as acres are withdrawn from the CRP.[41] Some of the features of supply control will therefore survive: moving acres into and out of the CRP will give farmers almost the same benefit that the short-term Acreage Reduction Program (ARP) provided through compensated set-asides. However, the ARP defined eligibility for crop payments, while the CRP does not. US agriculture will be more responsive than before to market signals and less dependent on government decisions as to how much and what to produce.

The FAIR Act has introduced a more complete decoupling of payments from output and cropping decisions. The range of farmer decisions that are influenced by market conditions rather than policy will be greatly expanded. The US farmer has in effect been liberated from government controls on planting and can now react to market opportunity. It is in this respect that the FAIR Act is a fundamental change in approach to the succession of farm bills since the 1930s.

The importance of the FAIR Act extends beyond the United States. It changes the economic conditions for farmers in the most important agricultural exporting country. By moving away from government involvement in the market, the US industry is likely to be more aggressively competitive in world markets. The policy change will also affect world prices. Greater quantity response in the United States will dampen price spikes, though acreage might not contract in times of weak prices. In addition, the policy change in the United States has important implications for agricultural policy reform in other countries, particularly in Europe. It will stand as an example for other countries, and the US negotiating position will be strengthened in the next round.

Canada and Farm Policy Reform

Canadian policy toward the agricultural sector has been undergoing reform for some years. Rather than experience a discrete reform, it has been changed by a series of modest improvements. Many of these have reduced government involvement in commodity price support. Canada was among the first of the major countries to explore the range of income

41. It seems likely that about one-half of the 27 million hectares that are currently in the CRP will remain under continuous enrollment in the program, including land that is particularly vulnerable to environmental degradation.

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policy alternatives that could replace straightforward price support. Starting in the 1980s, the Canadian government attempted to reduce market intervention in favor of direct payments intended to stabilize producer incomes. Examples of these attempts are the Gross Revenue Insurance Program (GRIP) and the Net Income Stabilization Account (NISA), which together took over from the main federal price support programs. These experiments gave Canada a special role in the discussion of decoupled payments during the Uruguay Round, and it had some useful experience with implementing the regulations that emerged from the round. New policies in Canada are closely matched to the WTO green box criteria, and not coincidentally, they are sheltered against international challenge by the Peace Clause.

Among major agricultural countries, Canadian farm policy stands out in two respects. First, responsibility is shared between federal and provincial authorities. Although other federations face similar problems coordinating the conflicting views of their constituent states and provinces, nowhere else are these views so diverse. Different views from province to province exacerbate the problem, as does the continuing controversy over the constitutional status of Québec. That province has the largest dairy production and is the most ardent defender of Provincial Marketing Boards with powers to control access to the provincial market. Agricultural marketing issues are thus entangled with those of the Canadian federation. Although the federal agricultural ministry shares responsibility over agricultural market institutions with the provinces, federal agencies administer some parts of the dairy policy and the federal government has charge of the main parastatal marketing organization for western grain exports, the Canadian Wheat Board (CWB).

Barriers to trade among provinces are another interesting aspect of Canadian policy. There have been a number of attempts over the years by the federal government to achieve a free market within Canada. Agricultural goods, particularly when marketed through the Provincial Marketing Boards, are subject to restrictions on interprovincial trade. Consequently, national food companies have emerged slowly in areas that might be competitive in international markets. And once again, such interprovincial tensions within the country limit the effectiveness and cohesiveness of external policy.

Implementation of the URAA in Canada reflects the importance of these two issues. The biggest change was the introduction of tariffs in commodities, mainly dairy and poultry, that were managed by the provinces through their marketing boards. As discussed above, tariffs were introduced at such a high level that no imports were likely to enter, other than the minimum market access granted under the agreement. Thus, control of the domestic market was preserved for the immediate future, but the industry was set on a course toward increased competition once the high levels of protection are eroded.

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The European Union and CAP Reform

CAP reform has been discussed for 30 years. The policy was set up in the 1960s to stimulate European agriculture by providing a secure domestic market. It proved so successful that food surpluses began to emerge before the decade was out. Inflexible decision making and a lack of financial control thwarted all efforts to modify the CAP.[42] A succession of budget crises led to tinkering with the policy and to broad limits on spending. However, the substance of the policy survived remarkably intact and apparently immune from reform.[43]

The CAP threatened the stability of the European Community in the early 1980s, because its budget costs were soaring. The European Community had to find a way to put agricultural finance on a sure footing and prevent it from precluding other desirable activities, such as fighting unemployment, protecting the environment, developing technology, enlarging the community to the south, and completing the internal market. Thus, the CAP had to be reformed (i.e., brought under control) before it did serious damage to the European Community.

CAP policy reform began with the introduction of milk quotas in March 1984 (strengthened in December 1986), continued with the adoption of the stabilizer package in February 1988, and culminated with the MacSharry reform package of June 1992.[44] The stabilizer package was a fairly modest quasi-automatic device that linked price levels to output at the community level. Guarantee thresholds had been around for much of the 1980s but were generally regarded as ineffective. The 1988 program extended their use to most major products, including cereals, and fixed the penalties for overproduction. Large-scale cereal producers now faced an additional levy of 3 percent (in addition to the 3 percent "coresponsibility" levy already in place), which was only to be reimbursed if output fell short of the maximum guaranteed quantity (MGQ).[45] The levy was to be translated into a fall in the intervention price the following year. If the commission had not negated these automatic price reductions at the annual price review, the price restraint could have affected output. But set

42. The need for unanimity in decision making gave a conservative bias to the policy, and the shared financial responsibility made it less urgent for individual countries to push for reform.

43. For convenience, developments in the current European Union will be considered domestic policy changes and the incorporation of 10 countries of Central and Eastern Europe into the European Union over the next few years will be discussed as a regional trade development.

44. For a full discussion of these earlier agricultural policy reforms, see Moyer and Josling (1990).

45. Coresponsibility levies had been introduced earlier to establish the link between surpluses and farm price supports.

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against productivity changes in the cereals sector, the restraint was modest because small farmers were exempt from the coresponsibility levies (as was grain used for feed on farm), and prices were generally increasing due to the green currency system.[46] And since the cereals stabilizer only lasted for three years, there was no guarantee that any permanent change had been achieved.

The stabilizers program included oilseed and protein crops (field peas and beans), because support costs for these products had been steadily rising, and these costs had to be financed entirely out of the community's budget.[47] The net effect of the stabilizer program on the price of oilseed and protein crops was expected to be minimal. The program may have helped to inhibit soybean production in Spain, but the balance between cereal and oilseed markets remained a contentious issue within and outside the European Community.

One significant aspect of the European Community's 1988 reform package that many overlooked at the time was the sociostructural measure that allowed for direct income assistance to farmers. Farmers earning significantly below the national-average farm income level could receive up to 1500 ecu per year, with the member states covering up to 70 percent of the cost. Though this scheme looked to have been a relatively minor addon to the range of structural programs that were available, from the commission's perspective it seemed significant. It established the principle of direct payments and introduced the idea of nonprice income policies to the political process.

A further intensive review of agricultural policy came in the context of the Uruguay Round. For much of the round, the community resisted changes to its policy instruments. The negotiations issued a direct challenge to the European Community to abandon its support system. The variable levy was to be turned into a fixed tariff, the export subsidies were to be eliminated, and all domestic support was to be phased out (with the exception of research and extension, domestic and international food aid, and some other subsidies that had negligible effects on trade). The EC market management system would have been effectively dismantled. In addition, protection levels would have been slashed by up to 75 percent over a decade. The European Community agreed conditionally to modify its levy system and to scale back the overall level of support by 30 percent (as measured by a Support Measurement Unit, a variant of the PSE) over five years. This would have rescued the CAP, subject to a modification in the levy system. No change in internal market management would be

46. The green currency system established special exchange rates (green rates) for converting agricultural support prices into local currencies. The system proved inflationary as the common prices were ratcheted up in response to exchange rate changes.

47. Border protection for these products was ruled out by the zero bindings negotiated in the GATT during the Dillon Round for oilseeds and by the low tariffs for high-protein meals.

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dictated, and price levels would not have had to be reduced markedly. Meanwhile, the level of support in the European Community was already falling relative to the start of the round, 1986. Thus, whether the CAP would even need further reform had become an issue in the talks.[48]

The issue came to a head in the summer of 1990 with the de Zeeuw draft, which, as it has already been noted, the European Community rejected because it seemed to follow the US/Cairns Group line too closely. Despite President Bush's diplomatic "arm twisting" at the Houston Summit in July, the issue was unresolved at the final meeting of the trade negotiators in Brussels in December 1990. Swedish Minister of Agriculture Mats Hellström attempted to broker a compromise, but failed to convince the European Community.

Within hours of the breakdown of the talks, Agricultural Commissioner MacSharry was circulating a document in Brussels that proposed a new policy development. The support price for cereals, oilseeds, and pulses was to be cut by 35 percent, but the cuts would be offset by hectarage compensation payments to farmers. Dairy and beef prices were also to be cut, with compensation paid to these producers. The plan would allow the community to introduce these reforms and live with greater international constraints. Consumption stimulated by the market price cuts and some reduction in output from a set-aside program would enable the community to reduce export subsidies. After some modification, the policy reforms were passed by the Council of Ministers.[49]

With the June 1992 passage of the MacSharry package, the CAP was radically changed. The package took Europe in the direction of the US farm support policy, though at generally higher levels of protection. The reforms might not have been as radical as most economists would have desired, nor as sweeping in their scope as the European Community's trading partners would have hoped, but no return to the old CAP is likely in the foreseeable future. The URAA has locked in these policy changes and made any backsliding difficult. Also, future expansion of the membership in the European Union will make it almost impossible to regress to the policy as it existed before 1992. The new CAP was distinctive because cereal-market price support was sharply reduced, and farmers were to receive compensation payments that did not depend on current output levels. This change gave a greater degree of flexibility to EC policymaking and weakened the direct link between price support levels and farm receipts.

This change has had important implications for other trading countries. Commercial policy has some flexibility that it has not seen since the inception of the CAP. The new CAP opened up the possibility of reduced con-

48. The link between CAP reform and the Uruguay Round is carefully analyzed in Coleman and Tangermann (1997). Using the analogy of two linked games, they document the impact of the trade talks game on that of CAP reform and vice versa.

49. See the detailed discussion of CAP reform in Swinbank and Tanner (1997).

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flicts between domestic and trade policies. And it moved the community into the growing group of countries that have chosen not to rely exclusively on price policies for income support. Just as the 1996 Farm Bill expands the United States' negotiating possibilities for the next round, so too does the MacSharry reform process for the European Union.

The US FAIR Act is compared with the MacSharry CAP reform in table 11. The two policy reforms are superficially similar but have somewhat different market impacts. The MacSharry reform reduced price supports (for cereals) and replaced the revenue to producers by hectare payments based on regional yield and base year hectares. The farmer must plant a particular cereal or oilseed crop to get this quasi-decoupled payment. The 1985 US Farm Bill had already fixed base hectares and yields, and the MacSharry reform picked up many of the features of the US scheme. The US farm policy is now more decoupled than the EU policy, because the only condition the US policy imposes for receiving the program payments is previous participation. In general, the FAIR Act removes restrictions on farmers, while the MacSharry reform increases restrictions through the set-aside program and the criteria for compensation.

Japanese Revisions to the Basic Food Law

The emphasis of agricultural protection in Japan is somewhat different from that in Europe and other industrial countries.[50] First, support is concentrated in a small number of commodities. Rice in particular is much more heavily protected than are the basic food grains in Europe such as wheat. Other food grains are supported incidentally, to encourage diversification away from rice and discourage substitution in consumption. Oilseeds and animal feed ingredients, by contrast, are imported with fewer restrictions. Beef protection is high in Japan to perpetuate a profitable sector that sells high-quality (and high-price) beef to discerning consumers. Although dairy and sugar are accorded high levels of protection in Japan, as in Europe, they are less crucial to the social and political fabric of the countryside.

As is often the case in Japan, public and private agencies form a web of supporting institutions for the farm sector. In Europe, firms tend to deal at arm's length with public agencies, and the agencies operate with more transparency than in Japan. This difference shows up in the internal marketing of farm products and the importation of foreign goods. With few exceptions, private wholesale concerns are responsible for marketing and importing in Europe. Japan has a mixture of cooperative and private interests that resist competition on the domestic market as well as parastatal

50. A comprehensive account of the state of Japanese policies around the time of the Uruguay Round is given by the Australian Bureau of Agriculture and Resource Economics (ABARE) (1988).

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Table 11 Comparison of EU's MacSharry reform (1992) with US FAIR Act (1996)

MacSharry Reform	FAIR Act
1. Reduces market price and pays hectarage payments	Replaces deficiency payments with contract payments
2. Makes set-aside compulsory	Removes set aside
3. Lowers production through reduction of incentives	Increases production through increased flexibility and removal of restrictions
4. Cuts need for export subsidies but allows full use of those permitted by GATT schedules	Makes (almost) full use of permitted export subsidies, depending upon budget appropriations
5. "Accommodates" US by allowing GATT agreement to be concluded	"Challenges" EU by increasing competitiveness of US agriculture
6. Adds regulations to ensure set-aside compliance and administer compensation programs	Removes regulations and lowers administrative cost
7. Adds to short-run budget cost and promises continued payments	Adds to short-run budget cost, with promise of lower costs later
8. Return to previous policy unlikely due to significant market disturbance	Return to previous policy not ruled out by law but considered unlikely in practice
9. Next reform due in the year 2000, along with smaller changes in fruits, vegetables, and wine sector policies.	Not much change likely in next seven years (sets up a commission to recommend changes by 2002).

marketing agencies that still control imports of several products. The privatization, deregulation, and liberalization of the wholesale sector is one of the more critical issues that affects trade with Japan. In the next round of negotiations on agricultural trade, the issue of state trading and its relation to domestic marketing is bound to be central. In addition, Japan offers a level of protection that is still extremely high compared with other developed countries. Moreover, the changes in farm policy that have been evident in other industrial countries have yet to take place in Japan. Farm income support still rests heavily on price support and supply management, and the move to decoupled payments has been slow.

Public awareness of high prices and rigid marketing systems has increased in Japan in recent years. The strong yen that followed the Plaza Agreement in 1985 made the price difference between domestic and imported foods more noticeable. Imports of grain (other than rice) and oilseeds were joined by other products such as beef, citrus fruits, and processed vegetables. More recently, the country has imported significant quantities of fresh vegetables to complement the domestic supply. The marketing and distribution system was tested by this import surge because traditional channels for the distribution of domestic products were not easily adjusted to the new source of supply. Small retail stores were in increasing competition with variety stores and even supermarkets. It was clear that significant adjustments were necessary.

In April 1994, the Agricultural Policy Council (APC), a body set up to advise the government on future policies, published a report, "The

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Direction of Policy Development in Japanese Agriculture in a New International Environment." This report emphasized that the food system—both the price supports for farmers and the state-controlled distribution channels for the major products—faced a challenge from abroad. It recommended that the system allow for more private involvement in marketing and adjust the instruments of support to be more consistent with multilateral trade rules. Some aspects of the APC report have already found their way into legislation. The government abandoned the Food Control Law and replaced it with the New Staple Food Law of 1995, which goes some way to deregulating the system for rice. However, some of the improvements merely legitimize changes that were taking place through the expansion of unauthorized rice sales. And in some respects, controls on the sector have actually increased. Much remains to be done before the Japanese consumer can be assured of a reliable flow of quality foodstuffs at reasonable prices from the farmers of the world.

Developments in Other Asian Countries

South Asian countries have significantly reformed their economic policy in recent years. The policies that were reformed were often inimical to agriculture, discriminating against the sector by price controls and export restrictions as well as by macroeconomic distortions. A comparative study on agricultural price policies undertaken by the World Bank found that the disincentives to agriculture through exchange rate misalignment and nonagricultural tariffs often outweighed any positive incentives given directly to the agricultural sector (Krueger 1992). In South Asia, the net effect of direct and indirect policies on agriculture was equivalent to a tax of 40.1 percent for Sri Lanka for 1960–85 and of 39.5 percent for Pakistan for 1960–86. (India and Bangladesh were not among those countries included in the study.)

The process of economic reform started with Sri Lanka in the late 1970s and eventually led up to the reform program adopted by India in 1991–92 (see the chapter by Pursell in IATRC 1997). However, India has retained quantitative restrictions on all imports of consumer goods, including those of agricultural origin.[51] In addition, India continues to use state trading institutions extensively in agricultural marketing, and it gives these agencies a monopoly position in international trade. The partial liberalization has lifted controls on storage and export of rice, wheat, sugar, oilseeds, cotton, and livestock. Licensing, price controls, and regulations on processing margins have also been terminated. The oilseeds market

51. Other countries in South Asia have progressed further along the path to reform of agricultural trade. Sri Lanka, Bangladesh, and Pakistan liberalized their agricultural trade policies along with general policy reform, and Nepal has tended to be more open (see Pursell in IATRC 1997).

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has been somewhat liberalized, with a tariff of 20 percent replacing the previous import restrictions. The market for these oils was privatized with the removal of the exclusive import licenses of the National Dairy Development Board (NDDB) and the State Trading Corporation.[52] Moreover, the Rao-Singh reforms of 1991–92 in the nonagricultural sector have had an impact on agriculture, such as the liberalization of investment in the food processing industry.

One problem with Indian economic policy in this area has been its lack of consistency, both from year to year and among the states. Export controls, for instance, were first lifted in 1994 only to be reimposed in 1996 and removed again in 1997. Changes in government have left the private sector to speculate on the longevity of reforms. Agriculture needs the clear signals of deregulated markets and less government intervention. Once again, the importance of external constraints is clear. Removal of remaining quantitative import restrictions and the abandonment of the use of Article XVIII:B of the GATT as an argument for their retention would be a major step forward in this regard.[53] However, as Pursell points out (IATRC 1997), the price gap between internal and world market prices is not yet large, which indicates that liberalization could occur without dramatic changes in the conditions facing domestic farmers.

South Asian policy reform is different from that in Latin America in at least two respects. First, it does not seem to be pushed by regional trade agreements. The one agreement that has been under discussion for some years, the South Asian Association for Regional Cooperation (SAARC), has not yet moved toward a free trade zone and, therefore, has not had to tackle the agricultural issue. Whether this body ever develops the political momentum to influence the pace of reform remains to be seen. Moreover, the multilateral constraints are generally rather weak in this region. The URAA does not seem likely to have the same influence on the countries of South Asia as on the other countries of Asia and the Americas, because the South Asian countries have generally bound high (ceiling) tariffs for agricultural products. The next round may have more impact on policies in this important part of the world.

Regionalism and Agriculture

The most recent wave of regionalism, unlike many of the earlier regional trade agreements, has had significant implications for agriculture. Earlier regional trade agreements have left out agriculture in deference to the political sensitivity of the sector and the potential conflict with domestic

52. I am grateful to Richard Gilmore for information on the status of the Indian reforms.

53. Under Article XVIII, countries can resort to import restrictions if they have severe balance-of-payment problems.

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policy objectives. The situation is rapidly changing. NAFTA, Mercosur, the Andean Group, Caricom, and the Australia New Zealand Closer Economic Relations Trade Agreement (ANZCER) include agriculture in their free trade provisions. The countries of Central Europe have included agriculture in the Baltic Free Trade Area (BFTA) and in a more limited way in the Central European Free Trade Area (CEFTA). The Europe Agreements, which aim for free trade between the Central and Eastern European countries and the European Union, also include agriculture, albeit with some temporary quantitative limits. In Asia, the process has not gone as far: the countries of the Association of Southeast Asian Nations (ASEAN) have been unwilling to incorporate agriculture as an integral part of the ASEAN Free Trade Area (AFTA), though some commodities are included. To the extent that these agreements include agriculture, they have a new significance in the process of liberalizing agricultural trade, and some coordination with the multilateral process is needed.

It is clearly a mixed blessing that the new brand of regional trade agreement includes agricultural trade within the bloc. It carries with it the danger that these trade blocs will shelter and support high-cost production, just as Europe's regime of free trade did within the European Union. But this high-cost production arose because of the high level of support and the protection at the border. Today's new regional blocs seem to have learned the lesson and have generally modest external protection.[54] In other blocs, trade creation seems to have dominated, helped in large part by the domestic policy reforms that have gone hand in hand with the regional trade pacts. Freer regional trade in agricultural products seems in most cases to be consistent with and, hence, a step toward global trade liberalization. The only major qualification is that each member of a regional trade agreement should reduce tariffs on third-country agricultural trade to avoid regional preferences and trade diversion. This could either be done through agreement with other members on external protection, in the case of a customs union, or independently through unilateral liberalization, in the case of a free trade area. Multilateral negotiations become the best way to keep down the level of protection against nonpartner imports and avoid trade diversion. If both internal and external protection is progressively removed, the regional and the multilateral paths promote the same goal.

In addition to trade creation and diversion, regional blocs have dynamic significance for agricultural trade liberalization. For example,

54. Europe's high prices seem to have been an inevitable consequence of the political need for rapid integration between France and Germany, where the latter was not prepared to open up its markets for agricultural goods and instead had to pay to subsidize the export of French surpluses. The system was undoubtedly perpetuated by paying for export subsidies through the common budget, thus making no individual country responsible. Other regional trade blocs seem to have avoided this trap.

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Table 12 Mercosur common external tariff (CET) for agricultural goods

Commodity	Percentage
Beef	10
Rice	10
Wheat	10
Cotton	6
Maize	8
Sorghum	8
Soybeans	8
Sunflower	12–14
Milk	12–14
Sugar	Not in CET

Source: Valdés in IATRC (1997).

free regional trade may release a number of policy pressures that lead toward freer trade in the world as a whole. One way that this can happen is if the regional process has an influence on domestic policy. This will be discussed in more depth after a brief review of the developments in regional trade arrangements for agricultural goods.

Regional Agreements in the Americas

Latin America was an early convert to the regional camp. The Latin American Free Trade Area (LAFTA) and the Central American Common Market (CACM) were both established during the first wave of integration, following the lead of the European Economic Community (later the European Union) and the European Free Trade Association (EFTA). Later, the Andean countries (Bolivia, Colombia, Ecuador, Peru, and Venezuela) decided to split off from Brazil, Argentina, and Mexico to form the Andean Group. Each of these groups followed an economic policy based on import substitution, particularly for manufactured goods, in an attempt to catch up with the industrialized West. This strategy called for high protection against imports from third countries. Agriculture had a minor role and was often excluded from trade liberalization. Statist and corporatist institutions controlled agricultural markets, and producers were often taxed by policies designed to raise funds for industrial development.

There have been dramatic changes in economic policy in the region. As mentioned, domestic agricultural markets have been liberalized. This newfound liberalism has spurred regional trade agreements in Latin America that have an impact on agricultural trade policies and domestic programs. Mercosur, formed in 1991, included agriculture in its free trade provisions, and now farm products flow much more freely among the four full-member countries (Argentina, Brazil, Paraguay, and Uruguay) and among the new associates (Bolivia and Chile). Table 12 shows that the

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common external tariff for Mercosur is also relatively modest. The revival of the Andean Group in recent years has also stimulated agricultural trade among its members, in particular between Venezuela and Colombia. The common external tariff for agricultural products is also set relatively low, but still too high for Bolivia and Peru, which have even more liberal external policies. However, the success of Mercosur seems to be overshadowing the Andean Group and drawing the members of both groups into a larger free trade bloc. The same forces are acting on the CACM and Caricom, both of which have largely liberalized agricultural trade internally but may have to join forces with either NAFTA or Mercosur in the competition for regional market access. The activity of each of these regional groups is becoming oriented toward the formation of the Free Trade Area of the Americas (FTAA) sometime in the next decade or so.

In contrast to the enthusiasm for regional trade areas in Latin America, the United States has always been more wary of local entanglements, preferring the multilateral approach. This began to change in the mid-1980s as the United States sought alternative trade strategies in the face of reluctance by trade partners to start another GATT round. In North America, the 1990 United States-Canada Free Trade Agreement included tariff cuts for agriculture, but not the removal of nontariff barrier.[55] Neither the United States nor Canada thought of the other as a big potential market for agricultural goods, and the GATT round seemed, at that time, to be taking care of agricultural trade issues.

NAFTA (in 1992) also was overshadowed by the Uruguay Round, but in this case, because Mexico wanted more secure access to the US market, agricultural trade could not be overlooked. The result was a substantial improvement in market access through two bilateral (United States-Mexico and Canada-Mexico) access agreements for agricultural products (to supplement the United States-Canada bilateral) and through the trilateral schedules for reducing tariffs within NAFTA. Some agricultural liberalization was achieved when the agreement was signed, and more will follow over the next decade. Nontariff barriers were also phased out on United States-Mexico trade, leading to a relatively free internal market in much of the continent. However, farm trade between the United States and Canada remains governed largely by the preexisting United States-Canada Free Trade Agreement and, hence, is somewhat lagging on the path to liberalization. The negotiations for the FTAA will bring some of these issues to the fore.

55. The exception to this was the liberalization of Canadian cereal import licensing, conditional on lower US protection. This condition was met soon after the implementation of the agreement. The discrimination against sales of foreign wine in provincial retail outlets in Canada was also curbed by the United States-Canada agreement.

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Regional Integration and Agriculture in Western Europe

The European Union's CAP has had the most significant impact of any regional trade agreement on agriculture.[56] Unfortunately, the CAP has led farmers to expand the production of many commodities well above the ability of the market to absorb them at supported prices, and it led the European Union to dump surpluses on world markets for many years. High import barriers also disrupted world trade and led to conflicts with developed- and developing-country exporters. But at least domestic price support policies disappeared in the member countries, and agricultural goods flowed relatively freely (save for some currency fluctuation adjustments) within the union—albeit at high prices.

The contrary experience was evident in the EFTA countries, which decided to leave agriculture out of their free trade zone. Agriculture was also excluded from the series of bilateral trade pacts among the EFTA countries and the European Community that followed the desertion of the United Kingdom and Denmark from EFTA in 1973. Clearly, trade barriers could not be reerected among former EFTA partners: free trade between EFTA and the European Community looked to be the answer. But in agriculture and fisheries the issue did not arise. No new barriers were erected on farm products because no preferences were eroded. The talks that aimed to establish a European Economic Area took the same approach. Rather than open up the question of trade in agricultural products, the European Community and the EFTA countries agreed that it be left off the table. By the time three of the EFTA countries came to join the European Union, they still had relatively isolated and highly protected agricultural markets. Removing the domestic price policies in these countries (with the exception of Sweden, which had just undergone an agricultural policy reform of its own) implied a reduction in support to farmers. Nordic and Alpine farmers considered joining the European Union a process of agricultural market liberalization, an outcome that the Norwegian farmers chose not to accept. Thus, free trade has finally come to most of these countries in agricultural goods, but at the high internal prices of the European Union.

Central European countries had been part of a somewhat different type of trade agreement, together with the former Soviet Union and other Eastern European countries. The Council of Mutual Economic Assistance (CMEA or COMECON) was founded in 1949 as an Eastern European "counter" to the Marshall Plan and ended up as a "counter" to the Common Market of the European Union. It was intended to facilitate trade

56. An intimate link between political and economic integration separates Europe from other continents, where regional trade arrangements often are deliberately kept distinct from political integration and any hint of federalism is avoided. Nevertheless, the extensive experience that Europe has had in the area of regional trade arrangements makes it an important point of reference. Moreover, what happens in Europe affects other countries and the world trade system.

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through complex bookkeeping and planning devices. It did not promote free trade in the Western sense. It did, however, provide secure outlets for predetermined sales of goods, including agricultural products. As such, it constituted a system of intensive intraregional trade, even where such trade may not have been generated by market supply and demand. This trade collapsed with the breakup of the CMEA and the Soviet Union, making the transition to a mixed economy more difficult.

The key issue for the next few years is whether the countries of Central and Eastern Europe, as they line up for membership in the European Union, will resist the pressure to protect their agriculture in anticipation of enjoying the high prices and secure markets of the CAP, or whether political leaders will convince farm groups that they need to become efficient and competitive and wait for the European Union to further reform its policy by the time of accession. In this regard, the creation of CEFTA and the BFTA have significant implications for agriculture. They allow trade to continue in the region at a time when the Europe Agreements with the European Union are attracting trade to and from the Union.

Asia and the Pacific: Regional Integration

Asia has the least experience with regional trade agreements. Therefore, the effect of such agreements on agriculture is much less significant than in other regions. However, the ANZCER is one of the most successful regional trade arrangements from the viewpoint of agriculture. Farm products flow freely between the two countries, even where domestic marketing regulations were modified to allow competition between these two countries. The dramatic domestic policy reforms undertaken first in New Zealand and then in Australia obviously paved the way for regional free trade. But the regional trade agreement deserves some of the credit for overcoming domestic resistance to reform. The same blending of domestic and regional reforms may be under way in other parts of Asia. ASEAN has long operated a collective agreement on food security, involving the sharing of rice stocks at times of shortage; otherwise, it has had little agricultural content. Agriculture is to be largely excluded from the recently strengthened AFTA, though a few agricultural goods benefit from regional preferences. Countries in Southeast Asia have shown less interest in reforming agricultural price support schemes and allowing more intense regional competition through free trade areas. Other parts of the region are also reluctant to try the path of regional free trade. A meeting of the South Asian Association for Regional Cooperation in May 1997 set a date for completing the free trade area between its seven members (Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan, and Sri Lanka) at 2001. However, these countries have been discussing a preferential trade regime for some time to no avail, and bilateral disputes have sapped the political commitment to cooperate on economic issues. It would appear

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that multilateral negotiations in the WTO (or supraregional plurilateral surrogates such as APEC) may be the more effective lever to open the attractive markets of Asia.

Regionalism and Domestic Policy Reform

The dramatic increase in the number and size of regional trade agreements in the past decade has posed an interesting challenge for agricultural trade policy. As regional trade arrangements have increasingly included agriculture in their free trade provisions, the clear distinction between domestic imported products has broken down. Goods imported from countries with which a free trade agreement has been concluded undermine the ability to control the domestic market. Though the danger is that the partner country is a high-cost supplier, and the agreement will divert trade from more competitive supplier, the threat to the control of the domestic market is also important.

One solution is to introduce collective protection against outside products, as exemplified by the European Union's CAP—though this can result in high levels of protection. Thankfully, recent regional agreements have avoided the trade-diverting problems of the CAP. Common market intervention policies have rarely been tried, and domestic support prices have generally been moderated when regional groups have formed. But it would not be accurate to conclude that such regional schemes have had minimal impact on agricultural policy reform. Countries joining such groups are discovering the strength of the linkages between domestic policy reform and regional trade liberalization. Mexico used the lever of NAFTA to complete its own radical domestic liberalization program. The reform, in turn, has helped it to maintain pressure on the United States to keep to the NAFTA schedule for import liberalization. Canada has felt the pressure of NAFTA-induced trade liberalization on its beef and pig meat sectors, if not so much on dairy and poultry. Freer regional trade in food products has pressured governments to reduce price support on locally produced raw materials. Even the United States has felt some pressure from NAFTA, resolving a long-lasting dispute over avocado imports from Mexico and allowing more Canadian grain into US markets. Regional trade agreements have direct effects on domestic agricultural policies that push the countries concerned in the direction of policy reform. Once trade is liberalized within a region, the degree of competition within the region becomes a matter of interest for the member countries. Subsidies clearly distort competition and will be unpopular. Different marketing systems may create problems, in particular if some of them appear to offer hidden subsidies. Regional trade agreements also have indirect and long-term impacts on domestic policy choice that are just beginning to be noticeable. Regional agreements and agricultural policy reform are indirectly linked through the impact of the partial opening of borders on the effectiveness

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of policy (Josling 1993b). In some cases, this will lead to harmonization, and in other cases, to common policy instruments. In a few instances, policies will become so ineffective that they may have to be abandoned. Whatever the reaction, domestic policy will look very different after a few years of adjustment to regional trade agreements.

The case for harmonization of policies can be seen in the matter of tariffs against third countries. In free trade areas, these tariffs are still in the competence of the individual member. Trade deflection (the transshipment of goods through the lowest-tariff country) is controlled by rules of origin and calculations of domestic (regional) content. Two problems immediately threaten the ability of even the most diligent customs service to make these effective. First, homogeneous commodities are much more difficult to track and label with a country of origin than are differentiated and specialized parts for manufactures such as the automobiles. Second, and more fundamentally, nothing can stop a country from exporting its production to its partner and importing for consumption. This "legitimate deflection" can only be deterred by common external tariffs or by quantitative trade controls at the external border. A small country that has a free border with a large neighbor must take on the larger country's tariff structure when it is lower than the small country's (subject to transportation costs, of course), and it must develop profitable exports when it is higher.

The impact of different export policies is even more clear-cut. If one partner has an export subsidy, then free regional trade will encourage imports from neighbors either (illegitimately) for reexport or (legitimately) to replace the exported quantity on the domestic market. In effect the export subsidy becomes a common policy.[57] This is the underlying cause of the conflict between the United States and Canada on the rising exports of Canadian wheat to the United States. In addition, export subsidies on internal trade are likely to be outlawed within a free trade area, because they are obvious distortions of trade. The United States-Canada Free Trade Agreement, which preceded NAFTA, accomplished this task. The arbitrage possibilities of regional free trade strongly weaken national policy instruments. One good example is a supply control that aims to raise the price of a product by restricting supplies onto the domestic market. However, some form of border protection (usually in the form of an import quota) is needed to make supply control effective. If the regional trade agreement removes such external protection, then the domestic supply control is rendered ineffective. This same reasoning applies to policies that try to stabilize the domestic market, such as holding public stocks. Such policies are made less effective or more costly by a free intraregional market. This indirect impact through arbitrage may prove in the longer run to be the most significant link between regional trade agreements and the changes in domestic agricultural policies.

57. For the same reason, export restrictions are also difficult to maintain.

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