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PROBLEMS OF US-EEC TRADE:
SOURCES OF CONFLICT AND THE NEED FOR COOPERATION

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Problems of US/EEC Agricultural Trade: Sources of Conflict and the Need for Cooperation.

In this paper I shall discuss the specific points causing friction between the United States and the European Economic Community in agricultural trade, categorizing these according to whether they fall under the heading of bilateral trade or multilateral issues (i.e. competition for trade in third-country markets). I shall deal in most detail with grain trade issues, as being potentially the most abrasive, and consider the extent to which the current recession in US grain exports can be said to be the fault of the European Community. Finally I shall point to the advantages of cooperation over confrontation, and suggest certain lines of policy along which cooperation should be developed. First a bit of history from a British point of view, particularly concerning grain markets.

I have been concerned with EC agricultural policy - in particular the grains sector - since 1972, when I formed part of the team which negotiated UK entry to the European Community. The US government was whole-heartedly in support of our application to join. The Soviet Union was equally emphatically opposed to it and tried by all means to influence trade union and public opinion against it. I was myself in favour of joining - the reason was simple. It was in the Western interest to make Europe strong and united: it was in the Soviet interest to keep it weak and divided. I

reasoned that if the Soviets were so strongly opposed to our entry, joining the community must be the right thing to do.

In the entry negotiations the UK made no serious attempt to change the Community's Common Agricultural Policy (which I shall refer to as the CAP). Although it was totally different from our existing policy of support through deficiency payments. We were in no position to do so. We had been refused membership twice - once in the Macmillan Government in 1960 and once in the Wilson Administration in 1967 - and the plain fact was that if you apply to join a club that usually means that you agree to accept the rules of that club. In fact we sought exceptions for the import of butter and lamb from New Zealand, and the results are contained in Protocols of the Accession Treaty. These exceptions were not popular with British farmers, but they were regarded as justified by the country as a whole, in view of New Zealand's historical relationship with the UK.

Although in 1972 over 50% of the British bread grist was composed of high-protein hard (or strong) wheats imported from North America - and we were then importing over 4m tonnes a year of these wheats - we did not seek a special regime for these imports. It was simply not negotiable, as the then deficit UK cereals market was one of the few attractions which British membership offered to continental producers, especially France. Moreover we had already been obliged to introduce an import levy on cereals

even before we joined the EEC. As a matter of fact neither Canada nor the US pressed us to seek exception for grain imports - they were realistic enough to be aware that it would not succeed. Later on, under the second Wilson Administration, in 1974, and largely due to pressure from our own millers and feed compounders we did seek a concession as part of the famous "re-negotiation" package prior to the referendum on European membership, but it got nowhere. I was present in the Council of Agriculture Ministers when the case for a reduced levy on hard wheat was presented. The EEC Commission opposed it as infringing the sacred principle of Community preference, the Dutch Minister to whom we had looked for support ostentatiously read a newspaper during the discussion and nearly everybody else misunderstood the translation and thought we were talking about durum wheat. Looking back I regret this. It would have helped to kept down the Food Price Index and thus made the EC less unpopular in the eyes of the British public; it would have restrained to some extent the growth of wheat production in the UK and provided small additional outlets for North American exports. One should not exaggerate this however. It was the Soviet crop failure in 1972/73 which drove up grain prices even above the Community's threshold price, the success of the plant breeders at Cambridge which almost doubled wheat yields in a few years, and the invention of the Chorleywood Bread Process which enabled

British machine bakers to incorporate much higher proportions of European wheat in the bread grist.

Now let me turn to the present day and look at some of the wider problems of EC and US agricultural trade. What are these sources of conflict which we must consider? They are of two main kinds - the first bilateral - that is to say which concern US exports to the EEC and vice versa; and the second multilateral in the sense of situations where the US sees itself suffering from unfair competition in third countries.

1. Bilateral Problems.

These are the following:

1) Cereal substitutes. This concerns primarily corn gluten feed (though other substitutes include manioc, citrus pulp, etc.,). Corn gluten feed is produced in the US as a by-product of high fructose corn syrup or isoglucose (the sweetener now used by the US soft drinks industry) or of ethanol. It enters the European Community levy-free under a concession granted in the GATT Tokyo Round before HFCS was invented. Imports have been running as high as 3 m.t. p.a. The Community sees this as a loophole in the CAP which is preventing the domestic consumption of an equal or higher quantity of EC feedgrain. Nothing has happened since May or June last year when the Member States approved a mandate to the Commission to approach the US to negotiate limits on cgf imports. The US finally agreed to talk, but said little,

and - since it takes two to tango - the problem is at present dormant.

2) Rice. It is anomalous that the CAP imposes a high tax on long-grain rice which cannot be grown in Europe in order to protect varieties which can. But this is mainly an Italian interest. On the whole the US makes surprisingly little fuss about it and my wife like many others is resigned to paying a high price for the packets of US rice which her supermarket continues to stock.

3) Citrus The EC grants preferences to N. African countries and Israel. The US picked this out for a quarred not because of its great importance, but because it thought it had a good case in GATT, and indeed got a favourable opinion from the GATT panel. The EC reckon that the Mediterranean countries constitute the Community's backyard just as the Caribbean is the US's backyard. If President Reagan can justify his Caribbean and Central America initiative the EC think they should be allowed to help the developing countries of N. Africa. There is no economic advantage for the EC in this but it does promote political and economic stability in the Mediterranean. The US also has its own special arrangements with Israel and ought to be grateful to the EC for sharing the burden. However, this problem cannot be disregarded because it will blow up again when Spain and Portugal enter the Community.

4) Pasta. The EC pay export refunds on pasta and the argument centres around whether GATT rules allow subsidies

to be paid on processed products (or just on primary products). The GATT panel gave a divided opinion or some say in favour of US. The US introduced high duties on imports of pasta, which irritated the EC who both threatened to put duties on US walnuts and lemons, and offered to reduce the pasta subsidy. A truce has been called until November and this is really a storm in a teacup.

5) Dried fruit and canned fruit. The point at issue here is whether the EC system of support by direct aids is compatible with GATT. On canned fruit the GATT panel has issued a decision favourable to the US which the EC has blocked. Canned fruit has been a bone of contention for a long time; dried fruit since Greece entered the Community. The President has warned the EC that if the canned fruit problem is not solved by December 1st the US will act. The EC has tried to lower the temperature by reducing aids to canned fruit producers.

6) Almonds. The US is campaigning for a reduction in the EC's 8% fixed tariff because it fears that once Spain is in the EC US imports will be squeezed out. In return they are offering compensation for the benefit of the Italians in the form of a higher quota for Italian cheeses.

7) Wine. Last year the California grape industry filed a protest with the International Trade Commission against French and Italian producers. The ITC said 1) grape growers are not wine producers and therefore not entitled to file; and 11) anyway no evidence of damage had been produced.

However the grape growers have filed again on the basis of a new US law which the EC says is incompatible with US obligations in GATT. Since EC wine exports to US are around $700 million per annum the trade is politically sensitive in the EC, and this could grow into a damaging dispute.

8) Community exports to the US. This time it is the EC grumbling about US restrictive practices. After World War II when GATT was set up and before the US had become a major exporter America insisted on being given a waiver to allow her to operate limitations to the extent required to protect her own domestic agriculture. This affects US imports of milk products such as cheese and butter on which the US regime is very restrictive; of beef and lamb (which is less restrictive but the Australians and New Zealanders are most affected, not the EC); and on sugar where there is a very strict quota regime (which encourages inter alia production of isoglucose). The EC say this is iniquitous because whenever the EC has imposed restrictions it has negotiated out of its obligations by granting compensation (e.g. the CAP levies and refunds). Also they say that the original waiver was granted on the understanding that these measures would be gradually phased out over 30 years, and they haven't been. This may well come up again in the next GATT round.

2. Multilateral Problems.

1) Eggs and poultry. These are grain-related products. Here the blame for US problems is more distributed, the

chief offender now being seen as Brazil (but if it has a $90 bn debt can you really criticize a country for trying to maximize its exports).

2) Dairy. The US operates a system of dairy support like the EC but without export restitutions. They give their surplus away free to institutions like the US Army and increasingly do one-off subsidized deals. The US has increased its share of the world market while the EC has lost market share (the reverse side of the coin compared with the grain sector). There was a row over Community sales of old butter to E. Europe and the US withdrew from the International Dairy Agreement so as to be able to undercut the system of minimum prices.

3) Grain. This is the really explosive issue in this marketing year. It is a monumental question of struggle for markets and of surplus disposal - of increased stocks and record harvests on both sides of the Atlantic, of sustained high production and shrinking outlets. Look at the world figures:

Wheat

Year	Production	Trade	Consump.	Stocks
1981/82	454m	101m	447m	100m
1985/86	515m	95m	510m	141m

Over the same four-year period the price of US no 2 Hard Winter f.o.b Gulf has dropped from $171/t. to $125/t.

Coarse Grains

1985/86 Production is forecast at a record 836 m tonnes (+38m), trade down by 13 m. and closing stocks up to 145 m. tonnes (+45 compared with last year). The surplus position is thus no better than for wheat.

Shrinking markets. China and India, both formerly importers are now exporters or becoming so. Russia who took 55m t.last year is only expected to take 35m this year.

3. Opposing Arguments in the Grains Sector.

What is the specific US complaint? They say that they have lost market share to subsidized EC exports and that this is unfair; the markets must be recovered, and if the EC is not prepared to give way gracefully she must be driven out of these markets by force of greater subsidies. The use of the word BICEPS to describe this process is not an accident.

As a farmer myself I have a great deal of understanding of the US point of view in this matter. When I was here in the Mid West in June I saw a number of Minnesota farms; obtained data on the critical indebtedness of grain farms; the calamitous drop in land values; the parlous situation of rural banks who see the value of the collateral on their farm loans disappearing and agonize over whether or not to foreclose; I spoke to the export managers of grain companies whose own jobs and those of many others depend on revitalizing the export traffic; I spent three days travelling on a Mississippi grain barge-tow and know the

hardships on which this magnificent transportation system has fallen. I can thus well understand the political pressures being exerted on Capitol Hill to do something, preferably to strike back. The Americans regard themselves as the most efficient producers in the world (which indeed they are though grain yields here are only half what they are in the EC) yet they are victims of circumstances outside their control. However hard they work they can't improve their condition. Therefore, they feel frustrated and angry.

What does the EC say about it? Several things. First, they take the view that they are not to blame for the US predicament (or at least not mainly to blame) and that they have been cast in the role of scapegoat for US frustration. They suggest that the US have largely brought the trouble on themselves by fixing loan rates too high in the 1981 Farm Act, and when this was combined with the strong dollar it set up an umbrella under which not only the EC but other exporters could sell. The American mistake, they say, is to try to set a world price at this level, to balance the world market as a whole, buying up enough grain to keep prices at this level and not adjusting to the fact that others then get in underneath them. The Argentines have been consistently undercutting US prices; the EC have in fact been very restrained: they have monitored wheat exports very carefully, not attempted to compete with low Argentine prices; it is nonsense to say that they have been irresponsible - or they wouldn't have accumulated stocks,

unlike the Argentines who do not hold stocks. The European Commission point out that the conjunction of strong dollar and high US support prices led to a situation last October where the EC were exporting virtually with a nil refund: by stepping up the refund then they could have exported all they wanted to and really taken over US markets, but they didn't - they excercized restraint. In accordance with GATT they refrained from taking more than a fair share of the market. And how were they repaid for acting responsibly? By the US "targeting" export markets like Algeria and Egypt (which are as close to the EC as Central America is to the US). By selling to Egypt at $8/t. below the prevailing world price the US effectively set a new world price entailing lower returns to all exporters, and obliged EC to increase their export refunds by 20 ecus a tonne. The more recent sale to Algeria involves I understand a subsidy of about $40/45 per t. i.e., even below the Argentine price, now around $90 per t. Who benefited? The buyers of course. Who is laughing all the way to the Narodny Bank? Mr. Gorbachev. Why do you think the Russians have held off the grain market this year, defaulted on their minimum purchases under their bilateral agreement with the US? Because even the <u>threat</u> of action under the BICEPS programme has created an expectation of lower world prices. I am told that some people even in USDA think it was a mistake.

There is some support for the Commission view among American economists. Professor William Meyers of Iowa State

University in a paper presented to the Curry Foundation Conference this June pointed out that the US expanded its share of the world grain market from 37% in 1970 to 56% in 1979. That it has since fallen back to 48% is due to three factors according to Meyers - changes in foreign income growth, changes in US exchange rates, and EC support prices. Of these three factors the impact of the CAP is the smallest - the other two are 5 times more important. This view is shared by Robert Paarlberg of Wellesley College (Curry Foundation Conference).

4. Likely Consequences of These Disputes.

What will happen if the disputes sharpen, and how much does it matter?

First, we are in for a damaging competition in the grain export sector. Under pressure from farmers and export managers etc. the US will step up their BICEPS programme and become more efficient at using it. In return the EC, now that it has the prospect of a raised VAT ceiling and sufficient money in the budget, will step up the export refunds to retain its markets and this will be extremely costly and make everyone on both sides very angry.

Some of the specific cases mentioned such as pasta, wine, and canned fruit could become bitter arguments with reprisals. If US protectionism spreads the EC may take action against corn gluten feed and pressure will increase for action against soya through the oils and fats tax which is still on the table. It should be remembered that the

counterpart of the decline in US grain exports to the EC has been a vast upsurge in exports of soya. US soya exports to the EC over the past 3 years have been between $2.4 bn and $3.9 bn so there is a lot at stake here. (Lest this appears alarmist I would add that the European Commission at present say they have no intention of taking action against soya.) Furthermore, the EC is the world's biggest importer of food and farm products and the US farmer's best customer. In fiscal 83 the US exported farm products worth $7.6 bn to the EC - $1.75 bn more than to Japan and $2.75 bn more than to the whole of Latin America. The EC ran a balance of payments deficit with the US last year of $3.6 bn on farm trade. If Congress turns from the popular pastime of Japan-bashing to that of EC-bashing there is a lot to lose. There is moreover a danger that agricultural disputes may spill over into other trade, sour political relationships and eventually impair even defence cooperation.

5. Possible Courses of Action.

So what are we going to do about it? Responsible politicans pay lip-service to the need to avoid conflict but the politicans in Europe only worry about losing votes (the same may apply in the US) and the danger is that leaders will be forced into acting against their better judgement. I am not optimistic. Things will get worse before they get better. There is a possiblity of disorder on the world markets. For the present we must all be concerned about damage limitation.

For this purpose the most important thing is to maintain and improve communication. The present scheme of official contacts is quite inadequate for this purpose.

There are EC/US Ministerial meetings December each year in Brussels, the US team headed by Mr. Schulz, the EC team by the President of the Commission, M. Jacques Delors. Finance, Foreign, Trade and Agriculture Ministers are involved on both sides.

There is an Economic Summit annually. The next one is due in Tokyo in May 1986. There are also periodic visits by single Ministers.

Talks between agricultural officials on both sides in Brussels have run into the sand and need revitalizing. The US Mission must be authorized to say more than that the Administration is not interested in market sharing.

The best hope is for progress in the next GATT round. The US has offered to put the waiver on the table. The Community has got its act together on GATT and is operating effectively in Geneva. The EC has agreed to discuss services which the US is keen on (problem is India and Brazil). The latest breakthrough means that a date could be fixed in the spring and the next GATT round start later in 1986. But we must recognize that GATT negotiations are long drawn-out and there must be continuing action elsewhere.

The existing contacts should be strengthened and supplemented by greater informal contacts. A useful example can be found in those between the EC and Australia. The

European Commission meet top people in the Australian Departments of External Trade and of Primary Industry. They compare forecasts of production, consumption, and what analysis of the market both parties are basing policies on. This sort of discussion is better than puzzling over diplomatic notes. The European farm organization COPA could talk to the American Farm Bureau and NFO. They should check figures together and discuss what the target is. They should assess what threats are genuine and what aren't.

We might even consider a North Atlantic Agricultural Council, whose task should be to coordinate official and non-official contacts and to provide a forum for exchanges of views and negotiations.

The first specific aim of negotiation - let us say in the December Ministerial meeting - should be to reach agreement whereby the US would drop BICEPS in return for an undertaking by the EC to limit export restitutions. The first point to recognize in exchanging views is that what divides us is of less importance than what unites us. In the farm sector we face many of the same problems, some of which I have outlined above - namely, surplus production, overhanging stocks, and shrinking markets. We both have an agricultural industry which is under threat due to the depressing effect on returns caused by these circumstances, leading to insupportable debt and a shrinking asset base. There is an uneasy awareness that the agricultural sector on both sides of the Atlantic is faced with an inevitable

process of contraction. Instead of sterile squabbles which benefit nobody but our customers and our competitors we should be looking for a joint approach to alleviate the situation. We share, for example, to a large extent a common interest in conservation and in improving the environment and quality of life. We both have a caring approach to the problems of famine in Africa and should increase the quantity of basic foodstuffs needed to combat hunger in this area, while at the same time taking all possible steps through the appropriate international institutions to increase the purchasing power of developing countries so that trade can legitimately expand.

We must not allow ourselves to fall into the trap of permitting the capitalist world - the western democracies - to tear itself apart by its own contradictions, as our adversaries so confidently predict. The only alternative to this is the way of consultation and cooperation.