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Government Interventions In Agriculture

National Policies and Agricultural Trade. Organization for Economic Cooperation and Development Paris, 1987, 344 pages, $25

Reviewed by Mathew Shane

There are serious conflicts in global agricultural markets between growing world interdependence and domestically focused agricultural policies The current Uruguay round of multilateral negotiations under the auspices of the General Agreement on Tariffs and Trade (GATT) offers a strategic opportunity to alter fundamentally international agricultural markets and to overcome growing conflicts Domestically focused policies have led to a misalignment of production and use of agricultural products with resulting cycles of substantial surpluses followed by global agricultural shortages

In this book, the Organization for Economic Cooperation and Development has provided a benchmark study on the magnitude and consequences of national agricultural policies As such, it is a major contribution to the global analysis of the effects of government interventions in agriculture It should be read by all serious students of the subject The report is timely and relevant given the current multilateral GATT negotiations

The report is divided into six chapters Eight annexes follow In some ways, these are the most interesting part of the report For instance, tables 2 and 3 on pages 117-8 provide detailed estimates of producer subsidy equivalents (PSE's) and consumer subsidy equivalents (CSE's) by country and commodity Table 4 on page 134 provides estimates of the level of costs of agricultural policies compared with gross domestic product (GDP), gross value added by agriculture at market prices (GVA), and final value of agricultural production (FVAP) Agricultural subsidies are, not surprisingly, small compared with GDP since agriculture in industrial market economies is a relatively small sector The costs of the policies in terms of GVA and FVAP, however, are enormous ranging from a low of 6 1 percent of FVAP in Australia to a high of 58 percent in Japan Compared with GVA, the high exceeds 100 percent for Japan and approaches 100 percent for the EC

The conclusions of the study are equally unsurprising, supporting the same general conclusions which have been flowing out of the work at ERS and elsewhere Nonetheless, the importance of these conclusions make them worth scrutinizing

- "Policies have aggravated the growing imbalance between supply and effective demand at current prices and the spread of the imbalance to most commodities and to most countries " (p 7)

- "The level of assistance to agriculture during the period 1979-81 was quite substantial averaging over one third of the value of output for OECD producers and over 60 percent, on average, for dairy and rice About half of this assistance came from Government budgets and half from transfers from consumers Support levels were this high even though this period was one of generally buoyant markets with limited intervention compared with more recent years " (p 13)

- "Agricultural trade problems have their origin in a set of domestic policies that shield producers from world market signals and are incompatible with the upward trend in agricultural productivity and the low growth in food demand facing OECD countries Policies, whose principal although not exclusive purpose is to improve the level and stability of the standard of living of farmers, have been largely implemented on the basis of raising the value of output resulting in the expansion of supply beyond market requirements " (p 24)

- The income objective of agricultural policies "has not been entirely achieved to achieve it in a more economic and more socially-acceptable way and with the minimum distortion to trade requires a switch away from measures that stimulated output " (p 25)

- "Policies have evolved to counteract the effect of other policies, either of domestic origin or not A partial approach, even a unilateral approach, could bring benefits to domestic consumers, to other economic sectors through better resource use and to other exporters if reductions are made by those countries which heavily subsidise exports However, the partial approach is likely to generate some further imbalances in some cases, exacerbating international trade tensions, and to yield significantly lower benefits than multilateral reform If progress is to be made in resolving the serious problems confronting all OECD members, a multilateral, multi-commodity approach, both to the analysis and the resolution of the problems, should be urgently pursued " (p 49)

Shane is deputy director of the Agriculture and Trade Analysis Division ERS

- "The higher the degree of insulation of domestic markets, the larger are the world price changes which result from unforeseen changes in market circumstances The inflexibility of agricultural policies has led in most cases to agricultural trade actions by OECD countries that have exported agricultural adjustment pressures to world markets " (p 60)

- "There is little choice but to accept that, for the OECD area, adjustment at the point of production is an essential part of reform Such a reorientation, by reducing the export of adjustment pressures will be a major contribution to an enduring improvement in the situation " (p 61)

- "The present problems of agriculture stem primarily from past policy incentives which have led to an excessive expansion of production capacity while the food needed could be produced with far fewer resources and at a lower cost with consequent gains to the whole economy Furthermore agricultural assistance policies have not been sufficiently adjusted to take account of productivity increases and the rigidity of the support mechanisms have [sic] not only prevented the appropriate market signals from being transmitted to producers, but has in several cases been interpreted by farmers as an encouragement to produce " (p 69)

Although the study is well done and an important contribution to this area, there are some serious limitations to the analysis For example

- The study has limited commodity and country coverage The focus is on liberalization of the major industrial market economies' agriculture Although the developing economies tend not to subsidize their agriculture, they still intervene substantially in their agricultural sectors Any analysis that assumes that the developing countries are not subject to policy reform is omitting a major part of the global agricultural economy which could lead to serious errors of interpretation

- A partial equilibrium global commodity model is used No consideration is given of the interindustry effects of liberalization of agriculture Other analyses of multilateral liberalization using general equilibrium models conclude that major changes occur in the nonagricultural sectors because of trade liberalization

- The analysis is static in nature Most of the benefits of trade liberalization will come from the induced structural changes which occur because of the removal of constraints to economic agents As such the benefits as estimated in this study should greatly understate the potential benefits of policy reforms

- The liberalization scenario is a very limited one One must ask whether a 10-percent reduction in subsidies represents policy reform at all An analysis conducted at ERS suggests that almost all countries could undertake such a reduction without a major change in their policy regimes The increase in world prices caused by the 1988 U S drought reduced subsidy levels as measured by PSE's by more than 10 percent

- Finally, what is the United States hoping to accomplish by the multilateral negotiations under the GATT? Reducing subsidy levels? Reducing the trade-distorting effects of the current policies? If the United States is interested in the latter, then the PSE's are a poor measure of trade-distorting policies Rethinking of the analysis, and better tools for the measurement of government subsidies are required

The United States faces a world that is increasingly interdependent, both in terms of trade and financial resources, and yet agricultural policies are still designed for a world in which international consequences of domestically focused policies are quite small The increasing divergence between this growing interdependence and interventionist agricultural policies is the longrun driving force toward reform

Aside from the obvious benefits of trade liberalization and as clearly recognized as the current inefficiencies within existing policies, the movement toward reform has been slow, unsteady, and uncertain The current lack of progress in the GATT negotiations on agriculture is an indication of how difficult it is to change policies that benefit a few well-organized groups whose costs are broadly dispersed

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