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AGRICULTURAL TRADE IN THE URUGUAY ROUND: INTO FINAL BATTLE

by

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I hope that I shall not be asked by the House to give any definite account of such measures as we are able to take. If I were to set them high, I might raise false hopes; if I set them low, I might cause undue despondency and alarm; if I stated exactly what they were, that would be exactly what the enemy would like to know (Sir Winston Churchill 1940, p. 309).

Introduction

"Trade is war." So bluntly stated an Australian agricultural economist after returning from a stint at OECD in Paris (Young). Commercial policy has always been a form of strategic weapon. Thomas Jefferson, discussing relations with the Indian tribes in 1808, remarked that "Commerce is the great engine by which we are to coerce them, and not war." A primary difference between the pre- and post-nuclear age is the reduced appeal of force as a means of achieving economic advantage. Because modern tactical weapons make armed engagements riskier and more expensive, Jefferson's dictum has new appeal: the imperial ambitions of nations are pursued through economic trade policy. What could be accomplished in the 1930s and 40s by lethal force is now pursued through economic expansionism.

Trade strategy is thus defined, like warfare, primarily by national interest, and involves threat, counter-threat, subterfuge and retaliation.

While the rhetoric of trade may lay claim to higher principles, such as "free trade," "self-sufficiency," or "fair trade," thinking of these principles as calls to battle, rather than as real objectives, gives a more accurate impression of trade diplomacy. This paper will adopt such a perspective (see also Runge, 1988).

Churchill's difficulty in making full and accurate statements about strategic interests to the House of Commons carries over into the problems of U.S. negotiators' relations with Congress. If announced public aims are set too high for the Uruguay Round, or too low, false hopes or fears may be fostered in Congress and with the affected public. Yet being totally forthcoming would show one's hand before it can be played. This is what necessarily makes trade strategy even within the committees of Congress so much an insider's game. It is also what leads many affected interests to fear that they will be traded away as pawns.

From the negotiators' perspective, we can think of the final year of the Uruguay Round as a war waged on three fronts. The first is in Geneva, where the multilateral trade negotiations (MTN) will be played out, supposedly in December, 1990. This multilateral front, and support for the General Agreement on Tariffs and Trade (GATT) as a mechanism for trade reform, is the most visible of the three.

The second front involves the bilateral relationships that exist with individual countries, played out in national capitals. These bilateral relationships include the on-going tensions between Washington and Brussels, as well as individual discussions with the European Community (EC) and its member states, especially in London, Bonn and Paris. They also include Washington-Tokyo relations, and to a lesser degree, those with

Cairns Group members such as Canada, Australia, Brazil and Argentina. Because these bilateral relations are of longer and more permanent duration than those in GATT (where the Uruguay Round is the eighth since World War II) they are often more informative and influential. It is often a chain of bilateral deals which forms the basis for a multilateral one in GATT.

Thirdly, and perhaps most importantly, is the relationship with Congress and affected interest groups. Along this home front is to be found the rear guard of trade negotiation and the political supply lines which give negotiating authority to the GATT negotiators themselves. Two aspects of this support from home are vital to the Uruguay Round process. First, any multilateral agreement struck under GATT must, by law, be ratified in Congress. Those provisions dealing with agriculture will thus fall in part to the subcommittees and committees on agriculture whose interests are most directly affected by various commodity groups. Second, the timing of the Uruguay Round will be interrelated with Congressional decisions over the 1990 farm bill, making the domestic politics of agriculture impossible to disentangle from trade strategy. This paper will be organized around a discussion of each front in turn: (1) the multilateral negotiations in Geneva; (2) bilateral negotiations; and (3) the home front negotiations with Congress and affected interest groups.

#### Geneva: Multilateral Trade Negotiations

The MTN process in Geneva has wound through nearly three years of discussions as part of the 1986-90 Uruguay Round of the GATT (for a review see Barkema, et al.). In December, 1988, a "mid-term review" meeting in Montreal ended in discord, when the U.S. and EC failed to bridge their

fundamental differences over agriculture. Additional problems in three of the fifteen other negotiating areas: textiles, intellectual property, and safeguards, also prevented a package of framework agreements designed to lay the groundwork for the final two years of the Uruguay Round. However, the midterm review was retrieved in April, 1989, when Geneva negotiations resulted in framework agreements in the problem areas. In agriculture, the U.S./EC differences were papered over with language that called for "substantial progressive reductions in agricultural support and protection . . . resulting in correcting and preventing restrictions and distortions in world agricultural markets." On the U.S. side, which had unsuccessfully called for "elimination" of all trade distorting subsidies in Montreal, the Geneva language was interpreted as a lot of reform in a hurry. On the EC side, it was interpreted as modest reforms over an extended period. The long term goal of the Uruguay Round was reaffirmed as "a fair and market-oriented agricultural trading system."

Despite these negotiating nostrums there were several important departures in the April framework agreement worthy of note (Gifford). Areas that had escaped scrutiny since 1947, through seven previous GATT rounds, were targeted for reform, including the EC's variable levies and other countries' voluntary export restraints. In addition, country-specific policies previously exempted from GATT rules and given special treatment when various countries joined GATT were put on the table for negotiation. These policies include the majority of Swiss agricultural subsidies, Canadian wheat import permits, and the U.S. "Section 22" import quotas. The midterm review also explicitly identified domestic measures as a source of trade distortion, and hence in need of reform, and

developed a detailed work program with milestones, including a first set of (unspecified) long-term commitments to occur in 1991.

In the short term, the package agreed to in Geneva capped the level of domestic and export support and protection at "current" levels, consistent with existing legislation and GATT rules. This does not imply that old legislation cannot be changed and current programs replaced, unilaterally or in coordination with other countries. How countries will roll back or eliminate existing trade or output distortions in 1990 and after was left vague. Overall, the midterm review package provided evidence of progress in the Uruguay Round, but it is far from clear that the good intentions it expressed will be realized in a final 1990 package.

Immediately following the April accord, relatively little was done for several months, as negotiators allowed themselves relief over the fact that a midterm agreement had been reached at all. In the July 10 meeting of the Negotiating Group on Agriculture, however, the U.S. put forward a major part of what is emerging as its final package of proposals (GATT Secretariat). This is the so-called "tariffication" concept, hailed by The Economist as "the most promising way yet suggested to break out of GATT's agricultural thicket." In brief, tariffication means converting all non-tariff import barriers to tariffs, which can then be "bound" and negotiated downward over time. Bound (or fixed) tariffs are the preferred method of import protection under GATT law. The U.S. proposal suggested that the difference between domestic and world prices be used as the basic measure of tariff equivalence. For example, a quota increases domestic prices by reducing the amount of supply available to consumers at the world price. The difference between the world price and the higher domestic price is



equivalent to a tariff of that amount. If the domestic price for the product in question during the reference period is 100, and the world price is 50, the tariff equivalent would be 100 percent =  $[(100-50)/50] \times 100$ .

The tariffication proposal sounds reasonable in the abstract, but is sure to encounter resistance from those sectors most reliant on quotas and other nontariff protection for their livelihood. In the U.S., this includes those protected by dairy, sugar, tobacco and peanut import quotas. There are also a variety of technical problems in calculating tariff equivalents, including the choice of reference prices and base period. The U.S. paper also presages that "as tariffication proceeds, some countries may be tempted to impose new import restrictions in the form of product standards, such as sanitary and phytosanitary restrictions."

Tariffication may be thought of as the import protection side of the U.S. proposal. In addition to this there will be provisions for eventual removal of export subsidies and output distorting domestic policies. At the moment, the U.S. Trade Representative's Office (USTR) and U.S. Department of Agriculture (USDA) are preparing a larger U.S. proposal to GATT for submission in October or November, of which tariffication is one part. While Carla Hills and Clayton Yeutter will lead the negotiations at the highest level, the operating U.S. team will be led by Richard Crowder of USDA and Ambassador Jules Katz of USTR, and represented in Geneva by Ambassador Rufus Yerge (formerly Representative Dan Rostenkowski's chief trade aide). At the staff level will be Joe O'Mara at USDA and Suzanne Early at USTR, with Deputy Chief of Mission Andrew Stoler in Geneva. The new proposal will include explicit treatment of export subsidies, internal subsidies, sanitary and phytosanitary measures, and GATT rules and disciplines.

It may be useful to summarize in graphical form the conception underlying the evolving U.S. proposal (see Runge and Taff). In general, trade-distorting measures may be thought of in terms of their effect on (a) exports, (b) imports and (c) output. Tariff equivalents describe distortions on the import side, and subsidies on the export side. Output distortions resulting from internal policies are derived with respect to their effect on production in domestic markets. In each case, policies may either promote or retard exports, imports, or output.

With respect to exports, a policy has a distorting trade effect if either buyers or sellers in the domestic market face different conditions from those who participate in the cross-border market. Such a definition encompasses not only policies that affect the difference between export and domestic prices, such as export taxes and subsidies, but also non-price protective barriers such as voluntary export restraints. As shown in Figure 1, such policies may distort trade either by artificially promoting exports (as in the case of the Export Enhancement Program) or by artificially retarding them (as in the case of Argentine export taxes or voluntary export restraints). Over the remainder of the Uruguay Round, the attempt will be to define and to set GATT-negotiated limits, for each country, on those policies that are definitely slated for elimination, preferably as soon as possible ("Red Light" policies); those that may remain in place in the short-run, but are to be modified and reformed during a transition phase ("Yellow Light" policies); and those that are sufficiently non-distorting to remain in place indefinitely ("Green Light" policies).

Figure 1

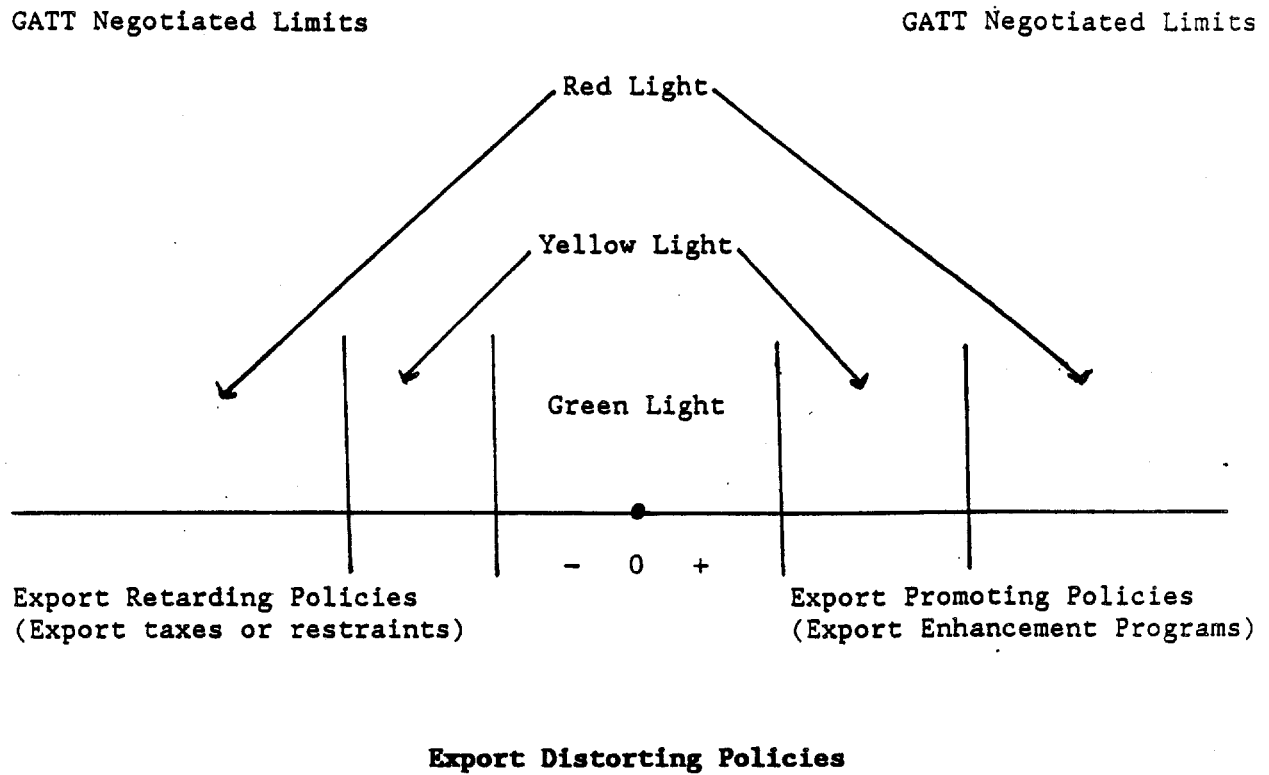


Figure 2

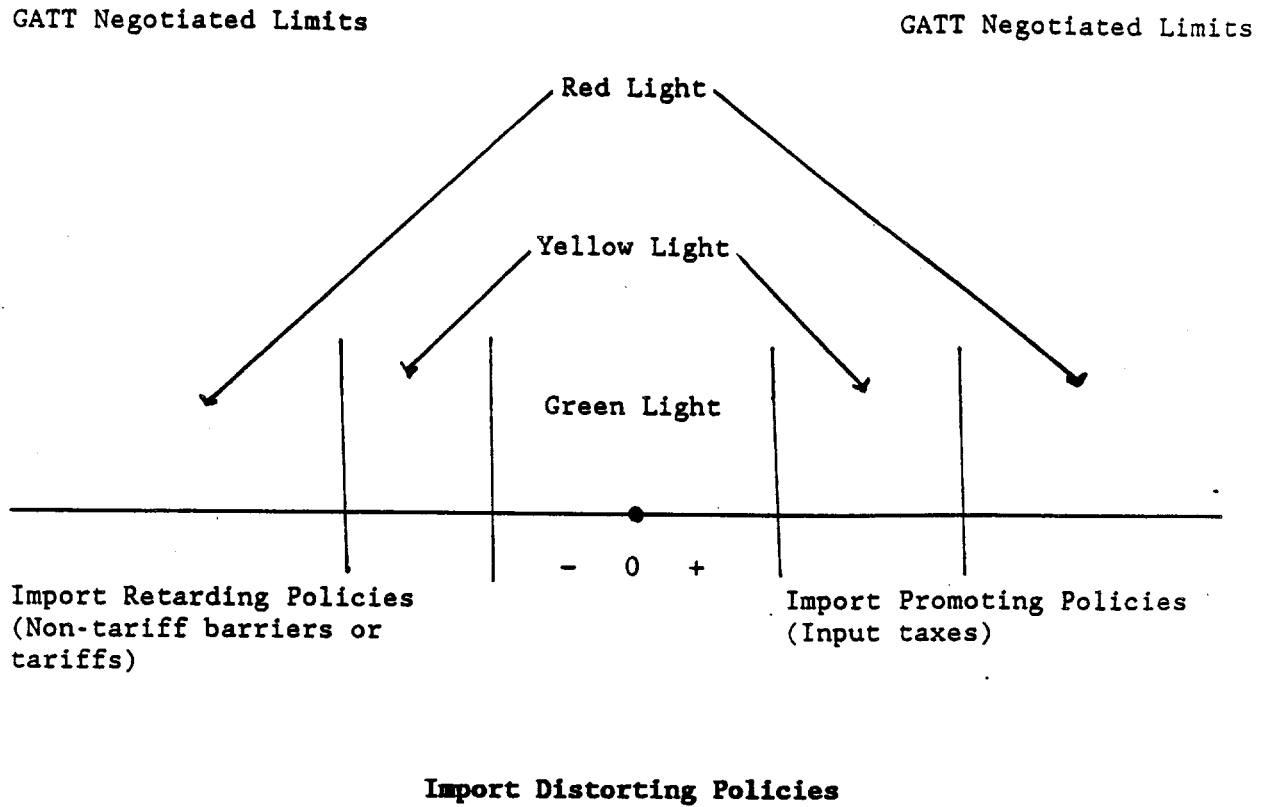
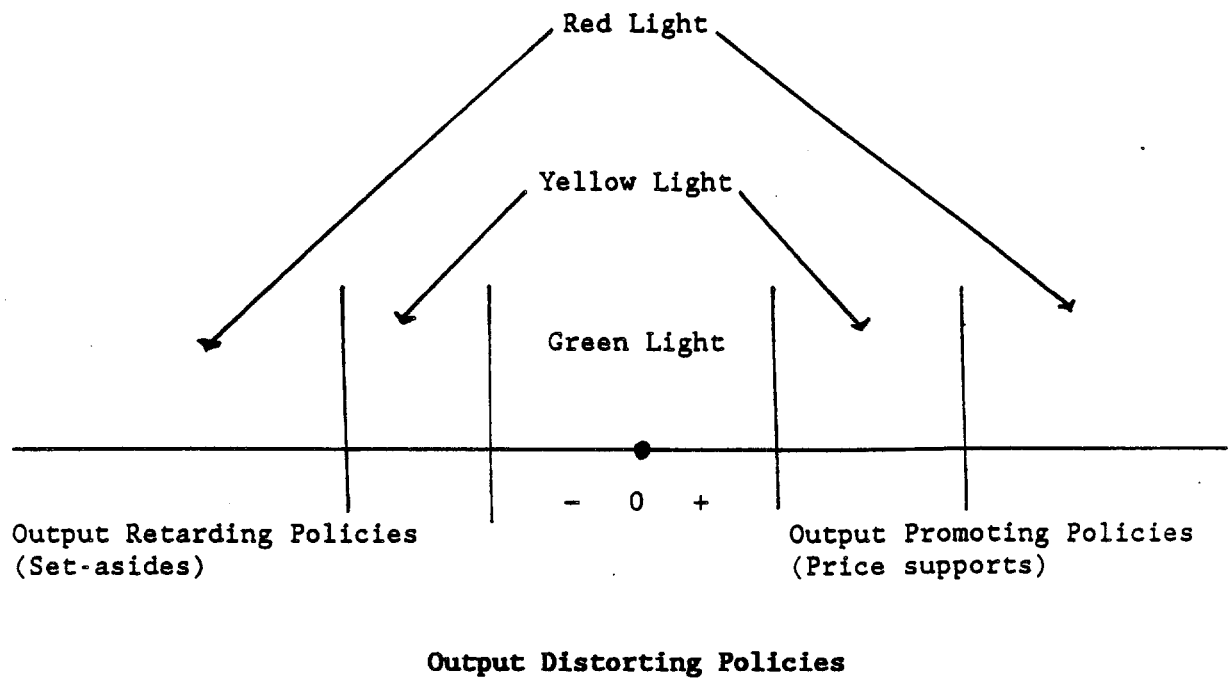


Figure 3



Similarly with respect to imports, a policy has a distorting trade effect if either buyers or sellers in the domestic market face different conditions from those who participate in the cross-border market. As shown in Figure 2, policies that retard imports, such as quotas, explicit tariffs, or health, safety and other sanitary or phytosanitary restrictions, are one side of such distortions. On the other side (less frequently mentioned) are policies that artificially promote imports. An example might be environmental regulations on fruit and vegetable production which prohibit the use of certain cost-saving chemicals in the U.S., leading to incentives to import foreign fruit and vegetables which employ such practices. Because it is quickly realized by domestic growers that such regulations have this effect, calls for import protection through health and safety standards applied equally to foreign produce are quickly heard, converting the regulations from import-promoting to import-retarding policies (see Runge, 1990). In principle, either type of distortion can be expressed as a tariff equivalent, with import promoting policies defined as a negative tariff. Once again, the issue is which policies are determined to be definitely out-of-bounds ("Red Light"), which are undesirable and to be phased out over time ("Yellow Light") and which are acceptable ("Green Light").

Finally are those policies that have an effect on domestic production. As shown in Figure 3, such policies may be negative, such as U.S. and European set-aside programs that pay farmers not to produce; or they may be positive, such as price supports tied to specific crop yields and acres of production. The goal of U.S. domestic agricultural policy in the Bush administration is generally to eliminate policies that are most distortive

of production decisions ("Red Light" policies), including large set-asides and high price supports, and to phase out ("Yellow Light" policies) those that have tended to distort production over time, such as crop-specific acreage bases. What remains ("Green Light" policies) will be programs in which farmers are relatively free to plant whatever crops are most in market demand, with support paid not to specific crops, but on the basis of some type of income criteria.

Overall, progress in the present GATT negotiations can be defined as an agreement to eliminate a specific set of "Red Light" policies in each realm (exports, imports, and output) with a well-defined timetable, and to designate a set of "Yellow Light" policies for discussion in subsequent years. It seems inevitable (to this author) that successful negotiations will ultimately involve agreements to end specific policies, and that such political decisions cannot be finessed by an agreement simply to achieve an aggregate level of support or level of tariff or subsidy. This is the route sometimes suggested by advocates of a single aggregate measure, such as the Producer Subsidy Equivalent (PSE). As Hertel (1989a, b) has recently shown, a given reduction in the aggregate level of support can be achieved with a myriad of different options, many of which have extremely different effects on exports, imports and output. His analysis shows that aggregate measures, because they abstract from this complexity, "underidentify" the problem, and thus do not provide sufficient discipline to achieve longlasting reform.

Before turning to the bilateral and home fronts, let me touch on the relationship between agriculture and several other key areas of the Uruguay Round negotiations. While publicly stating that all fifteen areas are

crucial, the tactical importance attached to some is more important than others. This is sufficiently well-known to the negotiators themselves that it does seem seditious to state them (the "enemy", in other words, already knows which battles will be key). Agriculture, throughout the Uruguay Round, has been crucial, and remains so. A minimum of results must be achieved in agriculture for the U.S. trade strategy to be called a success. Some type of framework agreement in Services is also vital, largely due to the substantial interests of the American financial community. The remaining three areas of vital importance are Trade-Related Investment Measures (TRIMS); Trade in Intellectual Property (TRIPS); and the negotiations on Subsidies. It is beyond the scope of this paper to discuss these areas, each of which would require treatments of similar length.

#### The Bilateral Front

Despite the emphasis on multilateral negotiations, a large share of negotiating gets done in capitals. Several examples are illustrative of the importance of this bilateral front. In agriculture, an important issue with Europe has been the continuing dispute over beef hormones. On January 1, 1989, the European Community announced a ban on all beef imports from the United States containing hormones used to help increase cattle growth. Citing health risks, the EC action touched off a cycle of retaliation that has affected the world trading system (Bredahl). This apparently isolated example of health regulations acting as trade barriers is part of an emerging pattern of environmental and health issues with major consequences for world trade. The larger significance of the hormones dispute relates to the growing role of non-tariff import barriers, especially justified on health, safety and environmental grounds. As noted above, the temptation



to use such sanitary and phytosanitary restrictions is increasing, for a variety of reasons.

In the high income countries of Europe and North America, health, safety and environmental regulations are especially attractive candidates for use as non-tariff barriers. They are part of a larger problem: environmental and health risks are increasingly traded among nations along with goods and services. While increasing emphasis is given to the growing role of services trade, comparatively little has been directed to risks which are the opposite of services: environmental and health disservices traded across national borders. This problem arises directly from the transfer of technology, and will increasingly affect international investment flows, product liability, trade and development, and the relative competitiveness of U.S. business (Runge, 1990).

The emergence of a two-tiered international structure of environmental regulation results from increasingly stringent rules and regulations and a rising concern with environmental quality and human health among wealthy nations. In most developing countries, however, rapid economic growth remains the primary focus of concern. This creates incentives to export restricted industrial materials--or whole production processes--from North to South. A kind of "environmental arbitrage" results, in which profits are gained by exploiting the differential in regulations. In the United States, for example, the Federal Insecticide, Fungicide, and Rodenticide Act (FIFRA), the Safe Drinking Water Act (SDWA) and the 1990 Farm Bill are all likely to be amended in ways that effectively constrain chemical and land use choices. These are but several examples which may lead multinational firms to expand in markets where regulatory oversight is less constraining.

This environmental arbitrage results from conscious policy choices that reveal differences in the value attached to environmental quality by rich and poor countries. As these paths of institutional innovation increasingly diverge, so will the differential impact of environmental constraints on businesses in Europe, North America and, say, Argentina and Brazil. The competitiveness implications of these trends are not lost on developed country firms. They have been quick to see the trade relevance of environmental and health standards in limiting access both to developing country competition and other developed countries. Growing consumer concerns with health and the environment create a natural (and much larger) constituency for nontariff barriers to trade. It is doubtful, for example, that beef-offal merchants in the European Community could have blocked competitive U.S. imports solely in the name of superior French or German beef kidneys. But the hormones question created a large, vocal, and committed constituency for denying U.S. access to this market. These distortions threaten more liberal international trade in ways that are damaging to both developed and developing country interests, yet are not widely appreciated.

The beef hormones dispute, while a relatively minor bilateral dispute in terms of total trade value (\$100 million annually), thus illustrates the importance of bilateral trade diplomacy in conditioning multilateral trade issues. While attempts are made to keep them separate, the bilateral and multilateral fronts of the trade war nonetheless relate to one another, if for no other reason than because they both draw down on the fighting strength of U.S. negotiators.

A second current example concerns the U.S.-Canada Free Trade Agreement (FTA) concluded in 1988. This bilateral accord, heralded as a triumph for trade liberalization, nonetheless raises questions in many capitals over the possible evolution of a North American trading bloc, which might, together with a unified Europe after 1992, end up destabilizing world trade. In his 40<sup>th</sup> Anniversary speech to the GATT contracting parties in Geneva, former Federal Reserve Chairman Paul Volcker warned of just such an eventuality. Because Canada is a member of the Cairns group, the Ottawa/Washington cable traffic inevitably causes FTA issues to be checked against GATT strategy to coordinate the two fronts. In agriculture, much of the FTA language refers specifically to the need for such coordination.

A third bilateral relationship of key importance is with Tokyo. The bilateral agreement struck between the U.S. and Japan on access to Japanese markets for beef in mid-1988, for example, provided a recipe for the 1989 U.S. tariffication proposal to GATT. The deal with Tokyo first determined that quotas and other non-tariff barriers to trade were equivalent to a tariff of 96 percent. It was then agreed to phase out the quotas and other non-tariff measures and to replace them with a tariff of 70 percent in 1991. Finally, tariff cuts to 60 percent in 1992 and 50 percent in 1993 were scheduled, with further cuts to be negotiated as part of the multilateral process.

These three examples of bilateral relations -- with the EC, Canada, and Japan -- illustrate the significance of the second front of trade warfare. Trade policy analysts who focus only on the multilateral front, and neglect the bilateral role, fail to see that both are crucial to victory. There is yet a third front, however, of greater importance even

than these two, because it involves the political supply lines of trade negotiation.

#### The Home Front: Relations with Congress and Interest Groups

The capacity successfully to resolve trade negotiations as complex and overriding as the GATT talks depends crucially on effective liaison with Congress and affected interest groups. In agriculture, there will clearly be winners and losers from the Uruguay Round, although in my view the winners will substantially outnumber the losers. Win or lose, no one who farms or is affected by farming wants to feel that a democratically elected government can make major changes in policy without consulting those most seriously affected by these changes. Failing to consult with such groups is political folly in any event, as administration after administration has learned. When Woodrow Wilson went off to Europe to create a League of Nations designed to end all wars, he failed to protect these political supply lines, and was dumfounded when Congress failed to ratify the treaty. His actions contributed to an isolationist response that helped to bring on World War II.

There are two elements of successful trade strategy on the home front, in my view. The first is to involve directly the members of Congress whose committees bear responsibility for trade matters, so that they develop a feel for what negotiators cryptically refer to as the "modalities" of this process. Earlier this year, House Agriculture Committee Chairman "Kika" de la Garza left for Geneva in a highly agitated state, worried that "the farm bill was being written in Switzerland." The trip turned out well, and helped to allay his fears. Other key members of Congress, including Senator Patrick Leahy, Chairman of the Senate Agriculture and Forestry

Committee; Dan Rostenkowski, Chairman of House Ways and Means; and Sam Gibbons, chairman of the Trade Subcommittee of Ways and Means, have all been briefed in Geneva on the process.

Beyond the members of Congress, and perhaps even more important, stand the interest groups that exert enormous influence over Congressional decision-making (Rapp). In agriculture, these include the commodity groups and general farm organizations, as well as the agribusiness sector. At USTR, an elaborate network of policy advisory councils, composed of thousands of representatives of U.S. business, labor, and farmers, meets regularly with negotiators to provide input into the process. The highest level of this pyramid of advisory committees is the President's Advisory Committee on Trade Negotiations (ACTN), a general advisory board on which agriculture is prominently represented. Members have included the head of the American Farm Bureau and the California almond growers, among others.

Despite these formal advisory groups, much more must be done outside of Washington to inform (and to be informed) by farm interest groups as the final year of the Uruguay Round commences. This is especially significant in light of the simultaneity of the Farm Bill and GATT processes (Drabenscott, et al.). In my view there are two tactical concerns that will dominate the home front. The first is the likely development of a large "war chest" of threatened export subsidies, perhaps in the form of "marketing loans across board," if the GATT talks fail. This is what nuclear strategists refer to as a "credible threat," one form of which is MAD, for "mutually assured destruction". The problem, of course, is that to work, the threat must be credible; but to be credible, it must be disastrous for all concerned. Despite these risks, I expect to see some such threat emerge from the 1990 farm bill process.

The second tactical issue on the home front concerns what I would call weak points in the domestic line. These weak points are defined precisely around commodities heavily protected from foreign competition by U.S. law, and thus standing to lose the most from trade liberalization.

Uncoincidentally, these are the commodities that have the most highly developed lobbying skills in Congress. Examples include sugar, some parts of the dairy industry (especially outside the Midwest, in California and Florida), and other, smaller commodities like peanuts. Despite the fact that the beneficiaries of these programs are few (10,000 sugar producers receive \$1.5 billion annually, according to one recent estimate), they happen to be located in places like Kika de la Garza's district in Texas, and in the Red River Valley of Minnesota (Mehra).

Weak points in a line, in my view, should not be exposed to undue fire, or the entire tide of battle may be turned. I thus am inclined to suggest an aggressive liberalization thrust at our strongest points (feed grains, oilseeds), saving weaker commodities for subsequent treatment. While some argue that such an approach is "inconsistent," it is far from clear that consistency is the path to reform, anymore than an effective assault requires uniform pressure along all points in the line.

### Conclusion

In conclusion, I have described three fronts of the battle for trade liberalization: the multilateral, bilateral and home fronts. Each is vital to the process of trade liberalization, and each will require its own approaches. Yet all must be planned and executed in a coordinated fashion. Little wonder that trade liberalization comes slowly. But a war is not won in a day.

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