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AGRICULTURE IN THE URUGUAY ROUND:

A PERSPECTIVE FROM THE POLITICAL ECONOMY OF PROTECTIONISM

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1. INTRODUCTION

Agricultural trade issues have a long and somewhat inglorious history within the General Agreement on Tariffs and Trade (GATT). During the last decade the conditions under which agricultural trade has taken place have increased international tensions. Over the same period the economic costs associated with national agricultural policies have escalated. As the growth of agricultural production has tended to outstrip that of consumption, trade flows have become more distorted through the use of export subsidies and increasingly restrictive import arrangements. Moreover, trade in agricultural products has become subject to greater politically-induced uncertainty.

International discussions to attempt to solve this hitherto intractable problem took place at the OECD Ministerial Meeting of 1982, at the Tokyo Economic Summit of the G-7 group of countries in 1986 and culminated in the Punta del Este Declaration of the same year which established the Uruguay Round of multilateral trade negotiations in the GATT. Included in that Declaration was the following statement dealing with agriculture. "Negotiations shall aim to achieve greater liberalization of trade in agriculture and bring all measures affecting import access and export competition under strengthened and more operationally effective GATT rules and disciplines..." (GATT 1986).¹ This aim was to be achieved by: a reduction of import barriers; an improvement in the competitive environment through reductions in the use of "all direct and indirect subsidies and other measures affecting directly or indirectly agricultural trade ..." (GATT 1986); and minimising the effects of sanitary and phytosanitary regulations. Implicit in the second of these steps was an acceptance, for the first time, that domestic agricultural policies were to be subjected to negotiation. This was an important break

¹ See also Miller (1986).

with tradition. In earlier negotiations national sovereignty on domestic agricultural policy had taken precedence over international obligations and the external effects of these policies. In particular, the size of income transfers to farmers was regarded exclusively as a national matter regardless of the impact on foreign countries.

During 1987 and 1988 certain of the Contracting Parties tabled proposals to initiate negotiations to give effect to the aims of the Declaration. Five were submitted and in essence they were as follows (Makinen 1990, Josling *et al* 1990). From the United States the proposal was to eliminate all trade barriers over a ten-year period, to remove agricultural subsidies that were coupled with production levels, and to use an aggregate measure of support (AMS) for monitoring purposes.² The European Community (EC) proposed short-term action to stabilise markets and to reduce further imbalances between commodity sectors, and longer-term action to cut support over an agreed time period using an AMS to monitor progress. The position adopted by the Cairns Group had three elements: an immediate freeze on trade distorting measures; reductions in support levels over a ten-year period towards some agreed target level using an AMS; and over the longer term a strengthening of the rules and disciplines of GATT together with a move towards transparent, tariff devices to control imports. The proposals tabled by the Nordic countries and Japan contained similar but not identical elements. The Montreal mid-term review in December 1988 foundered on the impasse over the agricultural negotiations but some progress was made in Geneva in April 1989. Subsequently, the US proposed that all protective instruments be converted to tariffs, which would be bound and then reduced over time through negotiation.

The content of these proposals indicate that the major countries had accepted, at least in principle and to varying degrees, that the reform of their respective national agricultural policies was crucial to the development of an international trading system which would bring about the benefits predicted by neoclassical trade theory. In particular, the new conventional wisdom was that the social problems of the farm sector would be separated from the economic aspects through the use of decoupled and targeted

² Much of the empirical work on the economy-wide benefits from agricultural trade liberalisation have been conducted in OECD (see OECD 1990). That organisation was also instrumental in implementing work on an aggregate measure of support using the formulation developed by Josling (see FAO 1973).

income support.³ Hence, market forces would be allowed to work in a way consistent with comparative advantage. The practical realities of the negotiating process, together with reluctance on the part of the EC and Japan to embrace totally this neoclassical economic position, have so far prevented the new era from dawning. For example, there has been a disagreement between the US and the Cairns Groups on the one hand and the EC and Japan on the other over the size of the reductions in support levels and export subsidies, and the time scale over which these reductions should be implemented. More fundamentally, however, there are basic differences in the economic principles which it is believed should apply to the agricultural sector and its place in an industrial society.

2. A SKETCH OF THE POLITICAL ECONOMY OF PROTECTIONISM

The intellectual justification behind the trade proposals outlined is that of the traditional trade model of commercial policy. There are two features of this model which are important to note: first, free trade is the optimal policy, subject to some qualifications connected with market failures; and second, government is viewed as a passive planner implementing recommendations which maximise social welfare subject to the pursuit of some non-economic objectives. In this framework government is exogenous to the model in which economic efficiency is the goal. By contrast, the political economy approach treats policy intervention as endogenous. "Policy is seen as an outcome of the interaction of rational policy-makers and trade-sensitive economic groups" (Moore 1990, p 143). The objectives of intervention and the choice of policy instrument are explained within the model. Another difference between the traditional and political economy approaches is that while the former is normative, the latter is descriptive. It makes no judgements about the desirability or otherwise of the actions of trade-sensitive groups who lobby government in order to influence policy outcomes.

Different sub-models provide different explanations of reality and they can be placed in one of two alternative categories. One group has been referred to as the "social concerns", "social insurance" or "self-willed government" group: the other as the "self-interest" or "clearinghouse government" group. In the former, government is viewed as providing social justice in order to prevent some groups in society, e.g. workers in declining industries, from suffering substantial income losses, or to counteract the effects of international risk on risk averse groups. The basic idea is

³ For details of the decoupling proposal, see Miner and Hathaway (1988).

captured in Corden's conservative social welfare function. Such concerns do not enter into the neoclassical model, being assumed away through perfect factor mobility and flexible prices.⁴ In the second group of models economics and politics are combined to introduce the rational self-interest of policy makers.⁵ Politicians are assumed to choose trade policies in such a way as to maximise political support and re-election.

The degree of political support is also dependent on the choice of policy instrument to achieve the policy objective. In a neoclassical world it is well known that price and quantity border instruments are equivalent in terms of their effects on price, quantities and, under some circumstances, the distribution of welfare effects. However, in the presence of imperfect competition, market growth, uncertainty and imperfect information, import quotas and various forms of border price protection are no longer equivalent. The rational choice of instrument does not rest only on calculating the size of the deadweight loss. Issues such as transparency become important. If the losers from protection cannot easily identify that they are losing, they will not exert lobby pressure. Consumers and taxpayers, who are the groups in society who usually bear the costs of protectionism, are assumed to be in a position of 'rational ignorance', i.e. they have no incentive to incur the costs of being informed on issues over which they as individuals have very little influence.⁶ However, it is in the self-interest of producer groups in the import-competing sectors whose income is dependent on the provision of protection to be well informed, to lobby for protection or to lobby against its removal, and to lobby for particular forms of protection.⁷

⁴ Perhaps as agricultural economists we should make more use of the specific factors model of international trade and recognise the importance of short-run income losses to immobile factors in agriculture. In addition more attention should be paid to the adjustment costs of moving from one trade position to another (Milner 1985).

⁵ In some developments the political system is modelled as a direct democracy, in others as a representative democracy, while in others the bureaucratic/administrative process is also included.

⁶ The work of the BAE in the early 1980s could be interpreted as an attempt to dispel this ignorance through the free provision to EC taxpayers, food consumers and the manufacturing sector of the costs incurred from allowing the Common Agricultural Policy to continue in its then form.

⁷ In addition to the transparency explanation for the choice of instrument, uncertainty or international price risk will also influence the form that protection takes. It can be

In comparing the social insurance and self-interest explanations of trade policy, some economists have rejected the former because in part it is based on market-failure arguments to justify government intervention. It is argued that market failure is not a convincing reason, given the problem of government failure, i.e. with the same information as private agents, governments can do no better than the *laissez-faire* outcome and, therefore, there is no case for intervention.⁸ If the social insurance model were appropriate and if international price risk were a significant source of uncertainty, then there should exist inter-governmental agreements to pool that risk.⁹ Yet the dominant feature of international trade is one of inter-governmental conflict. This is consistent only with the self-interest model, a model in which income distribution is the main concern. However, the social insurance explanation also rests on altruism as a motivation for policy intervention and this basis is more difficult to dismiss analytically.

In agricultural trade it is possible to find a reason other than market failure to support a social insurance explanation of government intervention. It is the more nebulous one of the 'special' characteristics of the agricultural sector. Whilst some economists tend to dismiss or to ignore such non-economic matters in their advocacy for a free trade regime, in some countries, e.g. Japan and parts of Europe, such characteristics are widely regarded as important. These features include the role that the sector plays in retaining people and economic activity in the countryside, its ability to provide food security and its slow pace of structural adjustment. A general community-wide acceptance of these special features of the sector, rational ignorance on the part of

shown that risk averse producers will rank an import quota ahead of a specific tariff and ahead of an *ad valorem* tariff. Consumer groups would rank them in the reverse order but these groups usually do not engage in lobbying. Hence the political choice is likely to be for the quota, inefficient though it may be (see Lloyd and Falvey 1986). The self-interest approach can also explain why voluntary export restraints are popular, namely, because they avoid the use of instruments which are banned under the rules of GATT, they circumvent bound tariff rates and they allow a reduction in bilateral tensions caused by protectionism (see Hillman 1989b).

⁸ For a detailed analysis of the role of moral hazard, adverse selection and unobservable outcomes in determining trade policy, see Dixit (1990) and for a more general discussion see Hillman (1989a) and (1989b).

⁹ There have been instances of such schemes, e.g. in the international wheat, sugar, coffee, cocoa and tin markets, but most have failed for a variety of complex reasons.

taxpayers and consumers, together with the lobby pressure exerted by farm groups, combine to provide rational politicians with the political incentive required to maintain otherwise irrational policies.¹⁰ Therefore, the social insurance and the self-interest models should be regarded, at least in the agricultural context, as complementary explanations of observed policy intervention. Neither on its own is sufficient.

3. AN INTERPRETATION OF THE CURRENT IMPASSE

It is apparent from the way in which the trade negotiations for agriculture have progressed that there are basic differences between those countries which would seem to have a comparative advantage in agriculture and those which do not. It is in the economic self-interest of the Cairns Group and the United States to push for agricultural trade liberalisation to the greatest extent and at the greatest rate possible. The groups in their societies that have considerable lobby power are the producer groups which, in general, will gain from freer trade and expanded market access.¹¹ Similarly, in Japan and the European Community it is the politically-influential producer groups which will lose from liberalisation and, at least in the case of the EC, they are inhibiting progress in the negotiations.

Within the GATT framework there is an asymmetry, not recognised in trade theory, that domestic producers have property rights to domestic markets.¹² Granting foreigners access to a domestic market requires a concession on their part, namely, the exchange of rights of access, and should such an exchange subsequently cause injury to the domestic

¹⁰ Perhaps the following two quotes, albeit from only one of the major players in the current agricultural trade conflict, will illustrate the point: "My God, those food prices! They are such a minor concern" (Mansholt 1972); and "What is a free market? What we want is an orderly market and prices that are not so bad. For this, you will have to have intervention, you will have to have stockpiling. You will have food security ... In Europe, the feeling of rural worth will remain ... people are ready to keep farmers on the land. Consumers are now paying. They can afford it. Why do we need to change our policy?" (Souchon 1991). (Note: Mansholt was the first Commissioner for Agriculture in the EC and Souchon is currently a member of COPA).

¹¹ However, within each of these countries there are specific products which would be imported under freer trade and producers of such products will lose unless compensated.

¹² For a discussion of this point, see Baldwin (1978), Hillman (1989a) and Krueger (1990).

sector, the safeguards rule (Article XIX) may be used to control imports. Therefore, superficially at least, it would be possible to make progress on agriculture through the use of such concessions on market access. However, to placate domestic farmer groups would require some commitment to transfer income to them from the domestic gainers after liberalisation occurs. Since such domestic transfers usually do not take place, neither will trade liberalisation in the absence of determination on the part of the political process to resist the lobby pressure for continued income protection.

To understand why that determination has so far been lacking in the EC's position on agricultural trade liberalisation, it is necessary to note specific features of the agricultural policy-making process in the EC.¹³ First, certain of the major economic powers within the EC, namely, France, Germany and Italy, have a long history of pursuing protectionist agricultural policies (Tracy 1989). As a consequence, they have well-established national farmer lobby groups. Second, these national lobby groups influence decisions taken by the Community-level farmers' organisation (COPA) which is part of the formal consultative process in agricultural policy making of the Common Agricultural Policy (CAP). Third, whilst the Commission of the European Communities takes a Community-wide view in making proposals for changes in the CAP, it is the nationally-orientated Ministers of Agriculture in their role as members of the Council of Ministers who make the decisions. Fourthly, given the veto power (until recently) of a Minister, policy proposals which are not in a member country's national interest will not be implemented. This provision has been crucial when linked with the domestic political structure and the influence of small rural groups in the coalitions which dominate German governments. Moreover, the same veto mechanism has prevented countries such as the UK and the Netherlands from being successful in arguing for a reduction in internal EC support levels. And fifth, the French have a set of non-economic objectives for agriculture which severely constrain any moves towards reduced protectionism. These include maintaining small farmers in remote and poor farming regions, and the provision of an alternative source of food aid to that provided by the US.

It should be apparent that in such an institutional structure, it would be most unlikely for the advocacy of traditional, normative economic analysis to succeed in bringing about

¹³ For greater detail, see Harris *et al* (1983, ch. 2) and Marsh and Swanney (1980, ch. 2).

the changes in international trade which are sought. Indeed, the attitude appears to prevail in Europe that the Community is rich enough to be able to afford the efficiency losses incurred by the CAP.

3. CONCLUSIONS

During the 1980s it became obvious that international trade in agricultural products was becoming increasingly chaotic. Tensions between otherwise friendly nations were rising and the domestic costs of agricultural policy intervention were becoming, to a greater extent, a function of policy settings in other countries. The tabling of the agricultural proposals as part of the Uruguay Round was an attempt to move domestic agricultural policies and trade policies towards more *laissez-faire* and free trade positions. The economic arguments on their own appear to economists to be overwhelming.

Yet at the present time the entire negotiating process is stalled because of lack of progress in the Agriculture Negotiating Group. The EC is identified as the major culprit preventing a successful outcome to the Round. The EC's agricultural policy process is highly politicised and is dominated by the interests of farmers in France and Germany in particular. Consequently, to understand the EC's position, it is necessary to take cognizance of the agro-political complex within Europe and to find ways of helping it to make compatible its own and the international community's objectives by means which are much less damaging to international trade and international relations.

In order to do this it is important to accept the objectives of the CAP, to remind the EC of its obligations under Article 110 of the Treaty of Rome, but also to find politically acceptable policy instruments which internalise to a much greater extent than hitherto the impact of its agricultural policy. The search for such instruments will not be easy. However, in the longer run it will provide a better basis for negotiation than a strictly economic rationalist approach on its own.

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