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## Opening Global Markets for Agriculture: The Next WTO Round

**Daniel A. Sumner**

More open international markets benefit the economy as a whole, as well as most U.S. agricultural producers. The Uruguay Round Agreement laid out a useful framework. Specifically addressed here is why the key to further liberalizing agricultural trade is reduction of tariffs as comprehensively and rapidly as politics will allow. Other issues such as export subsidies, tariff-rate quota quantities, and developing-country relationships are also important, especially while tariffs are coming down. Internal support rules have much less potential to liberalize trade. Finally, as the December 1999 World Trade Organization ministerial meeting in Seattle demonstrated, delay in the negotiation process threatens liberalization.

**Key Words:** agricultural policy, agricultural trade, commodity trade, tariff-rate quotas, tariffs, trade negotiations, WTO

### Introduction and Motivation

Economists typically support unilateral liberalization, and certainly economists supported the general thrust to open markets that has been a part of multilateral international trade agreements over the past five decades. Here I will spend little time on the goal of more open markets.<sup>1</sup> This article focuses on using the World Trade Organization (WTO) and the upcoming round of trade negotiations to move toward that goal. Josling (1997) presents views that are generally consistent with the thrust of the arguments here.

The GATT, and more recently the WTO, were formed explicitly to open markets and facilitate trade. But even market-opening trade negotiation agreements seem to use the mercantilist language implying that the goal of trade is to stimulate exports, while allowing imports is called a “concession.” Yet, there is no practical economic

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Daniel Sumner is Frank H. Buck, Jr., Professor, Department of Agricultural and Resource Economics, University of California, Davis, and Director, University of California Agricultural Issues Center. This paper was presented at the National Symposium on the Future of American Agriculture, August 25–27, 1999, Athens, Georgia.

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<sup>1</sup>Readers may instead see Adam Smith’s 1776 treatise, or for more arguments and evidence specific to agriculture, see Johnson (1950, 1991), Gardner (pp. 27–40 in this issue), or Sumner (1995).

reason for a nation to favor exports over imports. Access to imports is a strong and proven stimulus of economic success. Unrestricted trade almost always enhances national wealth and well-being. This is not only a mathematical theorem under certain specific assumptions, it is also backed up by several centuries of evidence and by some pretty straightforward common sense. Allowing buyers access to the best products on the most favorable terms directly provides benefits to consumers and lowers input costs to producers. While I do not have the space needed to build the argument and evidence, the basic proposition that trade is good for agriculture, and for the economy generally, underlies the arguments presented here—and so it is important to state this principle up front.

In agriculture it is commonplace for those nations that tend to export a commodity to push for more open markets for that commodity, while importing nations with domestic industries producing the same commodity tend to resist its liberalization. Trade policy discussions tend to be organized around industries that produce similar outputs rather than around groups of consumers or industries using similar inputs which might be imported. For example, the U.S. Department of Agriculture's (USDA's) Agriculture Trade Advisory committees are examples of this tendency, although these groups do have a few representatives from processing industries that use imports.

The United States is a natural agricultural exporter of most major commodities. Some have assumed this is the reason that open agricultural trade is positive for the nation. The fact that the United States has comparative advantages in many agricultural commodities implies the special interests of agriculture and the general interests of our whole economy overlap. This article discusses what international trade negotiating positions are in the interest of U.S. agriculture and the U.S. economy more generally. For the most part these are the same.

Finally, when we consider what features of trade agreements are good for agriculture as an industry, we must not neglect the importance of general economic health both in the United States and in other (especially importing) countries. More open markets in general have been good for U.S. agriculture in part because trade is good for the domestic and global economies.

## **Background**

My arguments here must be developed against a background that includes the state of agricultural markets and policies, both within and outside the United States. Let me state my broad assumptions in those areas:

1. Agricultural productivity will continue to improve in the United States and in other countries.
2. Demand for farm goods will rise slowly with population and income growth, and the composition of consumption will continue to evolve toward higher quality.

3. Market prices for most commodities will continue to be variable against a long-term downward trend in real terms. I do not predict specific prices for any specific years; such predictions have a tendency to embarrass the forecaster.
4. In the United States there will continue to be little mandatory land idling, relatively few planting restrictions, and generally low production-enhancing farm subsidy. Recent changes along these lines were reinforced by the 1996 farm legislation (USDA/Economic Research Service, 1996; Young and Westcott, 1996). Note this has not meant smaller outlays or smaller income transfers to farmers.
5. Most of the world is on the same broad policy path as the United States. Australia, New Zealand, Argentina, and a few others are further along on the liberal path; others, such as Japan, Korea, and most of Europe, are lagging. Nonetheless, the general direction of policy reform seems clear.

### **The Uruguay Round as a Starting Point**

The Uruguay Round Agreement (URA) specified a gradual reduction of export subsidies and an increase in market access for agriculture as well as nominal but nonbinding provisions on domestic support programs.<sup>2</sup> Although the rate at which markets open may seem slow, if this rate were simply to continue, substantial market opening would result relatively soon by trade agreement standards. Agricultural tariffs, including the newly created ones, as well as outlays for export subsidies, are all being reduced in rich countries by an average of 6% per year (starting in 1995). At this pace, with no delay and no change in the base period, these agricultural tariffs and export subsidies in developed WTO member countries will be zero after 16 years and eight months from January 1995. Tariffs on certain politically sensitive products in some countries are being reduced at a slower rate of 2.5% per year. But, given that the overall average is pegged at 36%, and that many of the low tariffs have already been eliminated, as the tariff reduction pace continued, even some of the tariffs that are now on the slower track would need to be reduced more quickly.

The substantial liberalization built into the URA is also shown by results of simulation modeling. For example, Cox et al. (2000) show that if the pace of dairy liberalization were simply to follow the URA path until 2005 (i.e., for a total of 10 years of implementation), the result would be about 50% of the market effects attributable to free trade. For poor countries, the elimination of tariffs occurs later—and this is a feature of the URA needing reconsideration. The worst possible negotiating

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<sup>2</sup> For more details on the GATT and the URA for agriculture, good reference sources are Josling, Tangermann, and Warley (1996); Josling et al. (1994); Sharma, Konandreas, and Greenfield (1996); Tangermann et al. (1997); and Sumner and Tangermann (2000).

strategy for those looking to open markets would be to complicate the negotiations by raising new issues and additional demands. The most important policy position of the United States and its allies is to push for continuation of the pace of URA reforms as soon as possible and, if feasible, while other issues are being negotiated. Such a commitment would eliminate the strategy of delay as a tool for protection.

Naturally and unavoidably, there remain many specific concerns about the previous agreement, and particularly about how it has been implemented in various instances. A number of these concerns are dealt with below. In some cases, WTO members may not have lived up to the letter or spirit of the agreement in the implementation process. There are real and legitimate concerns about implementation of access for specific commodities in specific markets, but it is my assessment that they do not reflect fundamental flaws in the URA approach.

### **Tariffs and Related Market-Access Issues**

With the main exception of rice in South Korea, the URA eliminated nontariff barriers for agriculture. Many agricultural tariffs are now zero or very low, but the average rate of agricultural tariffs remains well above that of industrial tariffs. Effective tariff reductions would apply to within-quota as well as to over-quota tariff rates. In some cases, in-quota tariffs and “mark-ups” remain significant; in other cases, over-quota tariffs remain several times higher than required to block virtually all over-quota imports.

It would be easy to skip over issues of tariff cuts in favor of more complex issues that have dominated the news recently, but this would be a mistake. In agriculture, there are numerous important product categories for which tariffs are important sources of trade distortion. If tariff protection were eliminated, many other problems in agricultural trade would be either significantly reduced or exposed to more internal or international pressure. For example, as discussed below, few nations could subsidize exports when they allowed open import access for that product.

There are reasonable arguments to support targeting the highest tariffs for the most reduction. Tariff dispersion creates distortions relative to uniform tariffs. The measure of a tariff is not simply the ad valorem rate or equivalent. One must have additional information to know how much trade it blocks or how much protection it provides. For example, the U.S. tariff on beef is currently a bit below 30%, while the new tariff for Japanese rice is in the range of about 450%. But, given Japan’s current domestic rice policy and production costs, a tariff of even 250% would probably allow a significant import of rice into that country, whereas very little beef would enter the U.S. (or Canada) over a tariff of 25%.

Thus, the case for lowering high tariffs first or most is not that high tariffs necessarily restrict trade most, but rather that they reflect the situations for which production costs are most out of line, and where gains from trade may be greatest. Of course, for the same reason, the most protected industries tend to be those with the most to lose and enough political clout to maintain their protection.

Tariff rates are not the only access topic. When tariffs start from prohibitively high rates, tariff cuts may not increase trade flows much in the short run. Certainly, many of the initial set of tariff cuts implemented over the past five years have had little impact for some particularly important commodities. Dairy stands out in this regard. Unless tariffs are cut dramatically and immediately, new access over the next few years would require expanded quantitative access. In a continuation of the two-pronged approach used in the URA, expanding minimum access as well as current access under tariff-rate quotas (TRQs) would allow economically meaningful trade quantities to be expanded while tariffs are gradually reduced.

We should note that the quota-quantity feature of tariff-rate quotas is a temporary measure which is important only while out-of-quota tariffs remain high. Thus, the reforms associated with TRQs will be applicable only so long as there are significant differences in in-quota and out-of-quota tariffs. Nonetheless, the administration of quotas is important for access during this period (Sumner and Lee, 2000). Also, since the basis for expansion is the base period quantities, expanded TRQ quantities does not necessarily mean that access will increase as a share of the current domestic market.

One concern is that governments may manipulate access to favor certain trading partners or to limit competition with domestic products. The appropriate principle is that access for limited quantities should be allocated across suppliers in a manner mimicking commercial market outcomes. The problem is that the “commercial” outcome remains unobserved, and therefore governments have taken wide latitude in setting quota rules. The challenge is to place the burden of proof on importers by requiring governments to document how their quota allocation procedures do not violate this market test.

The issue of quantitative access is linked directly to the use of state trading enterprises (STEs) for managing agricultural trade. The WTO does not outlaw STEs, and they remain important in many socialist and formerly socialist countries (Ackerman and Dixit, 1999). However, import (and to a lesser degree export) STEs do pose a direct challenge to implementing and enforcing agreements. STEs are government-related organizations that operate, in part, as commercial firms (Ackerman and Dixit). The central problem is separating the government policy measures from the commercial activities. The problem is made more severe when the importing activities of the STE are not transparent. This makes it difficult to demonstrate that import (or export) decisions are not influenced by government policy in ways which violate WTO rules. This problem will diminish when tariffs fall to very low levels, but so long as an arm of government manages trade, it will be difficult to assure trading partners that protectionist considerations do not affect the transactions.

### **Export Measures**

The URA provided for a gradual reduction in the use of explicit export subsidies over the implementation period. A huge literature has evolved around target export

subsidy programs, and for the most part these are seen as reducing welfare in subsidizing countries [e.g., Ackerman, Smith, and Suarez (1995) describe U.S. export subsidy programs, while Alston, Carter, and Smith (1993), and Alston et al. (1997) provide some evaluations]. Remaining agricultural programs are exceptions to the rule that export subsidies are generally forbidden under the GATT/WTO.

Beginning in 1986, the United States argued for elimination of export subsidies, but had to settle for gradual reduction in both the volume subsidized and the value of subsidy. The United States has made relatively little use of export subsidy provisions allowed under the URA. Export subsidies can seem appealing to combat export subsidies of other nations, but the evidence is clear that they generally do little to improve the bottom line for U.S. farmers growing products exported with subsidy. This is why the USDA has not used its authority under U.S. farm law and under the WTO agreement to subsidize wheat exports even in the face of low U.S. domestic prices after 1997.

There are now only a few countries practicing export subsidies, and the European Union (EU) clearly is the dominant user of export subsidies allowed under the URA. Elimination of remaining export subsidy measures would reduce one factor that continues to increase price variability in world markets and frustrate competitors who have reduced reliance on government subsidy programs in general. Elimination of export subsidies would also increase the chances of obtaining access improvements, because one reason countries list for keeping out imports is that world markets are distorted by subsidies.

For the upcoming negotiations, it again seems obvious that the appropriate course is a rapid elimination of export subsidies. The path to elimination of export subsidies that started in 1995 is relatively slow, and will leave subsidies in place for more than a decade. But immediate elimination is likely to be resisted by the EU.<sup>3</sup>

### **Internal Support**

The Uruguay Round Agreement on agriculture devotes more space to internal support than to either of the border measures. The result of all this attention is a text that imposed no serious commitments on any of the largest agricultural traders, and even where the URA forced changes, no significant changes in trade patterns followed. Sumner and Lee (2000) discuss the case of South Korean rice in this regard.

This problem with internal support disciplines was not accidental, nor is it something that can be easily changed by any WTO agreement. The problem is fundamental. Domestic subsidy programs occur with such variety and have such complex effects (many of which have relatively little to do with trade) that it is impossible in practice, if not in theory, to create effective enforceable policy commitments on

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<sup>3</sup> In fact, at the WTO ministerial meeting in Seattle in December 1999, the EU resisted listing elimination of export subsidies as a goal for the next round of negotiations.

internal supports in the context of a multilateral agreement. There are just too many individual policies to discipline each specifically, and the idea of using an index of trade effects of policies has proved chimerical (Sumner and Hallstrom, 1997). Policy indexes that measure trade impacts under changing market conditions are beyond the control of the country making a commitment. Further, aggregation of many policies into a single index tends to ignore their differential trade impacts, and may encourage more trade-distorting policies in preference to less distorting policies. For example, U.S. deficiency payment programs, which probably reduced production and export of grains because of the link between payments and acreage reduction, were not considered “green” and faced some loose restrictions. Recent U.S. payment increases motivated by ex post low commodity prices are likely to be considered fully “trade-distorting,” just as are marketing loan payments that clearly have a production subsidy element.

Internal subsidy reforms have occurred in the U.S. and elsewhere over the past 10 years, but URA internal support commitments were irrelevant to this process. Budget pressure, pressure to reduce regulatory burdens, and desire to increase productivity were the driving forces behind reduction in trade-distorting domestic subsidies in the United States. In some cases, reform of domestic price policy may be influenced by multilateral negotiations, but usually it is pressure from lowered import barriers or export subsidy reductions. For example, in the EU, high domestic prices for grains are possible only because trade barriers limit imports and export subsidies are used for any output in excess of that taken in high-priced domestic markets. If the import barriers and export subsidies were severely limited or eliminated, high domestic market prices simply would not be feasible except at prohibitively high budget costs.

International negotiations and agreements on internal support are not irrelevant; they can be actually harmful to progress in agricultural liberalization. One reason is that they interfere with the operation of other GATT principles and provisions. In general, WTO members may not use policies such as internal subsidies to reduce the effectiveness of lowered import barriers or other trade policy commitment. But, by including text on internal supports in the multilateral agreement, the effectiveness of an appeal to this “nullification and impairment” provision is weakened. Countries may argue that they are complying explicitly with the written agreement when they introduce subsidies which impair border measure concessions. In a sense, previously suspect policies now have a kind of WTO acceptance they did not enjoy before the URA.

One might argue that the problem with the internal support provisions was a failure of the negotiators of the URA, and that problems associated with internal support may be repaired with better modalities. We may have the opportunity to find out, but I argue instead that it is counterproductive to attempt to devise schemes to regulate internal subsidy policy. Diverting attention away from border measures reduces the progress on tariff cuts or direct export subsidies. [See also Tangermann et al. (1997, chapter 2), and Sumner and Hallstrom (1997).]



### **Sanitary and Phytosanitary Regulations and Technical Trade Barriers**

The sanitary and phytosanitary (SPS) provisions of the Uruguay Round Agreement have been used to expand access while simultaneously allowing countries to protect against legitimate plant, animal, and human health risks. There is no question that the WTO should help countries protect themselves, and one advantage of developing international standards is to provide some international security to the SPS regulations a country may adopt.

A number of complex issues remain to be adjudicated in this area, but the basic thrust is that countries may use human health, animal health, or plant health concerns to restrict trade only if they have reasonable scientific backing. In particular, trade in goods can only be restricted if the goods themselves pose a threat that can be documented scientifically. A number of issues have arisen recently related to products such as seeds which have been developed using relatively new scientific procedures or tools. So far, the claim that some consumers or other citizens do not like the process used to develop a product has not been accepted as a legitimate reason to block trade. It is important for agricultural productivity that these issues become settled as soon as possible to avoid undue delays of scientific advances important for global food security.

Every WTO member has occasionally been tempted to use technical rules or import protocols as indirect barriers to protect domestic interests from foreign competition. It is also natural for this tendency to grow as other nontariff barriers are converted to tariffs and tariffs are reduced with implementation of the Uruguay Round Agreement. The SPS agreement was designed to place limits on this abuse of legitimate reasons to regulate market access.

The Uruguay Round SPS Agreement was a remarkable achievement of common sense and practical economics. The agreement stipulated that individual nations could set their own human, animal, and plant health standards and have full liberty to engage in trade measures to assure protection of those standards. However, the only permissible trade measures are ones that actually contribute to the demonstrable protection of health. Thus if trade measures are challenged, WTO members are required to back up their claims with analysis and evidence showing a link from the trade measure to protection of human, animal, or plant health. This can be accomplished by using internationally accepted standards or, where member rules differ from those generally accepted in the international bodies, members are asked to provide their own acceptable scientific evidence. Trade barriers have been allowed based only on characteristics of the product being traded, not on characteristics of the production process.

The application and implementation of the SPS agreement has been as controversial as the concepts are simple. But without such rules, it would be easy for any nation to block access for imports from any other nation by claiming such imports were, for one reason or another, politically unpopular. If no evidence were required to back up technical trade barriers, or if no product differences were required,

national sovereignty would be directly challenged by trade barriers based on preference by citizens of one WTO member over internal regulations in another WTO member country.

For the past several years, WTO observers have been watching settlement of SPS disputes. During this period, a number of technical trade barriers have been removed voluntarily before they were challenged, others have been modified during consultation, and still others have been modified under the direction of WTO panels. However, the real headline dispute over importation of beef from the United States and Canada into the EU has not yet been resolved. EU import restrictions on agricultural goods with some connection to biotech processes, including genetically modified organisms (GMOs), has not yet become a formal WTO case, but the prospects of this dispute are looming in Geneva.

The SPS agreement has weathered the pressure of WTO disputes quite well. Naturally, the agreement does not provide specific guidance on exactly what evidence is sufficient to justify technical trade barriers, but the basic points remain well understood. Member states attempting to base import barriers on vague claims with little or no evidence have lost their dispute cases. Also, it is clear that popular opinion and political pressure have not been acceptable substitutes for empirical evidence about human, animal, or plant health consequences. Those who would like to weaken the WTO and allow members more latitude for blocking market access have been frustrated by the agreement.

The SPS agreement is under considerable pressure in the EU and by anti-trade lobbies in other countries. These forces found themselves unhappy with the agreement shortly after it was signed. Thus they do not seem satisfied to let "case law" proceed to set appropriate specifications for further implementation.

### **Developing-Country Issues**

The idea of special and differential treatment for poor countries has long been a part of the GATT process. In previous negotiations, poor countries have been allowed to delay implementation or use slower phase-in of tariff reductions. As noted above, this approach was applied in the URA as well. But this special treatment actually penalizes poorer countries, and many have adopted more rapid liberalization unilaterally. Real aid to developing countries would include further offers of more access to rich-country markets, not differential allowance to keep their own markets closed. There is no reason to enter the new millennium round by perpetuating the myth that agricultural trade barriers or export subsidies or taxes promote food security or economic development.

One fundamental problem is clear: Many countries, not just poor countries, rightly perceive they have less weight in the WTO. As a practical matter, a WTO member's weight in negotiations is related to its relative size in world trade. The WTO could function quite effectively even if New Zealand were to drop out, but it would be much less useful as an organization without the European Union. Thus individual

small countries have some disadvantage. Poor countries confront the additional problem of a scarcity of expertise in the WTO process, in WTO law, and in adapting domestic regulation to comply with complex agreements. Thus, even if the process and the final agreements were not unfair, they may nevertheless seem inequitable. One lesson from the December 1999 ministerial meeting in Seattle is that the next round of trade negotiations must engage developing nations fully. Technical assistance and other aid from multilateral groups can help the bargaining effectiveness of less-developed countries and make the negotiations more balanced. The WTO and the World Bank have both made considerable efforts in this regard, but more attention is needed.

### **Improving the World Food System and Enhancing the Chance for Reform**

Food security is one of the most commonly stated rationales used to support import protection in agriculture. The argument and evidence for this linkage is weak. Theory and fact suggest that food security is enhanced, not reduced, by open markets. Comparing North Korea to Singapore or Hong Kong dramatically illustrates the tragedy of blocking import access in agriculture. It is hard to treat as credible the claim that maintaining the price of staple food grains at double or triple the world price improves food security. Nonetheless, relatively rich countries from Austria to South Korea have pursued agricultural trade barriers under the guise of food security.

The claim that international markets are “unstable” or “unreliable” does not pass empirical muster in general, but there is a real concern. One problem is that in times of high prices or other problems, governments in exporting nations may impose export taxes or export embargoes. This issue was not addressed in the Uruguay Round. Export restrictions are relatively rare in agriculture, but that does not satisfy the concerns of food importers. Importers have a strong case that the WTO should explicitly and clearly ban the use of export taxes and embargoes in agriculture. Such a provision would help make world food markets more secure.

### **Concluding Remarks**

The upcoming round of trade negotiations in agriculture can build on the foundation established by the URA. For open markets and more liberal trade, the most important step for the next round is to keep the process moving: keep tariffs coming down as rapidly as possible, expand quantitative access in the short run, and apply vigilance to block schemes that circumvent the rules. The strategy of those who want to keep markets closed will be to delay and minimize. Delay will be rewarded with a suspension of annual tariff cuts and market access expansion while the negotiations proceed. With all the abstruse and contentious issues in international trade, it is all too easy to be caught up in the complexities. That would be a mistake.

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