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The Millennium Round of Multinational Trade Negotiations

Andrew Schmitz

The 1999 round of trade talks in Seattle, Washington got off to a rather shaky start; in fact, it may be several years before new trade talks will be held. Many special-interest groups, including environmentalists and labor unions, were successful in scuttling these trade talks. In addition, agriculture's role and position were not clearly stated. This paper deals specifically with key agricultural issues surrounding future progress in trade talks. These comments integrate the central themes covered by the several authors who participated in the session entitled "The Millenium Round of Multilateral Trade Negotiations." My discussion illustrates some of the outstanding issues which must be dealt with before significant progress will be made towards freer trade in agriculture.

Policy Harmonization

What happened to policy harmonization as agreed to under CUSTA and NAFTA? The United States and Canada were supposed to work towards a common agricultural policy; however, this has not happened. In fact, the two countries seem to be moving in opposite directions in the policy arena. The United States passed the 1996 FAIR Act whereby farmers were compensated over seven years for support received under previous farm programs. In addition, in 1999, U.S. farmers received a government cash bailout of over $8 billion. In 2000, it appears that significant payments will once again be made under various relief packages. On the other hand, in Canada supply management remains in place, as it has for quite some time. But for major commodities such as wheat, beef and pork, Canadian subsidies have essentially been eliminated (FAS paper). Key subsidies, including the Crow Rate transportation subsidy, were removed. As of February 2000, it appears that in spite of lobbying by farm groups in Western Canada little government support will be provided to farmers in Western Canada. Evidence surrounding policy harmonization suggests that even when agreements are signed, countries do not necessarily live up to those agreements. Why, then, if further free trade agreements are signed for agriculture should we expect material results?

With the removal of the Crow Rate transportation subsidy in Canada, very few subsidies remain for western Canadian farmers. The removal of the Crow was certainly a victory for tax payers, since the government compensation package paid to producers was much lower than payments made under the Crow rate agreement. Producers did not receive full compensation for the transfer they were receiving under the Crow rate. The removal of the Crow was also a victory for proponents of free trade; however, many argue that even if the Crow had remained in place, it would not have brought a halt to trade talks. They argue further that the removal of the Crow was nothing more than a budgetary decision on the part of the Canadian treasury. With the Crow and other subsidies eliminated, Canada is left to compete against countries, such as the United States, who have reintroduced subsidies. Is this policy harmonization?

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State Trading Enterprises and the WTO

The paper by the Foreign Agricultural Service (FAS) clearly states the American position on freer trade concerning STEs: the United States wants STEs eliminated. Two thorny issues arise. First, the United States has to consider the role played by its own STE: the Commodity Credit Corporation (CCC). At times, the CCC's activities have been significant in international grain marketing (Schmitz, Furtan and Baylis, 1999). In the late 1990s, because of extremely low commodity prices, the CCC again emerged as a major player. Second, despite claims to the contrary, there is no empirical evidence available to suggest that the Canadian Wheat Board—a major STE—is in violation of WTO rules (Schmitz, Furtan and Baylis, 1999).

STEs have to meet certain criteria to be WTO compliant. One important criteria concerns soft price discrimination where export subsidies are involved. STEs can practice hard price discrimination (which doesn't involve subsidies). Generally, when the CWB price discriminates, it practices hard price discrimination, and is therefore WTO compliant. In addition, regardless of the nature of price discrimination, and whether or not the CWB is efficient in marketing, the trade-distorting effects are small indeed. STEs should be judged on the extent to which they are trade distorting, rather than on other criteria that are espoused in trade circles.

Keeping the Borders Open

While there is general agreement that major countries and regions should continue pushing for freer trade, certain apparent contradictions have surfaced. For example, Canada, in its free trade stance, is unwilling to give up supply management. And in the United States, dumping and countervail laws (in addition to farmer subsidies referred to earlier) are in place to protect U.S. producers from foreign competition. Some allege that the United States is arguing for free trade on the one hand, but practicing protectionism on the other. However, these allegations may not be true. For example, consider the countervail and dumping cases leveled by U.S. beef producers against Mexico and Canada.

On October 1st, 1998, the Ranchers-Cattlemen Action Legal Foundation announced that–with the support of the National Farmers Union, more than 20 other state and local organizations, and nearly 8000 individual ranchers—it had filed three petitions in Washington, D.C. with the U.S. government seeking relief from unfair trade practices. If it is true that the United States only preaches free trade but does not practice it, then the countervail and dumping cases against Canada would have been successful. However, the cases were resolved in 1999 in favor of Canada. This decision was certainly a victory for Canadian beef interests, and a victory for U.S. proponents of free trade. As well, the injection of over $8 billion in 1999 into the farm economy in the form of government disaster relief payments is not in violation of the U.S.'s stance on free trade, though it may at first glance appear to be. The bailout is likely to be considered a "green box" policy by WTO rules (see below); that is to say the bailout, under WTO rules, is production and trade neutral.

Agricultural Policy Categories

Agricultural policies have been separated into multiple categories: blue, green, amber, or red, according to their trade distorting impacts. Green box policies are not actionable for countervailing duties or other GATT challenges. Ultimately, green box criteria ensure that policies and programs in the category are production and trade neutral.

According to Agriculture and Agri-Food Canada (1998a and 1998b), there are two types of domestic support policies: those which are subject to reduction commitment and those which are exempt. Exempt policies include green box programs and blue box programs.

Green Box Policies

Two basic criteria apply in Green box policies: (1) Support must be government funded and

(2) the money cannot provide price support. In addition to these criteria, a number of illustrative programs are given: research, inspection, extension and training, marketing and promotion, public stock holding for food security; domestic food aid; and decoupled income support, income insurance and safety net programs, structural adjustment assistance, regional assistance and environmental aids.

Blue Box Policies

Acceptable, but temporary, Blue box policies include program payments received under production limiting programs—based on fixed area and yields, a fixed number of head of livestock, or if they are made on 85 percent or less of base level of production.

Those programs which do not fit these three categories are subject to reduction commitment. For these non-exempt programs, a quantitative measure of the level of intervention is calculated using an Aggregate Measure of Support (AMS). Developed country WTO members are required to reduce their AMS to 80 percent of their 1986–88 levels by 2000.

Amber Box Policies

Amber box policies are trade-distorting domestic support programs that are subject to reduction commitments (such as market price support and input subsidies).

Red Box Policies

Red box policies are prohibited policies. There is no agreement on how to apply the "stop" red light to any domestic policies, so the "red box" has been empty.

During the Uruguay Round of trade negotiations a number of authors attempted to classify domestic support policies based on the degree to which they distort trade; however, certain policies do not fit neatly into the categories (Agriculture and Agri-Food Canada, 1998a and 1998b). For example, according to Agriculture and Agri-Food Canada, it is difficult to assign the Canadian program NISA a precise spot within the green part of the green-red spectrum. The program is not entirely neutral, since additional government contributions can be obtained through additional sales. The U.S. PFC program is also hard to categorize. Concerns surrounding the PFC program stem from the large dollar amounts of the payments, the expectation that production may now be required for a future program, and the recent use of the program to provide additional *ad hoc* transfers to producers. Clearly, E.U. compensatory payments cannot be considered "green" as they now stand, according to an Agriculture and Agri-Food Canada report (1998b), *An Examination of Nearly Green Programs: Case Studies For Canada, The United States and the European Union.*

Although green box programs are more benign than other forms of support, it is clear that large ongoing payments, by their size and permanence, attract and keep resources in agriculture. As the green box becomes a more popular avenue for governments to provide domestic support, the size of the expenditure envelope will expand and the potential distortions will increase accordingly. Moreover, although programs may be designed to be production neutral, they are not always so in practice. Even though a program may be only marginally distorting, large program expenditures may turn a small distortion into a big impact. This raises the need for a cap on total green box spending, possibly combined with a cap on each element of the green box.

Given the criteria spelled out above, we must ask: Do major farm policies fit within the green box? For example, does the $8.7 billion bailout of U.S. farmers in 1999 fit into the green box? The majority of policy analysts are silent on this issue. I would argue that if this program significantly distorts international trade, then it does not fit the green box category. It is my opinion that it is essentially impossible to carry out decoupled farm programs. Farmers use government payments in production decisions. These payments essentially increase the price of the commodities farmers produce (our surveys show that a dollar transfer from the government translated into a 75-cent increase in the price of the commodity produced). As a result, production is influenced by government transfers, and therefore trade is distorted as a result.

Multinationals and Trade Options

A significant volume of international trade is now conducted by multinationals, whereby firms not only trade a given product but are involved in producing the commodity in many countries around the world. This fact has important implications for freeing up international agricultural trade. Consider, for the moment, the case discussed above in which the United States brought charges against Canada under U.S. countervail and dumping laws. Perhaps a reason why the United States ruled in favor of Canada was because of lobbying by multinationals to keep the border open, given that multinationals in the United States would be hurt if the ruling went in favor of U.S. beef producers. The majority of beef cattle fed in Canada are fed in Alberta. A major packing plant in Brooks, Alberta is owned by Iowa Beef Packers Incorporated (IBP). In addition, a world-class beef-packing plant in High River, Alberta is owned by Cargill, Incorporated under the name of *Excel.* Clearly, closing the borders to Canadian beef exports would have a significant negative impact on the profit picture for these multinationals.

Multinationals continue to influence U.S. sugar policy, which continues to be in the news. The key component of sugar policy is the use of import quotas which restrict the importation of refined and raw sugar into the U.S. market. Support for this program varies by producer group (Schmitz and Moss, 1999). For example, it appears that the U.S. Sugar Corporation (a major sugar producer in Florida) supports more restrictive import quotas than does Flo-Sun (which produces in Florida and in the Dominican Republic). Flo-Sun ships sugar from the Dominican Republic into the U.S. under preferential quota treatment, receiving the internal U.S. sugar price for exports. Therefore, they attempt to maximize returns jointly from domestic production and from production in the Dominican Republic. To do this, they want a certain volume of imports to enter the U.S. duty-free. The quota levels which Flo-Sun supports are above those that the U.S. Sugar Corporation supports, largely because the latter produces sugar only in the United States.

Vertical Markets and Trade

Many sectors are now becoming vertically integrated either through direct contracts between processors and growers, or by direct ownership of all stages from production to marketing. Perhaps this increasing degree of integration favors lobbying activities for free trade. On the other hand, where vertical integration is not present, key players in the marketing chain with both economic and political clout can block trade reform. For example, in the production and marketing of cotton in Turkey, there is very little vertical coordination. A major cotton textile mill is owned privately and buys the majority of its cotton on the Turkish cotton exchange. When examining cotton policy in Turkey, it is clear that protectionist trade instruments (such as export subsidies, taxes, and import quotas on raw cotton) are in place which maximize returns to the private processing sector (Schmitz *et al.,* 1999). It appears that lobbying efforts could take on a different direction if the degree of vertical coordination were increased in the Turkish cotton sector.

The importance of the structure of vertical markets on trade can be further seen with respect to the U.S. sugar industry. Both Flo-Sun and the U.S. Sugar Corporation can handle additional raw-sugar imports since they have the capacity to refine raw sugar, which is not true for major sugar beet producers nor for sugarcane producers in Louisiana. Therefore the opening up of trade would have a less serious impact on these firms than it would on sugar beet producers and sugarcane producers in Louisiana. The latter does not own any sugarcane refining capacity.

What Must Be Given Up?

In negotiating for freer trade in agriculture, it is not clear what individual countries are willing to give up. Consider Canada for the moment: if supply management is to remain in place, then Canada has very few chips to bargain with, since all of the remaining sectors are not subsidized to any significant extent. On the issue of supply management, there are significant gains from trade if this system were eliminated; however, this would require compensation to producers which would approximate the transfers producers currently receive from consumers. Given the political climate in Canada and the frustrating experience of Western Canadian producers with respect to transfers from the federal government, compensation appears unlikely.

It is clear that there is a great deal to be gained by non-E.U. countries if the European Union gives up subsidies, but the problem remains: unless compensation is actually paid to losers in the move to freer trade then very little will happen in trade negotiations.

In terms of the United States we must consider whether or not it will give up sugar, peanut, tobacco, or dairy programs? Likely not, unless compensation schemes are devised. Would the United States terminate bailout programs? In view of the above, while it is interesting political rhetoric to argue that the world has a great deal to gain from freer trade in agriculture, achieving freer trade in reality is a different matter. A significant question remains: Who wants free trade anyway?

The Theory of Public Choice and Rent Seeking

Policy decisions are clearly influenced by rent seeking. Effective rent seekers are able to convince politicians that they need financial support regardless of the impact of such support on trade and the environment. U.S. farmers were successful in lobbying government to change the 1996 farm program in their favor, particularly when, in 1999, an $8.7 billion bailout was added to farmers' coffers. The U.S. government is once again heavily involved in U.S. agriculture. This involvement should not be surprising given the theory of rent seeking and public choice. Politicians' response to lobbying is largely a function of whether or not they can win votes.

This is clearly demonstrated concerning policy harmonization between Canada and the United States (see above). For example, wheat farmers on the Canadian prairies, unlike those in the United States, have recently been unable to lobby the federal government effectively for support in view of extremely low wheat prices. This was not true for the early 1990s when the level of support for Canadian prairie farmers was at least as high as support levels for American farmers. Why is support now not forthcoming? The answer seems clear: supporting prairie farmers generates very few votes.

The present Canadian federal government is a Liberal government, while the Alberta provincial government is Conservative. Saskatchewan and Manitoba are governed by the New Democratic Party. There are few elected Liberals from the West in the current federal government. (Remember that when the federal government provided high support levels in the late 1980s and early 1990s, a Progressive Conservative government was in place in Ottawa and in Saskatchewan.) Unless the Liberal government felt that it could obtain additional votes in future elections through farm support, it likely will not subsidize western farmers. The Liberal government clearly supports supply management, whose primary activities are located in eastern Canada: Quebec and Ontario specifically (Schmitz and Schmitz, 1994; Schmitz, 1995). There are also those who argue that the Ottawa civil servants who advise the federal Minister of Agriculture, including those in Agriculture and Agri-Food Canada, are not in favor of providing significant transfers to Western Canada. Both arguments combined—the political and the economic—suggest why Western Canada is not likely to obtain significant transfers from the federal government at anywhere close to U.S. subsidy levels.

Conclusions

In order to make future progress towards freer trade in agriculture, policy harmonization among countries has to be dealt with. The NAFTA and CUSTA agreements should be enforced. In addition, analysis is badly needed on the impact of the Free Trade Area of the Americas accord on North American agriculture. Freeing up trade among the countries comprising this block could have significant impact on U.S. agriculture. However, given the political climate and the mood which seems to be moving nations towards protectionism, actual compensation will likely need to be paid to those who stand to lose from free trade before they will join the bandwagon.

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