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CAP AND AGRICULTURAL NEGOCIATIONS IN THE DOHA ROUND: The issue of domestic support

The Uruguay Round Agreement on Agriculture (URAA) marked the end of an era in which agricultural policies could be elaborated independently of international rules. It defined a framework, which is again used in the Doha Round, with distinct commitments on the 3 issues of export competition, market access and domestic support. This framework explicitly acknowledges that domestic policies may have distorting effects on trade and, as such, may be submitted to disciplines in the context of multilateral negotiations on trade. This paper more specifically deals with the matter of domestic support in the Doha Round: the development of negotiations on this topic from the initiation of the round to the present day; the potential impact for the European Union (EU) of the commitments that would be undertaken regarding domestic support; a critical analysis of the discussions on this issue.

Domestic Support in the Doha round: what is the current position?[1]

The URAA (1994) classifies domestic support policies in three colour categories commonly called boxes: the green box contains payments that are authorised because they have very few or no distorting effects on trade; the blue box also contains payments that are authorised because they are granted within the framework of capped production; last, the amber box contains measures subjected to reductions because they have significant distorting effects on trade.

The Doha Ministerial Declaration of November 14th 2001, which launched the eponymous round, contains a commitment to substantial reductions in trade-distorting domestic support. The Geneva framework-agreement (FA) of summer 2004 gives details on how to calculate the so-called trade-distorting domestic support, though without assessing reductions. During the summer of 2004, it was agreed that the assessment had to be discussed further for agreement on the terms, at the Ministerial Conference of Hong-Kong in December 2005.

The Geneva framework-agreement of summer 2004: Definition of a blueprint

The Geneva framework contains a commitment to reduce the overall level of trade-distorting support (OTDS) according to a tiered formula. The reduction becomes greater as the OTDS increases. The OTDS is calculated as the sum of the amber box supports (to be more precise, the total aggregate measurement of support, or AMS), of the blue box and the *de minimis* levels (graph 1).[2] The framework-agreement also includes a commitment to reduce the agricultural sector AMS and put an upper cap on AMS by product. It acknowledges the blue box role in promoting agricultural reforms, and therefore suggests extending its content: henceforth, direct payments not requiring any production when they are based on fixed and invariable arable lands, yields or animals, or if they are granted for at most 85% of a fixed and invariable base level of production, would be included. It proposes to cap the blue box support to 5% of the benchmark production value of a reference period. Last, it includes a (very vague) commitment that the green box criteria should be re-examined and clarified. However, the agreement specifies that the fundamental concepts, the principles and the effective nature of the green box should be preserved.

The October 2005 proposals of the Members States: in line with their own interests

Table 1 shows some of the major actors' proposals (EU, United States, and G-20) on modalities (regarding domestic support), on the eve of the Hong-Kong conference (Brink, 2006). We note without surprise that the USA is ambitious when it is not concerned and/or when the proposal places constraints on other developed countries (and therefore on the percentage of the OTDS reduction of the upper tier, which in particular applies to the EU). It is more cautious when it is hindered (for instance, on the reduction in the *de minimis* support, or the benchmark choice selected to fix the ceiling of the AMS per product). No one will be surprised to learn that this behaviour is the rule, the EU by no means an exception. For example, the EU proposes a large reduction

[1] We only consider here the modalities applicable to developed countries without mentioning the most favourable treatments granted to developing countries. Likewise, the question of cotton, which benefits from a specific treatment following the results of the cotton panel, is not raised.

[2] As regards the URAA *de minimis* rules, the following are exempt from reduction commitments: the distorting domestic support per product less than 5% of the production value of the product, and the distorting domestic support other than per product not exceeding 5% of the value of the total agricultural production.

(80%) in the *de minimis* support (the EU does not use this provision very much and can propose such a reduction without any difficulty). On the other hand, it wishes to maintain the green box outlines unchanged so that the single payments from the 2003 CAP reform can be classified in that green box. As for blue box, the EU favours the maintenance of a ceiling up to 5% of the production value and wants there to be no ceiling by product in the blue box, a provision that could become restrictive in some sectors where partial coupling is maintained; it proposes to limit the opportunity to compensate price cuts via blue box measures, a mechanism which explicitly targets the contra-cyclical payments to the United States since 2002.

From December 2005 to the present day: in search of an unobtainable compromise?

The Hong-Kong conference did not assess commitments. The ministerial declaration of December 18th 2005 limits itself to reusing the framework-agreement terms concluded in Geneva some 16 months earlier. However, as an annex of this declaration, a report is enclosed, presented under the responsibility of the President of the extraordinary session of the agricultural committee of November 11th 2005, which aims at sorting out the differences of opinion via the definition of intervals within which the final commitments would be found. In spite of intense discussions in various configurations, there has not been any agreement yet as we write this paper (June 2007) on the matter of domestic support or on many others. We shall sum up the domestic support situation in this way:

1. Reduction of the OTDS according to a 3-tier formula

Tier	OTDS (billion $ US)	Reduction in %
1	0-10	31-70
2	10-60	53-75
3	60 or more	70-80

2. Reduction of the AMS according to a 3-tier formula

Tier	Reduction in %
1	37-60
2	60
3	70

3. AMS upper cap by product but disagreement on the benchmark period to be used to work out the ceiling: agreement of a majority of countries on 1995-2000 (URAA application years), with the United States against this choice and favouring a 3 year period from 1999 to 2001.

4. Reduction of the *de minimis* supports by product and others than by product, in a bracket ranging from a minimum of 50% to a maximum of 80%.

5. Blue box upper cap at 2.5% of production value, the question of phasing this upper cap not being resolved as well as that of the blue box per product.

Several uncertainties remain, in particular regarding the OTDS reduction. A 70% reduction may require a substantially greater effort than a 53% cut. But this is the bracket, which is proposed to countries having an OTDS of between US $10 and 60 billion, a very wide bracket. As well as this example, many differences remain between countries (an observation which also applies to other agricultural and non-agricultural matters in the negotiation), too numerous according to many people to hope for an agreement in a short time. However, we must emphasise the efforts of C. Falconer, the present president of the agricultural committee of the WTO, to find solutions to sticking points: for example, the various options which could help resolve the matter of the benchmark choice used to determine the blue box ceiling (measure aiming to remove the American objection to that point) or the possibility for a country which has placed a high percentage of its domestic support in the "old definition" blue box not to be constrained by the ceiling at 2.5% of production value (measure aiming to win the adhesion of Norway on that point). Seen more negatively, the discussion essentially involves the search for an acceptable compromise via a softening of common rules on the blocking points of each country, to the detriment of the initial objective (see the 2001 Doha ministerial declaration) and of an analysis of the potential impact on the exchanges of various proposals.

Can commitments on domestic support place constraints on the EU?

The last EU notification to the WTO concerned 2001/2002. The EU-15 domestic support was then divided into 39.3 billion euros in the amber box (AMS), 863 billion euros in the *de minimis* support, 23.7 billion euros in the blue box and 20.6 billion euros in the green box. The 39.3 billion euros AMS should be compared to the authorized ceiling of 67.2 billion euros, a comparison which shows that in 2001/02, the EU-15 had at its disposal a 27.9 billion euros' worth of room for manoeuvre, that is to say 41.5%.

The constraint of AMS reduction should not be restricting

In order to assess the percentage of the AMS reduction that the EU is in a position to accept within the framework of the Doha round, a date on which this reduction must be respected should first be set. We have selected the final year of the present financial perspectives, that is to say 2013. We then have to project the AMS to that year. To this end, we proceed in three stages, examining (i) the impact on the EU-15 AMS of the reforms implemented since 2001/02, (ii) the evolution of the AMS in both sectors in the process of reforms (fruit and vegetables, wine), and (iii) the effect of the EU enlargement.

The breakdown of the 2001/02 AMS by production (table 2) shows that the distorting support is high in the sectors that had not been yet reformed at that time but have since been reformed: the milk reform (2003), the hops, tobacco, olive oil and cotton reform (2004), and the sugar reform (2005).
By only considering price effects, we calculate that the EU-15 AMS on the above-mentioned products would drop by 9.3 billion euros, an AMS gain that would be spread between products as shown on table 2. The cereal AMS would only

drop very slightly, by 190 million euros. The beef AMS, very high in 2001/02 (9.7 billion euros) would show a drop of 6 billion euros. Since July 1st 2002, the intervention has been replaced by aid to private storage, aiming to give a safety net at a price of 2220 euros per ton, that is to say a far lower support-price than the intervention price that prevailed in 2001/02.

The 2001/02 AMS for fruit and vegetables is particularly high: 8.4 billion euros shared out in 4.6 billion euros for fruit (2.1 billion euros of which just for apples), 2.8 billion euros for vegetables (1.9 billion euros of which for tomatoes) and 0.9 billion euros for processed fruit and vegetables. The AMS reduction of 2.2 billion euros in fruit and vegetables shown in table 2 results from the cut in entry prices following an agricultural agreement of the Doha cycle in accordance with the EU proposal at the WTO in October 2005. The cancellation of the AMS for wine results from the change in its own calculation method. The same change applied to beef would allow the EU-15 to almost totally cancel the AMS for this product, and thus show an additional AMS gain of 3.7 billion euros.[3]

On the basis only of the reforms already done and without revising the method for calculation of the beef AMS, the EU-15 would be in a position to accept an AMS reduction of more than 64%. By including the changes the wine and in the fruit and vegetables sectors, and assuming a calculation of the AMS for beef on the basis of expenditures, the AMS reduction that the EU-15 would be in a position to accept would be around 75%. The enlargement of the EU to new member states would slightly reduce this room for manoeuvre by a few percentage points.

In conclusion, the EU would be in a position to accept, without difficulty, the AMS cut of 70% that would be imposed on it in accordance with the announcement of the President of the Agriculture Committee on April 30th 2007. Admittedly, the analysis developed above does not take into account the volume effects. Any rise in produced quantities mechanically increases the component "market price support" of the AMS. On this point, we only note that the decoupling of the support policy of agricultural incomes in the EU should have a negative impact on produced quantities. Conversely, the development of biofuel will have the opposite impact, that is to say a positive one, at least as regards large-scale crops.

The other aspects relating to domestic support should not be more penalizing for the EU.

The EU-15 blue box of 2001/02 represented 9.6% of the value of agricultural production. The replacement of a large part of aid per hectare and/or head by a single farm payment considerably cut the blue box amounts from 2006 onwards (by nearly 19 billion euros for the EU-15, according to our assessments).Therefore, the Eu-15 blue box would be slightly lower than 5 billion euros, that is to say 1.9% of the value of 2001/02 agricultural production. Enlargement would cut this percentage even more, since it results in an increase in the denominator with an almost unchanged numerator (at least as from 2013, when the additional payments that the new member States may grant to their farmers and which are included in the blue box should be null). Another factor should increase the room for manoeuvre regarding the blue box ceiling: the very probable cut in the payments that remained coupled, following the 2008 CAP health check (at the very least in the cereal sector; very likely, too, in some countries at least, in the herbivore sector). The upward trend in large crop prices in particular generated by biofuels will work in the opposite direction (cut in the EU room for manoeuvre by an increase in the value of EU agricultural production).

The EU should not be constrained by the blue box ceiling at 2.5% of production value. She should not be anymore penalized either by the 80% drop in the *de minimis* supports (a decrease percentage that will limit the *de minimis* support by product at 1% of the value of this product and the *de minimis* support other by product at 1% of total production value). Indeed, the EU has only rarely used this measure in the past.

In all, according to current proposals, the EU should not be capped by the OTDS reduction.

Clarifying the domestic support measurement

The Doha round was not used to clarify the domestic support measurement, more precisely the measurement of domestic support having distorting effects on trade.

In the great majority, the surveys aiming at quantifying the beneficial effects of liberalization of the agricultural markets suggest that the gain would essentially be due to an increased access to the market. The gains linked to a fall in domestic and export policies would be far more modest, less than 10% of the gains generated by the withdrawal of customs duties, according to Anderson et al. (2006). These figures are contested by the European Commission. This is easily understandable, because they justify concentrating effort on access to the market, the EU's Sword of Damocles, and allow a much greater tolerance as regards domestic support, which is convenient for the United States. Beyond the protest,[4] three factors explain the prime importance of market access (Anderson et al., 2006):

- A major part of the domestic support is always guaranteed by protectionist measures at entry which result in an increase in domestic prices;
- These import measures modify domestic prices at supply and demand (they have distorting effects on both sides of supply and demand), while direct payments do not play any part in demand prices;
- Import barriers vary more between countries and between goods, and thus generate higher costs than domestic support measures.

It is because a restrictive cut in entry protections will mechanically entail a reduction in the *market price support*

[3] The change to the method for calculating the AMS for beef would consist in calculating it on the basis of the expenditures relating to private storage, which should be very slight since the EU would be a growing beef importer in 2013.

[4] We note that the European Community bases a part of its protest on an US official survey (US Department of Agriculture) by presenting the effects not on aid but on world rates: both indicators are important; naturally their meaning and interpretation differ.

component of domestic support, and because direct payments are widely decoupled, that gains in social aid are more to be expected from a cut in protections than from a drop in domestic support. The Doha cycle must tackle trade policies as a priority, more specifically entry measures taking into account the modesty of direct export incentives, subject to a decoupling of income support policy (Guyomard, 2005). With this in mind, we provide a reminder that direct payments based on the land factor are clearly less distorting than variable input payments, a support to market prices or subsidies coupled to production. The CAP 2003 single farm payments (SFP) are based on the land factor (via the activation constraint). Their trade distorting effects are "minimized". If there is later a reform in the SFP, it will be for specific reasons internal to the EU (Guyomard et al. 2007).

We shall recommend clarification of the domestic support measurement according to the following principles. First, by considering only two types of measures: the ones which would be permitted, and the ones which would be subject to reduction (new green and amber boxes). The principle of a green box with several objectives, and defining, for each objective, the criteria that instruments must respect to reach that objective, must be kept. Nevertheless, on the one hand it is necessary to soften the measurement definition criteria when these focus on market failures, so that it is possible to pay for positive externalities and public goods and not only to compensate for additional costs or profit losses as is the case with the URAA green box), and on the other hand and simultaneously to limit certain flexibilities when instruments do not explicitly focus on market failures. We shall make no secret of the difficulty of this necessary clarification for the green box. In order to make sure that distorting effects are minimized and/or that measurements do not excessively remunerate positive externalities and public goods, we may consider capping the expenditures of each green box measurement. This measurement should only be temporary, pending a stabilized definition for the new green box. As for the new amber box, instead of the reasoning based on the AMS for the whole farm sector (however with a ceiling of the product AMS) we prefer reduction commitments, product by product, and for each product, measurement by measurement.

Lastly, should we not raise the question about the treatment of policies promoting biofuels? Is community policy on the matter not a policy coupled to certain domestic productions, i.e. rape, wheat, and sugar-beet? In the same way, in the United States, are policies not coupled to local maize (to soybean to a lesser extent), and in Brazil to local sugar cane? The environmental point may certainly be put forward to justify these policies, but should we not make sure that the measures, be they incentive or compulsory, only correspond to the remuneration of generated positive external effects, particularly in terms of greenhouse gas reductions? Furthermore, we should also count, on the negative side, the opposite impacts, which thus could be generated (re-conversion of set-aside lands, deforestation, and excessive consumption practices of potentially polluting chemical products, water, and so on.). Because although it is clear that biofuels have a positive impact on large crop producers' incomes (via the rise in these production prices), their impact on cattle-breeders' incomes is not determined and the consequences for consumers are negative.

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Graph 1: Breakdown of the domestic support /calculation of the OTDS

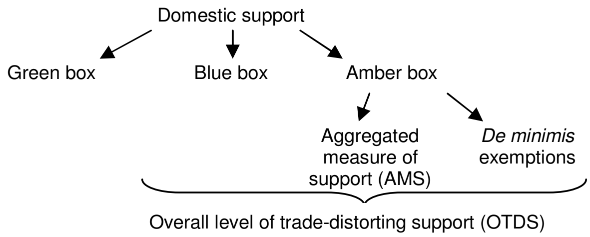

Table 1: Proposals by the EU, the United States and the G-20 on the matter of domestic support (Autumn 2005)

	EU	United States	G-20
% reduction in the OTDS	70/60/50	75/53/31	80/75/70
for the EU	70	75	80
for the United States	60	53	75
% reduction in the AMS	70/60/50	83/60/37	80/70/60
For the EU	70	83	80
for the United States	60	60	70
AMS ceiling by product: benchmark	1995-2000	1999-2001	1995-2000
% drop in the *de minimis* support	80	50	// to the drop in OTDS
Ceiling of the blue box (in % of value production)	5%	2,5%	2,5%
Increased disciplines at the level of the blue box	yes	no	yes
Green box	unchanged	clarified	clarified

Source: Proposals by the EU, the United States and the G-20 at Autumn 2005 at CMO; Brink, 2006.

Table 2: Assessment of the impact of policy reforms after 2001/02 on the UE-15 AMS: determined reforms and potential/foreseeable evolutions

	AMS2001/02	Variation in AMS	« final » AMS
Decided reforms			
Milk	5,8	-1,9	4,0
Olive oil	2,7	-2,7	0,0
Hops tobacco cotton	2,0	-1,9	0,2
Sugar	5,7	-2,8	2,9
	16,2	-9,3	7,1
Cereals	4,1	-0,2	3,9
Beef	9,7	-6,0	3,7
	13,8	-6,2	7,6
Total I	*30,0*	*-15,5*	*14,7*
Reforms in progress			
Fruit and vegetables	8,4	-2,2	6,1
Wine	0,9	-0,9	0,0
	9,3	-3,1	6,1
Total II	*39,3*	*-18,6*	*20,8*
Additional beef		-3,7	
Total III	*39,3*	*-22,3*	*17,1*
Decided reforms I		-15,5	24,0 (35,7%)
+ potential evolutions II		-18,6	20,8 (30,1%)
+ additional beef III		-22,3	17,1 (25,4%)

In billion euros; between brackets, report of the "final AMS" with the AMS permitted ceiling following the URAA (67.2 billion euros).

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