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Trade Liberalization in World Farm Markets

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The playing field in world agricultural trade is uneven. Some countries subsidize their imports; others subsidize their exports. Some tax imports; others tax exports. Most nations try to help their farmers through domestic farm programs. All these influences converge to distort the price signals that would otherwise govern supply and demand in a freer trade environment. The resulting hodgepodge has disadvantaged many producers in the United States and other countries, even though their farm products are among the least expensive to produce. We highlight the extent of such government intervention in agricultural products for 12 countries (including the United States) and the European Community.

This report gives a perspective on the issues and conditions that the United States and the other 91 members of the General Agreement on Tariffs and Trade (GATT) confront in spring 1987 as they negotiate a reduction in intervention in international markets. Agricultural trade negotiations are part of the broader negotiations of the eighth round of multilateral trade negotiations under GATT. Broad objectives and principles for these negotiations, called the Uruguay Round, were set forth in a Ministerial declaration signed in Uruguay in September 1986.

The U.S. farm sector is in the midst of a restructuring. Changing world markets and the U.S. linkage to those markets complicate that restructuring. The United States has responded to this situation by revising its farm commodity programs to enhance the competitiveness of U.S. farm exports and by working with other countries to lower the value of the dollar. While such policy adjustments help in the short term, a necessary prerequisite for a long-term competitive environment for agricultural trade is to improve the operation of the world market through forums like multilateral trade negotiations. Protectionist, inward-looking policies will lead only to a more erratic, less stable world market environment.

The United States and other key players in world markets have ambitious goals for agriculture in the Uruguay Round, including broadly reducing trade barriers imposed by many developed and developing countries. A trade environment more responsive to market conditions is needed to expand the market for U.S. farm products.

If the talks are successful, efficient agricultural producers will benefit: they will gain better access to many agricultural export markets now virtually closed and face less unfair competition from inefficient suppliers with subsidized exports. Trade liberalization will also help taxpayers by reducing government costs for farm programs and will foster price stability in the world market.

However, a more liberal trade environment would cost some producers. U.S. producers of highly protected products, such as dairy products, sugar, peanuts, and tobacco, would have to adjust to a competitive market that would likely mean lower market prices at the outset compared with current supported price levels.

Trade barriers, price and income support programs, and other domestic agricultural policies of trading countries contribute significantly to current problems in the agricultural trade environment. Many trade barriers ensure the effectiveness of each country's domestic policies, such as achieving food self-sufficiency, maintaining the family farm as a viable institution, or shielding farmers from price and income instability. Such policies buffer agricultural producers in many countries from world price movements and international competition and discourage supply and demand adjustments. World supply consequently has grown faster than demand, pushing world prices down. As agricultural market conditions worsen, many countries depend more on agricultural policies to protect their farmers. These programs are also costly to taxpayers and, often, to food consumers.

Shrinking foreign markets, falling international commodity prices, and growing commodity surpluses in exporting countries have greatly strained agricultural sectors in several countries, including the United States. Competition among agricultural exporters has intensified. Disputes over the use of export subsidies, export credits, and import restrictions abound, and the potential for more intense trade confrontations seems always to be simmering. This widening potential for confrontation is currently threatening to further undermine the operation of world commodity markets.

'80's PROTECTIONISM ROOTED IN '70's EXPANSION

In the early 1980's, growth in foreign production rebounded because of expanded investment in the agricultural sectors of many countries. In addition, a sharp drop in consumption growth accompanied a worldwide slowdown in economic growth. As agricultural trade grew more slowly and excess capacity in global agriculture grew more rapidly, nations tried to protect their farmers and, in some cases, their market shares by more intense government interference in the market process. But, the magnitude and types of government intervention are not all new to the 1980's.

Increased insulation of agricultural markets from the world market---the breaking of the link between world price movements and domestic prices---was already underway in the 1970's. During that decade, protection under the EC's Common Agricultural Policy was extended to the United Kingdom, Ireland, and Denmark, further insulating the important European market from world market conditions. In addition, the centrally planned countries, particularly major state traders like the Soviet Union, whose domestic markets are thought to be highly insulated from the world market, were becoming larger players in selected world commodity markets. However, in the upbeat market of the 1970's, these increased distortions to international markets went largely unnoticed.

Agricultural policies that were started or strengthened in many leading countries in the 1970's are putting additional pressure on falling commodity prices and declining world trade levels in the 1980's. These policies, and the trade practices employed to defend them, bring an added level of uncertainty and risk to a country's dependence on trade. Increasing confrontation over the use of protective agricultural policies, and the associated effect on market stability, could generate a move away from trade dependence equal to the move toward trade dependence during much of the postwar period.

GOVERNMENT SUPPORT TO PRODUCERS DIFFERS BY COMMODITY AND COUNTRY

The extent and magnitude of government intervention in agriculture are difficult to assess, particularly when making comparisons across countries. Intervention stems from many policies that affect not only direct payments and budget outlays but producers and consumers as well (see box).

USDA's Economic Research Service (ERS) recently measured government intervention using the notion of producer subsidy equivalents for the 1982-84 period. The producer subsidy equivalent (PSE) is an estimate of the subsidy needed to compensate producers for the income likely to be lost if all government support programs were eliminated (fig. 1). For example, an ERS estimate of 58 percent for the Canadian dairy sector means that the government's contribution to Canadian dairy producers' revenue is equivalent to 58 percent of the value of Canadian dairy production during 1982-84. On the other hand,

MEASURING GOVERNMENT ASSISTANCE—WHO PAYS?

Budget outlays are incomplete measures of government support to agricultural sectors. Some policy instruments, such as import quotas or variable levies, permit producers to receive prices higher than world market prices. The cost of these policies, however, is borne by consumers who must pay higher than world market prices. Yet, this implicit tax on consumers and the corresponding support received by producers do not appear in the government budget. That, in fact, is one appeal of these types of policies: no direct taxpayer costs are associated with them.

Whether government support to producers comes from food consumers (no cost subsidies) or taxpayers differs markedly among countries and, within a country, among commodities (fig. 2). Border measures affect consumer and producer prices. Border measures consequently are typically viewed as hidden subsidies to producers.

Most of the cost of public assistance to agricultural producers in the EC and Japan is borne by consumers through higher food prices. Most of the budget contribution in the EC represents export refund payments necessary to move high-priced EC commodities onto world markets. Large Japanese budget outlays are used to reduce consumer rice costs. Deficiency payments are also paid to Japanese dairy and oilseed producers.

Canada and the United States approach producer assistance in similar ways. Grain consumers in both countries bear virtually none of the cost of farm income support or stabilization policies, and the largest portion of support to beef producers also comes from taxpayer contributions. U.S. and Canadian dairy consumers, however, bear most of the support to dairy producers. Australian consumers bear the high cost of dairy pricing policies but none of the cost of supporting beef producers. Consumers in Australia paid nearly 60 percent of the cost to support wheat producers.

India, for example, subsidizes its wheat consumers an equivalent of 15 percent of the value of total wheat consumption.

A key point in this comparison of government assistance levels is that there are no free traders in the world. All governments intervene in their agricultural sectors in some fashion. What varies is the extent of the intervention, and in that context, the playing field for world agricultural trade is far from level.

Producer assistance levels were compared in several countries. For simplicity and to establish a rough basis for making cross-commodity and cross-country comparisons, the levels of assistance and taxation are presented in the following ranges:

- o *Low.* 0–24 percent
- o *Moderate.* 25–49 percent
- o *High.* 50 percent or more.

Figure 1
Ranking of Producer Subsidy Equivalent Levels

	Ranking	United States	Australia	Canada	New Zealand	European Community	Japan	Taiwan	South Korea	India	Argentina	Nigeria	Mexico	Brazil
Producer tax	Low									Cotton(MS)* Peanut meal Rapeseed meal Rice Soybeans Soymeal	Corn* Sorghum* Soybeans*	Cotton Rice		Beef* Corn Soybeans*
	Moderate						Citrus			Cotton(LS)* Wheat	Wheat*			
	High											Cocoa* Sugar		
Producer subsidy	Low	Barley* Beef Pork Poultry meat* Soybeans*	Barley* Beef* Cane sugar* Cotton* Mfd. milk* Pork* Poultry meat* Rice* Sheep meat* Wheat* Wool*	Barley* Beef Corn Flaxseed* Oats* Pork* Poultry meat Rapeseed* Rye* Soybeans Wheat*	Barley* Beef* Fluid milk Mfd. milk* Wheat Wool*	Barley* Common wheat* Corn Pork*		Corn Pork* Soybeans Sugar*	Poultry meat	Peanuts* Rapeseed		Corn	Cotton*	Mfd. milk Poultry meat*
	Moderate	Corn* Cotton* Dairy* Rice* Sorghum* Wheat*	Fluid milk	Sugar	Sheep meat*	Dairy* Durum wheat* Poultry meat* Rapeseed Rice Sheep meat Soybeans Sugar*	Poultry meat	Beef Dairy Poultry meat Rice* Tobacco	Pork	Peanut oil Rape oil Soy oil		Wheat	Sorghum Soybeans Wheat	Cotton* Rice
	High	Sugar		Dairy*		Beef*	Barley Beef Fluid milk Mfd. milk Pork Rice Soybeans Sugar Wheat	Sorghum Wheat	Barley Beef Corn Fluid milk Rice Soybeans Wheat				Corn	Wheat
	Weighted average PSE	22	9	22	23	33	72	18	64	8	-22	-9	40	7

* = Net exporter during 1982-84.
Mfd. = Manufactured.
MS = Medium-staple cotton.
LS = Long-staple cotton.

Australia provides the least assistance to its agricultural sector, with its PSE generally at the bottom end of the low range (9 percent). The export-oriented countries of Canada, the United States, and New Zealand fall in the top end of the low range in terms of producer assistance, with PSE's during the 1982-84 study period in the 22-23 percent range.

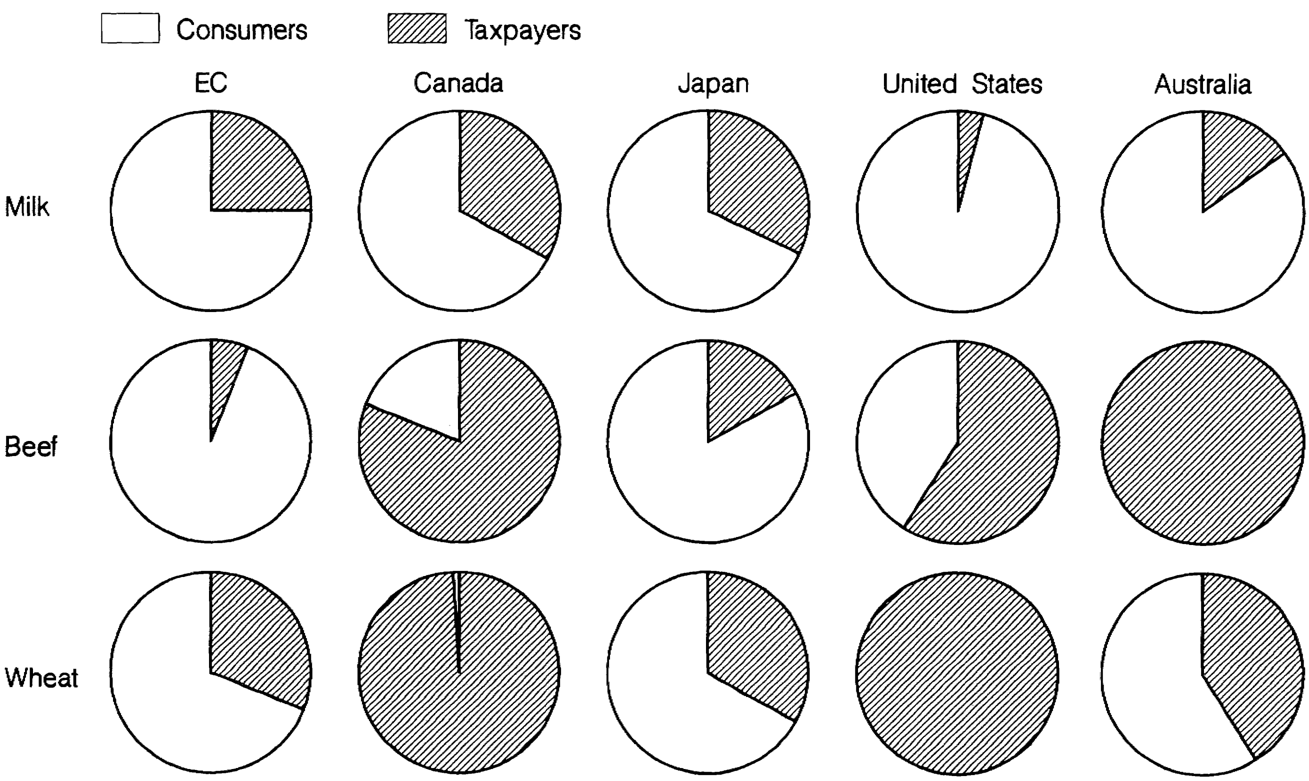
U.S. assistance to producers of soybeans, pork, poultry, and beef is low, while that to producers of grains, dairy products, sugar, and cotton is moderate to high. U.S. producer assistance is usually in the form of direct cash payments or direct price supports, resulting in government inventory operations through USDA's Commodity Credit Corporation. U.S. protection for beef, dairy products, and sugar takes the form of import restrictions.

Assistance to farmers in the European Community (EC) is mostly in the moderate range. Nearly all EC countries apply border measures, usually a variable import levy, or policies linked to border measures, such as public intervention buying at guaranteed producer prices that are often higher than world market prices. Soybeans is one of the few major commodities exempt from import restrictions; EC soybean producers receive deficiency payments, however.

Japan maintains the highest levels of government assistance to producers. Japan also relies on border measures to provide the major component of producer assistance. For example, Japanese beef imports are severely restricted by quotas, tariffs, and surcharges that result in domestic beef prices more than double world prices.

Figure 2

Who Pays for Producer Support?[1]



1/ 1982-84 average.

Some of the newly industrialized countries are providing more government assistance to agricultural producers. South Korea and, to a lesser extent, Taiwan--both growth markets for U.S. farm products in the 1970's--use strong government intervention in several agricultural markets to protect producers. For example, South Korea supports producer prices for livestock products with strict border restrictions enforced by a state trading agency for beef and complete bans on pork and chicken imports.

Agricultural and economic policies in developing countries sometimes make it possible to transfer income away from producers, usually to generate government revenue, as with Argentina and Nigeria. However, some countries, like Mexico, assist producers to increase self-sufficiency in staple foods and limit foreign exchange expenditures.

Heavy subsidies to producers often imply heavy taxes to consumers because policies that raise producer prices (such as tariffs, quotas, and domestic price supports) also raise consumer prices. Border measures affect prices to consumers as well as producers and are typically viewed as a hidden subsidy to producers.

Consumer taxes among developed countries are highest in the EC and Japan and lowest in Australia, Canada, and New Zealand. In the EC and Japan, consumers bear most of the cost of producer assistance through higher food prices. In Canada and the United States, most support to grain and beef producers comes from taxpayers. U.S. and Canadian dairy consumers, however, bear most of the cost of producer support. Australian consumers bear the high cost of dairy pricing policies but none of the cost of supporting beef producers.

Consumer subsidies, on the other hand, are generally highest in less developed countries. For example, Argentina implicitly subsidizes its consumers through policies that make domestic prices lower than export prices.

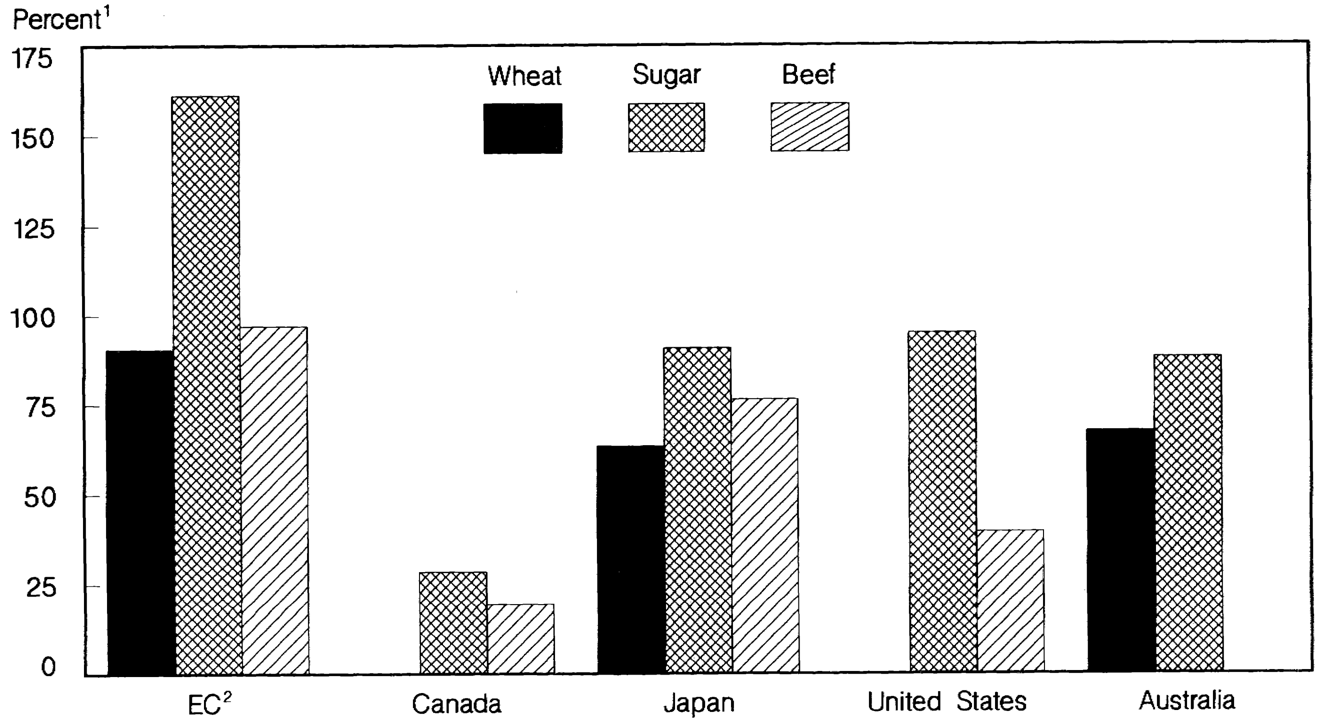
NEGOTIATIONS MUST REACH BEYOND BORDER MEASURES

The diversity in forms of government assistance and the often relatively minor role of border measures (tariffs, quotas, levies, and so forth) in some countries greatly complicate efforts to arrive at mutually acceptable ways of liberalizing agricultural trade. For example, the European Community and Japan make heavy use of border measures as a basis for producer supports. However, the United States generally does not rely on border measures as a major source of assistance to its agricultural producers, except to producers of beef, dairy products, and sugar. Figure 3 highlights the varying importance of border measures among countries and among commodities within a country.

The relatively unimportant role of border measures in many countries means that trade liberalization based solely on modifications to countries' border (trade) policies will do little to make the playing field more level. The Uruguay Round, for the first time, will make domestic policies a legitimate subject of negotiation. These negotiations present an opportunity to better align not only border measures but domestic agricultural policies and world market conditions and, more importantly, to create conditions for future expansion of world agricultural trade.

Figure 3

Importance of Border Measures Varies by Country and Commodity



1/ Border measures as a percentage of producer support.
2/ For sugar, total PSE is smaller than part attributed to trade measures due to co-responsibility levies.

FOR ADDITIONAL INFORMATION...

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Also see: *Government Intervention in Agriculture: Measurement, Evaluation, and Implications for Trade Negotiations.* FAER-229. U.S. Department of Agriculture, Economic Research Service, Apr. 1987.

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